

MEGATRENDS

ANNUAL REPORT 2016



SUSTAINABILITY

GLOBALISATION

ECONOMY 4.0

TECHNOLOGICAL
PROGRESS

DEUTSCHE HYPO AT A GLANCE

in € millions	01.01.- 31.12.2016	01.01.- 31.12.2015	Change (in %)
New business figures			
Commercial real estate finance business *)	4,540.7	4,075.2	11.4
Domestic finance	2,832.1	2,449.2	15.6
Foreign finance	1,708.6	1,626.0	5.1
Funding volume	3,938.2	3,571.5	10.3
Mortgage Pfandbriefe	1,800.0	1,601.5	12.4
Unsecured	2,138.2	1,970.0	8.5

in € millions	31.12.2016	31.12.2015	Change (in %)
Portfolio figures			
Commercial real estate finance business	11,977.0	11,953.6	0.2
Domestic finance	7,156.0	7,380.3	-3.0
Foreign finance	4,821.0	4,573.2	5.4
Loans to local authorities	4,815.5	5,588.6	-13.8
Securities	6,720.3	7,038.0	-4.5
Funding capital	23,493.4	25,243.7	-6.9
Mortgage Pfandbriefe	8,286.9	8,486.5	-2.4
Public Pfandbriefe	5,378.5	7,028.5	-23.5
Unsecured	2,740.5	2,606.9	5.1
Other liabilities	7,087.5	7,121.8	-0.5
Equity **)	1,382.6	1,330.6	3.9
Balance sheet total	25,202.6	26,943.7	-6.5

in € millions	01.01.- 31.12.2016	01.01.- 31.12.2015	Change (in %)
Income figures			
Net interest income	202.1	224.5	-10.0
Net commission income	3.7	0.5	>100.0
Administrative expenses ***)	76.4	77.8	-1.8
Risk result	-66.6	-41.3	-61.3
Income from securities and participatory interest	55.7	-29.4	>100.0
Result from normal operations	115.0	70.3	63.6
Extraordinary result	-1.6	-0.1	>-100.0
Interest on investments by silent partners	8.4	8.4	0.0
Profit before taxes and profit and loss transfer agreement	104.9	61.8	69.7

in %	31.12.2016	31.12.2015
Other information		
Cost-income ratio	37.8	35.6

*) In a change to the previous methodology, extensions of existing financing were included when the extension periods were at least one year. Previous-year figures have been adjusted accordingly.

**) including funds for general banking risks, jouissance right capital and subordinated liabilities

***) including write-downs and value adjustments of intangible assets and tangible fixed assets

The annual report of Deutsche Hypo is also available in German. In the event of any discrepancy, the German version shall prevail.

ANNUAL REPORT 2016

WE HAVE A CENTRE OF COMPETENCE:

Benedikt von Abendroth, Carolin Albers, Ingo Albert, Alois Algermissen, Antje Amelsberg, Anne-Kathrin Apel, Elena Argun, Daniela Assing, Jens Assmann, Hans-Hermann Baltz, Angela Bank, Philipp Bank, Nicole Barnert, Sabine Barthauer, Susie Bassett, Isabel Bauke, Jürgen Becksvoort, Michaela Behnsen, Ulrike Behnsen, Andrea Behre, Dana Beitz, Lara Bengsch, Nadja Bengsch, Alica Bergmann, Andreas Bergmeier, Marco Bertram, Olaf Beuleke, Wouter de Bever, Sebastian Biel, Heike Bien, Kathrin Biering, Petra Biering, Carsten Bläck, Markus Block, Ann-Christin Bloß, Martina Blum, Cornelia Bock, Marianne Böx, Stefanie Bojahr, Ines Bornemann, Oliver Boser, Lisa Bosetzky, Jasmin Bothe, Michael Brämer, Kirsten Brandt, Alexander Braun, Jens Breithecker, Brigitte Brenning, Iris Brünau, Marc Brune, Volker Brunner, Jochen Bucek, Carsten Bühring, Holger Busch, Lars Busch, José Luis Calderón Martínez, Anne-Isabelle Carbonnières, Juan Manuel Casas Guillen, Yvonne Coppel-Tamms, Claus-Halvard Cors, Bettina Cramer, Ursula Czech, Sandra Debbrecht, Katrin-Genevieve Deitermann, Ulrich Deppe, Carsten Dickhut, Andrea Dietsch, Frank Dittmann, Beate Droste, Jürgen Eckert, Nicole Edle von Wölfel, Ernst-August Endrulat, Carina Engelbrecht, Tobias Faust, Matthias Feifer, Raimund Ferley, Christian Fischer, Kai Fischer, Arabell Foth, Eric Mark Fowell, Jörg Franz, Michael Frech, Christine Frenzen, Oliver Frerking, Chiquita Sandra Freudel, Andreas Froebus, Björn Fuhr, Britta Gabriel, Christian Gail, Nikola Gaulke, Michael Gehrig, Melanie Geldmacher, Christoph Gennrich, Maria Germann, Annett Gierschner, Larissa Gieselmann, Michael Glatzer, Melanie Glende, Kristoffer Globig, Rüdiger Göricke, Sabine Gößmann, Silvia Golbeck, Claudia Grau, Georg Greive, William Groen, Elke Großer, Detlev Grote, Christian Gudat, Cristina Guilherme, Petra-Ingeborg Haake, Christian Haendel, Lars Haftmann, Ralf Hagendorff, James Hall, Thomas Hansen, Kevin Harmer, Axel Harms, Jan Hartmann, Tina Hartmann, Iris Hauser, Albrecht Heinecke, Stefan Heinitz, Markus Heinzl, Christian Hellwinkel, Birger Helm, Heini Katariina Hemminki, Janina Herrmann, Miriam Herzog, Janos Hielscher, Dr. Peter Hinze, René Hodko, Achim von Hoegen, Anne-Kathrin Hoepfner, Raimo Höpfner, Christoph Hötzel, Nils Hoffmann, Monika Hofschulte, Marcel Holk, Jule Hoppe, Karin Hornbostel, Chris Horswood, Simone Huch, Klaudia Hüskes, Thomas Hundertmark, Dirk Hunger, Tanja Hußmann, Malte Ilginnis, Axel Intemann, Peter Jabs, Anna-Dorothea Jäger, Amely Jessop, Thorsteinn Jonsson, Ute Jürges, Frank Junge, Georg Kaisler, Dirk Kallikat, Christina Kanning, Gudrun Karges, Moafak Kata, Brit Kaufmann, Melanie Kautzner, Cezary Kempisty, Kristina Kirchner, Andreas Kirschner, Til Kittkowske, Jürgen Klebe, Peter Kleinhütten, Lutz Klinkmann, Florian Knaul, Tobias Knoche, Detlef Koch, Dieter Koch, Gerald Kölle, Georg Richard König, Heiko Kollmann, Jörg Kopp, Jutta Carola Kopp, Renate Koppitz, Gabriele Kornweih, Stefanie Kortmann, Anna Carina Kostrzewa, Janina Krapp, Stefan Kriegs, Ulrich Krogmeier, Sarah Krüger, Regina Kubina, Elke Kücken, Frank Kühne, Silke Kues, Marcel Kujawski, Andrea Kuschel, Ralph Kutschki, Eike Oliver Laase, Bernd Lademann, Thomas Lang, Cornelia Lange, Sascha Langeheine, Katrin Langer, Beata Latoszek, Annemarie Leeuwen, Dr. Pia Leipertz,

OUR STAFF

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 Woodgate, Stefanie Wünsch, Martina Wulschläger,
 Olivier Zapf, Sebastian Ziegler, Nicole Zimmermann.

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FOREWORD BY THE CHAIRMAN OF THE SUPERVISORY BOARD

Dear Customers
and Business Partners of Deutsche Hypo,

the banking sector looks back on a challenging year. Apart from regulatory requirements, which continue to increase, and the persistent phase of low interest rates, all financial institutions are facing growing political uncertainty outside of Germany. In particular, the Brexit referendum and the outcome of the elections in the United States have intensified this trend. The pressure that digitalisation is putting on all financial institutions to change represents a major challenge as well.

Despite these challenging conditions, Deutsche Hypo achieved a result from normal operations in the amount of € 115 million in the financial year 2016. This success is due to a number of factors. Firstly, Deutsche Hypo is benefiting from stable economic conditions in its target markets as well as from investor interest in commercial real estate, which continues to be strong. In this favourable environment, the Bank has been extremely successful in developing its acquisition and earning power – both in Germany and abroad. The considerably higher volume of new business and the continuing high level of operating income reflect this achievement. Secondly, Deutsche Hypo's financial year 2016 was shaped by a significant non-recurring effect: the reversal of a large portion of the value adjustments for the Heta exposure.

However, the Bank would have had an exceptional result even without this effect, especially considering it was possible to add a respectable sum in the millions of euros to reserves. Deutsche Hypo is therefore well fortified and has started off the financial year 2017 with plenty of momentum. Even if the Bank is unable to match its exceptional result from 2016, I nonetheless fully expect that 2017 will also be a successful year for Deutsche Hypo. In turn, this will enable the Bank to reinforce its status as a sustainable generator of income in the NORD/LB Group.

Foreword by the Chairman of the Supervisory Board | Message from the Board of Managing Directors | 2016 at a glance | Sustainability | Megatrends



Dear Customers and Business Partners of Deutsche Hypo, by placing your faith in Deutsche Hypo, you are trusting in an experienced real estate finance bank superbly positioned in the market. With its expertise in commercial real estate financing, the Bank looks forward to further assisting you with projects and investments in future as well.

Best regards,

A handwritten signature in black ink, consisting of a stylized 'T' followed by a long horizontal line that curves upwards at the end.

Thomas S. Bürkle
Chairman of the Board of Management of NORD/LB and
Chairman of the Supervisory Board of Deutsche Hypo

MESSAGE FROM THE BOARD OF MANAGING DIRECTORS

Dear Customers and Business Partners,

None of us will soon forget 2016. We witnessed as terror struck in the heart of Germany, for one thing. What is more, the past year held two surprising political decisions in store regarding the outcome of the Brexit referendum and the US presidential election. We cannot even begin to predict at this point what the long-term impact of these decisions will be.

Despite these occurrences, 2016 turned out to be another excellent financial year for the commercial real estate sector in Germany. With a transaction volume of more than € 50 billion, 2016 seamlessly picked up where the successful years before it had left off. As a result, the positive trend from the last several years continued apace. Crucial to this development was the level of domestic and international investor interest in commercial real estate in Germany, which continues to be strong. In a world of growing political uncertainty, Germany has demonstrated its appeal, year after year. The German real estate market is benefiting from the country's reputation as a safe haven, and in these times of low interest rates, it continues to provide investors with attractive investment opportunities.

Against this backdrop, Deutsche Hypo pushed ahead with its positive business development from previous years and once again performed well against the competition in the field of commercial real estate financing. We generated the largest volume of new business to date, totalling € 4.6 billion. Among other things, we benefited from high-volume transactions to which we lent our structuring expertise in our role as lead arranger. Afterwards, we managed to syndicate large portions of the financing volumes.

In 2016, we were able to largely reverse the value adjustments made in financial years 2014 and 2015 for our Heta exposure after Deutsche Hypo, together with many other creditors, approved the securities conversion scheme that was offered. The exceptionally low risk result in our core business area of commercial real estate financing also had a positive impact. This was due to our conservative risk result, on the one hand, and to the favourable state of our target markets at the moment, on the other. The high quality of the real estate we finance and the impeccable creditworthiness of our customers are – and will remain – for us the key pillars of a business policy based on long-term success.

In sum, the result from normal operations for 2016 stands at € 115.0 million. Due to the non-recurring effect previously mentioned, this result can only be compared with the previous year's figure of € 70.3 million to a limited extent. Based on stable general conditions and the Bank's good position, we once again anticipate a successful financial year for Deutsche Hypo in 2017. We also expect to maintain the positive trio consisting of stable earnings, low levels of risk and efficient structures.

Foreword by the Chairman of the Supervisory Board | Message from the Board of Managing Directors | 2016 at a glance | Sustainability | Megatrends



from left: Andreas Pohl, Sabine Barthauer, Andreas Rehfus

We thank you, valued Customers and Business Partners, for the successful collaboration based on a spirit of trust in the past year. Our aim is for you to achieve your goals together with Deutsche Hypo – both in 2017 and beyond.

With best regards,


Andreas Pohl


Sabine Barthauer


Andreas Rehfus

2016 AT A GLANCE

15 February 2016

Deutsche Hypo successfully issues its first € 500 million benchmark mortgage Pfandbrief for 2016. The Pfandbrief has a term of seven years and a coupon of 0.25 %. The issue rate of 99.482 % corresponds to an issue yield of 0.325 %.

11 April 2016

The Deutsche Hypo Index is published for the 100th time. The index, which appears monthly, has now been contributing towards market transparency in the commercial real estate sector for more than eight years by documenting turning points in the economic cycle and market sentiment. Since its launch, the Deutsche Hypo Index has become the benchmark indicator for this industry.

22 April 2016

Deutsche Hypo publishes a study on serviced apartments. It concludes that they represent a niche with growth potential. Higher demand for flexible accommodation concepts in Germany is expected in future due in particular to increasing mobility on the labour market and growing appeal to tourists.

2 May 2016

A Deutsche Hypo study from the Global Markets series finds that, in particular, technological progress and other megatrends, such as demographic development and changing values, will significantly impact the location and amenities of logistics properties. For example, there will be greater need in future for smaller goods distribution centres at decentralised locations as a result of the trends towards urbanisation and individualisation.

4 May 2016

Deutsche Hypo receives a prime rating for the first time from oekom research AG, a rating agency in the field of sustainable investment. As a result, the Bank – with its current C+ rating – ranks among the best three companies in the industry at the moment. Also, imug Beratungsgesellschaft für sozial-ökologische Innovationen mbH raised Deutsche Hypo's sustainability rating in all of the categories it evaluates back in February 2016.

10 May 2016

Deutsche Hypo's second benchmark issue for 2016 is also highly successful. The mortgage Pfandbrief with a volume of € 750 million comes with a coupon of 0.25 %. The issue rate was 99.635 %, which corresponds to a yield of 0.294 % and thus a reduction in the yield of mid-swap minus one basis point. The issue was oversubscribed twofold.

19 May 2016

Deutsche Hypo's Supervisory Board appoints Sabine Barthauer to the Bank's Board of Managing Directors. She primarily assumes responsibility for the commercial real estate financing business outside of Germany and for the Structured Finance Division. Barthauer joins Andreas Pohl and Andreas Rehfus effective 17 August 2016. Pohl, previously the speaker of the Board of Managing Directors, took over as its chairman effective 1 July 2016.

15 July 2016

Deutsche Hypo successfully taps an existing benchmark mortgage Pfandbrief with a remaining term of just over six and a half years by € 250 million to € 750 million. The yield for the increase amounts to 0.0771 %. Demand for the Pfandbrief is tremendous: the issue was oversubscribed fivefold.

18 August 2016

Deutsche Hypo finances the purchase of the "Granite" housing portfolio in the Netherlands for a special-purpose vehicle managed by the PATRIZIA Group. The financing volume amounts to € 68.6 million and will be provided over a period of ten years. The well-diversified portfolio includes 29 residential properties with a total 1,275 units at 23 locations in the Netherlands.

6 September 2016

Deutsche Hypo's Megatrends study from the Global Markets series analyses the respective impacts of megatrend clusters, specifically Globalisation, Technological Progress, Sustainability and Economy 4.0, on residential, office and retail properties, and highlights key challenges. Megatrends will play an important role in the long-term development of real estate markets, as society is growing increasingly more global, digital and connected.

28 September 2016

Deutsche Hypo's Supervisory Board extends the contract of member of the Board of Managing Directors Andreas Rehfus ahead of schedule by an additional five years until 2022. As a result, the three-person Board of Managing Directors will continue to consist of Chairman of the Board of Managing Directors Andreas Pohl, Sabine Barthauer and Andreas Rehfus. Rehfus joined Deutsche Hypo in 1995 and has been a member of the Bank's Board of Managing Directors since 2007.

15 December 2016

Deutsche Hypo, Berlin Hyp and HSH Nordbank finance an extensive portfolio of existing properties for DIC Asset AG as part of a club deal. The financing volume amounts to € 960 million; of this amount, Deutsche Hypo is providing € 510 million as the arranger and syndicate leader. This marks the largest lending deal in the history of Deutsche Hypo.

SUSTAINABILITY

As one of Germany's oldest Pfandbrief banks, Deutsche Hypo combines decades of tradition and experience in the field of real estate financing with responsible corporate governance and a strategy squarely focused on the future. Sustainability is therefore one of the Bank's key areas of action, which is why Deutsche Hypo strives for a set-up that facilitates lasting profitability. This, in turn, will ensure the Bank's future earning power and secure jobs over the long term. With regard to real estate finance, the Bank serves as a partner whose financing has an impact on the physical design of many cities. Quality, professionalism and sustainability of the properties financed by the Bank are key factors in lending decisions.

Deutsche Hypo has identified a total of five fields of action for sustainability and backed them with strategic priorities: governance, customers, employees, society and the environment. Deutsche Hypo provides insight into its sustainability measures through the information on the Bank's website and in the 2015 Sustainability Report. Details are available at www.deutsche-hypo.de and <http://www.deutscher-nachhaltigkeitskodex.de>.

Award with a generous cash prize conferred

The Johann Georg Zimmermann Prize and the Johann Georg Zimmerman Medal are endowed by Deutsche Hypo and rank among the top awards in Germany for accomplishments in cancer research. The award ceremony was held this year on 6 February 2017 at Hannover Medical School (HMM).



Award ceremony 2017

(from left): Prof. Dr Christopher Baum, President of the Hannover Medical School; Prof. Dr Rebekka Schneider-Kramann, recipient of the Johann Georg Zimmermann Prize; Sabine Barthauer, Member of the Board of Managing Directors of Deutsche Hypo; and Prof. Dr Michael Manns, Chairman of the Board of Trustees of the Johann Georg Zimmermann Prize. Prof. Dr Axel Ullrich was not in attendance due to illness.

The € 10,000 Johann Georg Zimmermann Research Prize for 2016/17 – awarded to young medical professionals for their current scientific work in cancer research – went to Professor Dr Rebekka Schneider-Kramann (35), who is head of the Working Group on Haematology, Erasmus Medical Centre, Rotterdam, Netherlands, and Klinik für Hämatologie, Onkologie, Hämostaseologie und Stammzelltransplantation, Uniklinik RWTH Aachen [clinic for haematology, oncology, haemostaseology and stem cell transplant at the teaching hospital RWTH Aachen]. Her research focus is on del (5q) myelodysplastic syndrome, or del(5q) MDS for short. MDS is one of the most common malignant blood disorders among adults. In one current study, Schneider-Kramann identified a mechanism activated specifically in diseased cells which can be used for a particular treatment. In addition, she and her team uncovered the underlying defect in impaired blood formation in MDS.

The Johann Georg Zimmermann Medal for 2016/17 was awarded to biochemist Professor Dr Axel Ullrich, head of the emeritus research group for molecular biology at the Max Planck Institute of Biochemistry in Martinsried near Munich. He is one of the world's leading scientists in conducting research on signal transduction in cancer cells and a pioneer in the development of targeted cancer treatments. With his team, the molecular biologist is investigating the complex system used to transmit information from the cell surface to the cell interior. Ullrich's findings formed the basis for the development of the first targeted anticancer agent, for example.

Children's eyes shining with joy

Deutsche Hypo employees organised a Christmas wish tree for the seventh consecutive year, enabling them to fulfil the wishes of children and young people from the *Göldene Sonne*, an educational and therapeutic residential centre in Rehburg-Loccum.

This year, the wishes of 104 children were written on cards and hung on the large Christmas tree in the foyer of Deutsche Hypo. Colleagues had the opportunity to select a child's wish and make it come true. The guidelines specified spending an average of € 20 per wish. In the end, packages filled with toys, CDs, books or bedding worth more than € 2,000 in total came together under the Christmas tree.

The "*Göldene Sonne*" works in close cooperation with the child and adolescent psychiatry department at the Children's and Youth Hospital "*Auf der Bult*" in Hanover. The children and adolescents who live at the centre have often had to leave their home after experiencing domestic violence, problem relationships or even alcohol and drug abuse.



Works Council Chairman Dirk Metzner presents the gifts on behalf of the Deutsche Hypo employees.

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MEGATRENDS

A megatrend entails long-term social, economic, political and technological changes which, according to current trend research, influence the development of a society for 30 or more years. That means megatrends also have a fundamental impact on the development of real estate markets, because they lead to changes in framework conditions and thereby create major challenges for the real estate sector.

Researchers have currently identified twelve megatrends. They affect the real estate market in very different ways and to very different degrees. Some of the megatrends cannot be clearly separated, as they often overlap significantly. By considering the megatrends sustainability, globalisation, technological progress and economy 4.0, Deutsche Hypo identifies various developments and opportunities for the future, and provides examples of their positive impact on the properties currently financed by the bank.

MEGATREND GLOBALISATION

Globalisation has already significantly changed the structure of our lives, and the process is far from being completed. National characteristics are becoming increasingly irrelevant - the exchange of goods and information across the classic boundaries is becoming ever more important.

Through globalisation, all areas of our lives become connected at the global level. As a result, there is an increasing multi-dimensional and international interdependence. For example, globalisation has a major impact on mobility. People have fewer ties to their place of birth and are more geographically flexible when it comes to planning their lives. As metropolises have a great appeal, they are increasingly developing into global cities. Appropriate and affordable residential property offerings play an essential role here. Another facet of globalisation is the convergence and networking of formerly local markets. In the area of production, we can already observe globally differentiated value chains. Due to the increasing importance of e-commerce, the need for logistics real estate is growing.

Developments in the real estate sector:

- New residential concepts such as micro apartments for students and commuters, or serviced apartments for seniors are becoming established.
- Increased demand for logistics properties, particularly at transport hubs or due to the development of new distribution locations in urban regions.



Cross-Border Office Portfolio

Type of property	Office
Location	Various (for example in UK, France, Belgium)
Financing volume	€ 190 million
Customer	GLL GmbH & Co. Office II KG



Hotel Zoo

Type of property
 Location
 Financing volume
 Customer

Hotel
 Berlin
 € 35 million
 Kurfürstendamm 25
 Besitz GmbH

Developments in the real estate sector:

- The use of sustainable materials can make properties more attractive by reducing running costs.
- Refurbishment measures can sustainably improve properties that are no longer attractive to tenants.



MEGATREND SUSTAINABILITY

Sustainability has become a fashion word in recent years. The almost inflationary use must not, however, obscure the fact that the sustainability aspect is rightly of great importance in modern society. The goal is to consume resources in a way so that the opportunities of future generations are not impaired.

Sustainability is not restricted to particular areas of our lives. Instead the idea affects almost every area, including the real estate market. Sustainable action in the real estate sector therefore involves the consistent optimisation of real estate portfolios throughout their entire life cycle. This megatrend affects the planning, construction and utilisation of a property, and the subsequent recovery of materials. From an ecological perspective, a property's use of non-renewable resources should be minimised, and the materials used should be as environmentally friendly and recyclable as possible. From an economic perspective, the aim is to reduce life cycle costs to the lowest possible level and thereby ensure that a property remains economically viable throughout its life cycle. Meanwhile, from a social perspective, properties must also contribute to the well-being of the people that use them.

MEGATREND TECHNOLOGICAL PROGRESS

Always faster, always better, always more innovative. The technical progress has an enormous dynamic and changes our lives in almost all areas. Sometimes it is a small relief in everyday life, sometimes a change with a serious impact on society and thus also on the future design of real estate.

The technological progress includes technological innovations that allow the use of new methods and processes, or the production of new or higher quality products. Technological progress initially leads to increased productivity as well as a better supply products and services for people - whether in quantitative or qualitative terms. For example, the development of the internet and mobile communications led to a number of megatrends. This has also a direct effect on mobility. Access to information is no longer tied to a specific location. That has affected the requirements for modern office properties, in particular. The traditional pattern of location and time-based working is being replaced by solutions that are flexible in terms of structure, working hours and location.



Developments in the real estate sector:

- The marketing of apartments depends on their technical amenities, e.g. smart homes with networked technology and appliances.
- Co-working spaces are becoming increasingly important in major cities.

Dockland Hamburg

Type of property

Office and residential portfolio

Location

Hamburg

Financing volume

€ 215,0 million

Customer

ROBERT VOGEL
GmbH & Co. KG



Developments in the real estate sector:

- Demand for multi-functional office properties that include spaces for restaurants, medical practices and wellness areas.
- Creation of new retail formats, such as drive-in stores or warehouses used exclusively for the presentation of goods.

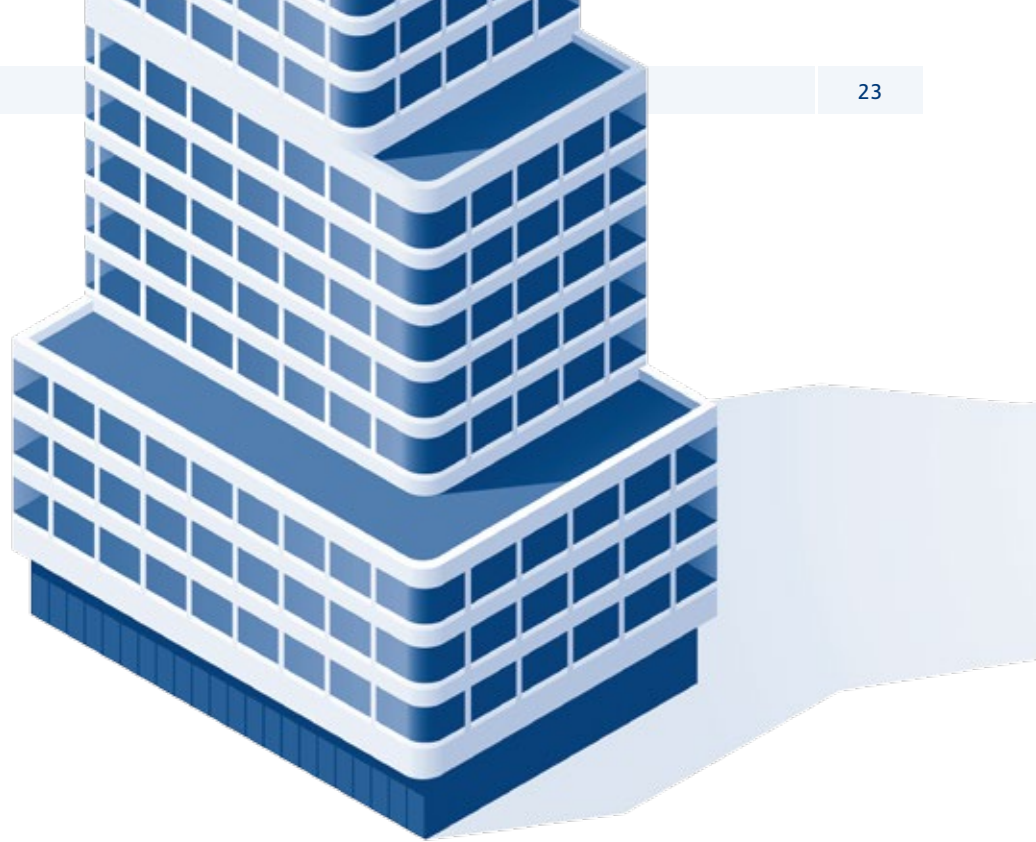


Source: Architecture: HASCHER JEHLE Architektur, Visualisation: bloomimages

Lister Dreieck

Type of property
Location
Financing volume
Customer

Office
Hanover
€ 64.0 million
Project company of
KÖBL KRUSE Gruppe



MEGATREND ECONOMY 4.0

The economy is in a profound process of change. There is a further change in value chains. New techniques enable a growing communication between us people, machines and products. The emerging knowledge society creates a completely new work environment, which is enormously flexible.

We face radical structural changes to our economy and its development. There is increasing economic integration at the global level. That integration is taking place in both the monetary and real economies. International financial markets will become increasingly important, while manufacturing will be subject to fundamental change. Examples include the fully automated ordering of materials or the ability to tailor products to the wishes of individual customers without the need for a separate production process. Digitalisation and technological development are closely connected because digital technologies can be used to improve business processes. The working world is also becoming a knowledge-based sphere, with service, information and creative workers playing an increasingly important role.

MANAGEMENT REPORT

The figures in the tables and charts in the management report are expressed in thousand euros (€ thousands), million euros (€ millions) or billion euros (€ billions). It should be noted that the amounts and percentages quoted in the tables, charts and text are rounded figures, resulting in rounding differences in some cases.

Fundamentals of the Bank

Deutsche Hypo's business model

Deutsche Hypothekenbank (Actien-Gesellschaft), Hanover, Germany (Deutsche Hypo or the Bank) was formed in 1872 and is one of the most renowned Pfandbrief banks in Germany. The headquarters of Deutsche Hypo are in Hanover. It also has offices in Hamburg, Frankfurt, Munich as well as Amsterdam, London, Paris and Warsaw. Deutsche Hypo is a German real estate bank with a European focus and supports its customers in the strategic target markets of Germany, the UK, France, Benelux and Poland as a professional and strategic finance partner.

As a company of the Norddeutsche Landesbank Girozentrale (Anstalt des öffentlichen Rechts), Hanover, Braunschweig, Magdeburg, (NORD/LB), Deutsche Hypo is the centre of competence for commercial real estate finance business in the Group. This also includes being the main issuer of mortgage Pfandbriefe in the NORD/LB Group. In addition to this, the Bank funds itself by issuing unsecured bonds. The goal is to have the possibility to fund at competitive conditions at any time. This plan is achieved through the quality of the cover pools and the associated ratings of the Pfandbriefe and through the credit rating of the Bank for the area of unsecured bonds.

Deutsche Hypo's main business activities can be divided into two business areas. Commercial real estate finance is the core business area. It bundles all the financing of customers that primarily generate their cash flow from real estate or make significant real estate investments on a regular basis. Commercial real estate finance produces roughly 80 % of the Bank's total net interest and net commission income. In the capital market business, Deutsche Hypo bundles the public sector finance business. For some years now, the Bank has been reducing this portfolio. Furthermore, this area handles business in securities, money markets, derivatives with banks as well as funding.

In its regular business operations, Deutsche Hypo reacts to numerous external influential factors. This is mainly due to the economic and sector-specific framework conditions that have a direct impact on the development of business in the business areas and thus the Bank's net assets, financial and income position. Furthermore, a number of customer-specific factors, such as changes in the redemption or extension behaviour, the holding period of real estate or the time of a sale in project developments, have a significant influence on the Bank's real estate finance portfolio that is relevant in particular for the Bank's development. In addition, regulatory framework conditions should be named as an external influential factor for the development of Deutsche Hypo's business and income. The various funding options are influenced, among other things, by developments on international financial markets and Deutsche Hypo's ratings. They also have an influence on the management of liquidity and the valuation of the public sector finance portfolio.

Group affiliation

Deutsche Hypo is a strategic participatory interest of NORD/LB, which holds 100 % of its shares. As a subsidiary, Deutsche Hypo is included in the consolidated financial statements of NORD/LB. NORD/LB's consolidated financial statements as at 31 December 2015 were published on 6 June 2016 in the federal gazette.

There is a profit and loss transfer agreement with an unlimited term between Deutsche Hypo and NORD/LB. This agreement requires that Deutsche Hypo transfers its profits to NORD/LB. At the same time, NORD/LB is required to compensate for any possibly arising loss at Deutsche Hypo. The profit and loss transfer agreement means that there is a fiscal tax unit. By transferring profits or losses, Deutsche Hypo reports an annual result of zero. Due to this circumstance, the result from normal operations and the profit before taxes and profit and loss transfer shall be the focus in the following.

Deutsche Hypo's goals and strategies

Deutsche Hypo's main corporate goals are to secure and increase corporate value, profitability and returns over the long term. The Bank also strives to further expand the significance of commercial real estate finance in the future. The expectation is that the Bank will continue to be perceived as an attractive competitor with interesting finance offers. It is involved in the selective and risk-appropriate strengthening of its market position in Germany and abroad. The strategic target markets of Germany, the UK, France, Benelux and Poland are characterised by high target customer concentration, a large portfolio of real estate and a long-term positive development. The financing in its home market of Germany also remains the largest share of the commercial real estate finance portfolio, accounting for at least 60 %.

In addition to the intensive support of customers on the financing side, the Bank is also pursuing close collaboration with institutional investors as well as insurance companies and pension funds that have an interest in investments involving real estate finance. The real estate know-how built up at Deutsche Hypo should be employed even more to serve the interests of institutional investors in future.

Deutsche Hypo strives to further reduce its public sector finance portfolio in the capital market business. New business is conducted solely restrictively in this business area and primarily serves the management of liquidity and cover pool management.

The Bank's Economic success must go hand in hand with an intact natural environment and in a society with stable social relationships. Sustainable corporate governance is therefore very important for Deutsche Hypo. The Bank's sustainability report is available at <http://www.deutscher-nachhaltigkeitskodex.de> and on Deutsche Hypo's website.

Controlling system

Deutsche Hypo's controlling system starts with the business and risk strategy and focuses on a sustainable increase in the corporate value. This value-oriented controlling philosophy is reflected in the central operating key performance indicators that are aimed at the Bank's profitability, productivity and risk profile.

Deutsche Hypo's controlling methodology includes the preparation of medium-term plans in which the economic development is considered over a five-year period. There are also regular plan/actual comparisons as well as projections for the end of each financial year and beyond.

Aside from the result from normal operations (result), the key financial performance indicators are the Return on Equity (RoE) and Cost-Income Ratio (CIR). The RoE is defined as the quotient of the result before taxes and the Bank's capital pursuant to commercial law (not including investment by silent partners). The CIR is defined as the ratio of the administrative expenses (including the depreciation and amortisation on tangible fixed and intangible assets) to the total from the net interest income, net commission income and other net operating income. On account of their particular influence on the Bank's income performance, the development of new business and the portfolio in the core business area of commercial real estate finance are used as supplementary central performance indicators in the Bank.

In addition, the development of risk weighted assets (RWA), margins in the new business and portfolio of commercial real estate finance and, due to inclusion in the external reporting of the NORD/LB Group, the development of results according to IFRS serve as supplementary performance indicators for the Bank. Deviating from the previous year, the RoRaC is only used as a supplementary performance indicator in the course of business area management. Compliance with external requirements for regulatory performance indicators, in particular in the context of risk measurement for credit, market, liquidity and operational risks, is ensured in the form of supplementary constraints. Additional economic performance figures and risk limits also apply.

The controlling system is rounded out by non-financial performance indicators such as the development of employee capacities. These act primarily as early indicators.

Corporate Governance Statement

The disclosures required in accordance with Section 289a of the German Commercial Code (HGB) apply fundamentally only to publicly listed stock corporations and certain other stock corporations focused on capital markets. As in previous years, Deutsche Hypo has nonetheless voluntarily published a Declaration of Conformity with respect to the Corporate Governance Code for financial year 2016 at the Bank's website under <http://www.deutsche-hypo.de>. It can also be found in the Corporate Governance Report of the Bank's annual report. Furthermore, the now mandatory disclosures on the percentage of women in management have been provided on the Bank's website in compliance with the requirements (also applicable to Deutsche Hypo) under Section 289a (4) of the German Commercial Code (HGB).

Economic report

Macroeconomic and sector environment

Economic performance in Germany and Europe

The development of the German economy was very solid in 2016. Economic growth accelerated slightly again despite several negative events. The real GDP rose by 1.9 % compared to the previous year. After very strong growth in the first half of the year and a brief lull in the summer, the pace of growth increased significantly in the last quarter. As expected, the economic expansion was supported mainly by domestic demand in 2016. The key growth drivers were private consumption (+ 2.0 %) and public consumption (+ 4.2 %). Construction investments made a healthy contribution to the economic expansion with 3.1 % growth. On the other hand, the development of net exports and equipment investments for the year overall was disappointing (+ 1.7 %). Positive economic development contributed to a further improvement in the employment situation. Nearly 43.6 million people, seasonally adjusted, were employed at the end of December.

The economic upswing in the Eurozone continued in 2016 as expected. The quarter over quarter growth rate was consistently above 0.3 %. The overall economic performance grew by 1.7 % in 2016. Overall economic development was rather heterogeneous again in 2016. Spain once again stood out among the large economies with very rapid economic growth. Expansion rates for the Netherlands and Germany were disproportionately high as well. Economic development in France and Italy on the other hand was more subdued. Both countries continue to suffer from structural problems. Greece once again brought up the rear in 2016 but was at least able to stabilise in the course of the year – starting from a very low level. While foreign trade impulses for the entire Eurozone once again remained weak, growth was supported by domestic demand. Furthermore, the high expansion rate for real private consumption was supported by a once again very low inflation rate of + 0.2 % and a noticeable reduction of the unemployment rate to an annual average of 10.0 %.

As the implementation and organisation of Great Britain's exit from the EU remains unclear, the country's economic dynamics showed initial signs of slowing towards the end of the year under review. The employment trend declined for the first time in more than a year and, most recently, consumer confidence decreased noticeably. Apparently the fear of rising prices leading to a decrease in buying power was the crucial factor here for many consumers. This development was not yet reflected in the real GDP, which was 2.0 % for 2016.

Development of real estate markets

Notwithstanding complex effects of the Brexit decision and the political course in the USA among other factors, the attractiveness of global real estate investments remained unshaken in 2016. The global transaction volume was € 628 billion in 2016 (2015: € 668 billion). While this represents a decrease of 6 % compared to 2015, the level remained high.

European real estate markets

The share of cross-border investments in the European real estate markets was stable in 2016. While the uncertain, in part politically defined framework conditions led to caution in European commercial real estate markets, the demand for real estate remained high and was reflected by a transaction volume of around € 234 billion (– 8 % compared to the previous year). The reduced availability of top properties led to local overheating tendencies with high prices in some areas.

Great Britain as a target market weakened in the course of the financial year due to the Brexit decision. This was reflected by partly reduced office leasing activities. Nevertheless, London remained in first place in a European comparison of peak rents in Q4 2016. The UK retail market also remained in very good condition in the course of the year, in particular thanks to international tourism in London. A cooling trend was most recently seen in the housing market even though this segment was less volatile in relation to the Brexit decision. The short supply of housing space caused the demand for affordable living quarters to increase continuously in 2016. Generally speaking, international investors continue to view the UK real estate market as an attractive market in the long term. This resulted in a transaction volume of around € 56 billion at the end of 2016 (– 36 % compared to the previous year).

France's real estate market remained Europe's third largest investment market once again in 2016. However, the transaction volume did decrease considerably to around € 28 billion, a drop of 8 % compared to the previous year. The high local price level that was already reached in part led to restraint on the demand side, reducing pressure on the general price spiral. Prime yields for office and retail properties averaged 3.5 %. Developments in the various asset classes continued to be favourable, notwithstanding uncertainties resulting from terrorist attacks and the occasional decline in the number of tourists. Stable retail sales were seen in the retail property market. Demand in the housing market was solid in the course of the year, especially in the larger metropolises. Leasing in the office property market, which is important for the Paris region, was favourable as well in the course of the year. The market for logistics properties was steady. Only the hotel property market saw a major decrease in occupancy rates and sales revenue.

Developments in the real estate market of the Benelux states were highly positive in 2016 as well. More than half the capital came from abroad since the Benelux states were also very much in the focus of international investors. Increasing housing demand was seen in the Dutch real estate market in the Randstad metropolises. The recovery of the housing market therefore continues unabated. Growth continued in both the retail and the housing property market for core properties in Amsterdam. On the other hand, secondary office properties and locations suffered from very high vacancy rates. Significant rent increases are seen in Amsterdam's retail property market. Revenues slumped in the hotel property market due to terrorist attacks, especially in Brussels. The transaction volume in the Netherlands was € 11 billion (+ 17 % compared to the previous year). Belgium recorded a transaction volume of € 4 billion (– 17 % compared to the previous year). Luxembourg's real estate market also continued its positive development, ending financial year 2016 with a transaction volume of € 1 billion (+ 5 % compared to the previous year).

The recovery in the target market of Poland continued, especially in the housing market. In the Polish retail property market, the development of prime rents in top locations remained stable in a robust market environment. Peak rents at the office location of Warsaw were approximately comparable to the metropolises of Hamburg and Brussels at the end of the year. High local construction activity was

seen in this segment. The development of private consumption and the employment market as drivers for the retail property market was solid. In Warsaw and the regional centres, the office property market was more differentiated. The vacancy rate in Warsaw's office market was as at a level not seen since 2003. At the same time, there were numerous project developments. The regional centres continued to hold their own. At the end of the year, the transaction volume was around € 5 billion (+ 29 %).

German real estate market

Historically low interest rates continued to drive the high investment demand of institutional investors in 2016. The transaction volume in the German investment market defined by an ongoing severe supply shortage was around € 53 billion (2015: € 55 billion). Demand continued to be strong for the office asset class with a high proportion of the total transaction volume at 45 %, followed by retail with a share of 23 %. It was a new record year for logistics properties with about € 4.7 billion. The seven real estate strongholds with a transaction volume totalling around € 30 billion remained in focus (2015: € 31 billion).

Clearly positive developments in the previous year continued for the office location of Germany. This trend was supported by positive economic development and the boom in the German employment market. The big 7, with a sales volume of 3.9 million m², generated growth of 9 % compared to 2015 overall. Ongoing high demand for space worsened the shortage of modern space and led to another increase in peak and average rents. The aggregate vacancy rate of the big 7 was 5.5 %. Space turnover increased by 9 % in A cities and 7 % in B cities in 2016. Vacancy rates continued to decrease in nearly all B cities, leading to significant local rent increases.

The German retail market benefited from positive consumer sentiment notwithstanding the ongoing growth of the online business. This was reflected by the continued although slower growth of retail sales. Most retailers focused on space optimisation over expansion. Peak rents in 1a locations remained largely stable in the course of the year. Only Berlin saw a rent increase. Large areas in excess of 1,000 m² accounted for more than 60 % of the rented space.

The German housing market continued to be defined by persistently rising prices and rents for attractive living space in the metropolises, combined with growing demand. However, the successes seen in 2015 could not be sustained in financial year 2016. With a transaction volume of around € 14 billion (2015: € 25 billion) and a turnover of 137,000 residential units, it was nevertheless a very good year for this asset class. Berlin accounted for one-fifth of all residential transactions. This once again puts the capital city at the peak of the residential transaction markets.

The German logistics market continued its successful trend in the year under review. Stable fundamental framework conditions and the steady growth in Internet trading remained the leading driving forces behind the demand for logistics properties in Germany.

The hotel market had another record year and exceeded the € 5 billion mark with its transaction volume at the end of 2016. This was the seventh consecutive sales increase. Foreign investors were comparatively active with a share of about 57 %. Hotel investments gained importance in 2016, also outside the seven largest investment locations.

Development of international financial markets

The capital markets were significantly influenced in 2016 by central bank measures and two major events in particular, the Brexit and the US presidential elections. The US Federal Reserve delayed the second increase in the prime rate since the financial crisis until December due to great political uncertainty. On the other hand, the European Central Bank (ECB) actually intensified its expansive monetary policy. In addition to lowering the deposit facility rate to – 0.40 %, further changes to the ECB bond repurchase program (EAPP) were decided – including a temporary increase in the monthly purchase volume for one year starting in April 2016. Corporate bonds are also being purchased since the middle of last year. The inflation rate did exceed the 1.0 % mark for the first time in more than three years at the end of 2016. However, this increase was mainly due to base effects of the crude oil price while domestic price pressure was low. Against this background, the ECB Council decided at the end of the year to extend the EAPP until at least the end of 2017. As a result, low interest rates were maintained in principle, even though capital market rates increased slightly from their low at the end of 2016, especially for longer terms.

The yield on ten-year US government bonds was 2.44 % at the end of December, while the return on German federal bonds with identical terms remained much lower at 0.21 %. The US dollar benefited from the interest turnaround in the USA and the increasing monetary policy divergence between the US Fed and the ECB. In this environment, the EUR/USD exchange rate in 2016 moved in a range of over 1.16 to temporarily less than 1.04 USD per € in December. The EUR/USD cross-currency basis swaps widened in the course of the year, standing at around – 45 basis points in the short and medium terms and around – 40 basis points for ten-year terms at the end of the year.

Pfandbriefe continued to enjoy their reputation as a safe financial investment in the international markets. Yields continued to fall in the year under review, mainly due to the massive bond purchases by the ECB. Around 88 % of Pfandbriefe with an issue volume of at least € 500 million no longer generated a positive yield. Nevertheless, there was no drop in the demand for Pfandbriefe since investors often compared Pfandbriefe to government bonds.

Development of the banking sector

Competition in commercial real estate finance once again increased in 2016 due to the lack of attractive investment options caused by low interest rates. The supply of high quality real estate could not keep pace with increased demand in the year under review. Investors increasingly switched to B and C locations. In part, investments were made in properties and locations considered critical based on risk aspects. Excessive price developments were also seen in some cases but no bubbles have formed to date. Deutsche Hypo maintained its conservative view unchanged and ensures an ongoing high quality for its real estate financing. Additionally, the real estate finance sector was increasingly confronted with investors that are cutting their internal financing to a growing extent. A trend towards financing large transactions was observed at the same time. Comparatively high prices and low yields were observed across all asset classes overall.

Course of business at a glance

Significant influential factors and developments in financial year 2016

The past financial year was once again largely defined by a fundamentally positive real estate environment and the ongoing high level of competition in commercial real estate finance. Deutsche Hypo succeeded in significantly increasing the new business volume in commercial real estate finance compared to the previous year. The quality of the real estate finance portfolio remained at the high level of the previous year. On the reporting date, the proportion of financing in default out of the overall portfolio was significantly below the expected long-term average due to the ongoing repayment of these financing transactions. Due to write-ups and the collection of receivables that had been written off, commercial real estate finance in fact had a slightly positive risk result in the past financial year.

One important development for the Bank was the so-called Brexit decision. As Europe's largest commercial real estate market, Great Britain is an important foreign market for Deutsche Hypo. There were no direct negative effects on Deutsche Hypo from the Brexit decision as of the reporting date. Based on the high quality of the financing portfolio, the Bank considers itself well positioned currently and also for the future. Since Deutsche Hypo does not expect any large-scale and permanent negative developments in Great Britain's real estate markets at this time, the Bank will continue to take advantage of attractive new business opportunities there, taking into account its own conservative risk policy and with particular attention paid to monitoring market developments.

Notwithstanding greater uncertainties in the international financial markets in the meantime, the ongoing expansive monetary policy measures of the ECB have maintained a largely calm environment for the Bank's public sector finance business. The Bank consistently implemented the reduction of the portfolio in this business area as planned and continued to improve the credit quality of the public sector finance portfolio in the course of active portfolio management.

Developments related to Heta Asset Resolution AG (Heta) were also of special importance within the capital market business. In the course of winding up Heta, creditors were offered cash compensation at 75 % of the original receivable or an exchange of the existing nominal receivable for a government guaranteed zero coupon bond of the Kärntner compensation fund (KAF), with a cash value of approximately 90 % of the existing receivables from Heta. This offer was accepted by the majority of creditors and the Bank chose the exchange for the zero coupon bond. Receiving the KAF papers was associated with an adjustment to the Bank's risk provisioning, which had a significant positive impact on the result in the capital market business for the past financial year. The charges from the two previous years were in part recovered as a result. Notwithstanding the settlement and the positive impact on results in the past financial year, a significant loss remains on the Heta receivables and securities.

In the course of servicing the market, some own public Pfandbriefe were also bought back in the past financial year. These buy-backs had a corresponding negative influence on the risk result in the capital market business but also led to a lower funding cost.

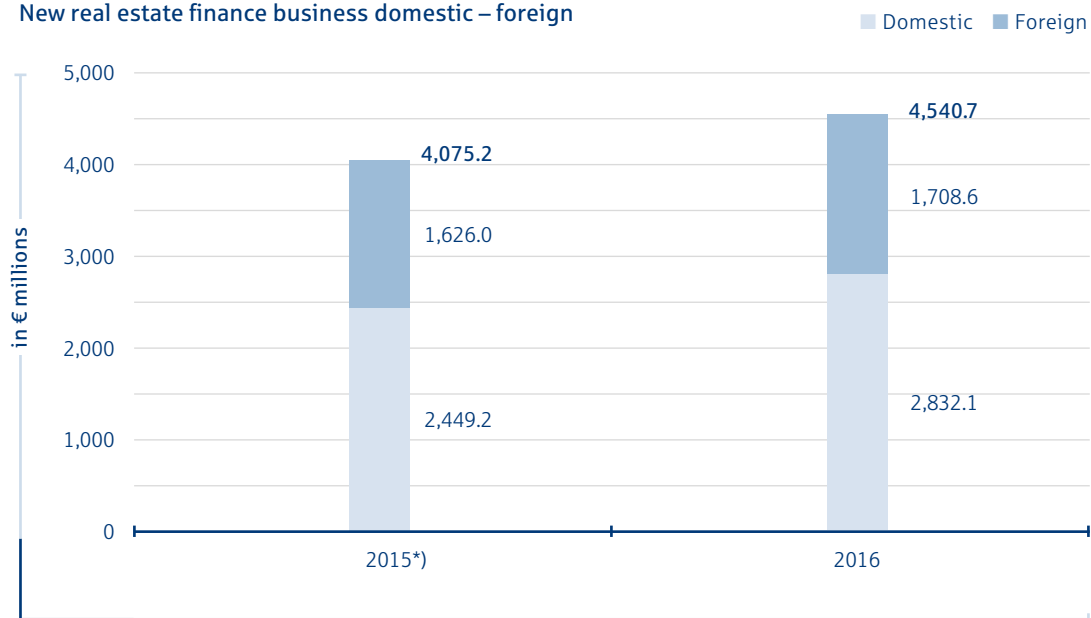
The Bank's business development continued to be affected by developments in the industry's regulatory environment. Deutsche Hypo managed to keep administrative expenses below the previous-year value notwithstanding increased implementation costs caused by new regulatory requirements and another increase in the bank levy compared to the previous year.

The disclosed developments and special effects led to an extremely good result of € 115.0 million in the past financial year (2015: € 70.3 million). In addition to strengthening the precautionary reserves, a much higher profit transfer to NORD/LB could be realised as a result. The reduced transfer in previous years due to the Heta charges was offset as a result.

Development of new business in commercial real estate finance

Despite increasing competition, Deutsche Hypo also continued to pursue its lending goal of only including loans with a sufficiently good risk profile in its portfolio. Notwithstanding the high quality standard for new financing and a challenging competitive environment, Deutsche Hypo increased the new business volume significantly in the past financial year to € 4,540.7 million (2015: € 4,075.2 million).

New real estate finance business domestic – foreign



*) In a change to the previous methodology, extensions of existing financing were included when the extension periods were at least one year. Previous-year figures have been adjusted accordingly.

The largest proportion of new business was once again domestic at 62.4 % (2015: 60.1 %). Commitments increased slightly to € 2,832.1 million (2015: € 2,449.2 million) in the domestic market and € 1,708.6 million (2015: € 1,626.0 million) abroad. Once again, a large proportion of the foreign new business was in the target markets of UK and Benelux. While new loans in UK remained nearly constant at € 749.3 million (2015: € 730.7 million), the new business volume in the Benelux target market increased significantly to € 652.5 million (2015: € 572.0 million). In UK, the focus was on maintaining the portfolio quality at the currently high level, also against the background of current uncertainty due to the Brexit, and on keeping the portfolio volume constant with a conservative approach in the course of new business. In the Benelux target market, the increase in the new business volume was in part due to a higher volume of residential real estate financing. Here, the bank is pursuing further improved diversification of the overall portfolio.

Office properties as an asset class continued to account for the largest proportion of the new business volume by far at € 2,010.4 million (2015: € 1,822.5 million). The financing volume for retail properties on the other hand dropped significantly compared to the previous year, to € 973.7 million (2015: € 1,378.5 million). In the course of the planned expansion, residential financing, at € 871.3 million (2015: € 411.8 million), accounted for 19.2 % (2015: 10.1 %) of total new loan commitments.

Funding activity

Funding in the past financial year was realised by issuing own securities in the amount of € 3,938.2 million (2015: € 3,571.5 million), thereof € 1,800.0 million (2015: € 1,601.5 million) mortgage Pfandbriefe and € 2,138.2 million (2015: € 1,970.0 million) unsecured bonds.

A clear trend towards large and benchmark issues was seen for Pfandbriefe. Deutsche Hypo, on the basis of both solid domestic and foreign demand, brought a 7 and an 8-year benchmark issue to market. The 7-year issue was floated in February with a volume of € 500.0 million and increased by € 250.0 million in July; the original transaction was oversubscribed one and a half times and the increase five times. The 8-year benchmark issue with a volume of € 750.0 million was double oversubscribed when it was floated. Private placements that were larger from the outset were also increased by considerable amounts by the Bank. The unsecured bonds were issued exclusively as private placements. Here, there was a noticeable preference among German investors for loans (Schuldscheindarlehen) and registered bonds.

Overall, the process of obtaining liquidity went well. Thanks to its product quality, establishment in the market, and due to the ECB purchase program, the Pfandbrief was very easy to place. Obtaining unsecured liquidity proved more challenging. Difficult market conditions, the bail-in discussion and the changed perception of some issuers with the accompanying higher spreads made the market more price-sensitive and placement more difficult. Notwithstanding a rating adjustment of its own unsecured bonds, Deutsche Hypo consistently succeeded in obtaining the required liquidity from the market at competitive prices in line with the market.

Deutsche Hypo was once again engaged in secondary market servicing for its own securities in the past financial year, as usual. The portfolio of own securities at face value was € 39.2 million (2015: € 24.5 million) at the end of the year. Replacing the cash flows for the respective purchases was not a problem.

Net assets, financial and income position

Income position

in € millions	Total result		Commercial real estate finance		Capital market business		Other business	
	2016	2015	2016	2015	2016	2015	2016	2015
Net interest income	202.1	224.5	168.6	175.5	17.2	31.2	16.2	17.8
Net commission income	3.7	0.5	4.3	1.4	-0.6	-0.9	0.0	0.0
Administrative expenses	76.4	77.8	40.0	39.7	6.0	5.3	30.4	32.7
Other operating income	-3.5	-6.3	0.0	-2.0	0.0	0.0	-3.5	-4.3
Risk result	-66.6	-41.3	2.8	-15.6	-37.4	-7.7	-32.0	-18.0
Income from securities and participatory interest	55.7	-29.4	0.7	0.0	55.0	-29.4	0.0	0.0
Result from normal operations	115.0	70.3	136.5	119.6	28.3	-12.1	-49.8	-37.2
Extraordinary result	-1.6	-0.1	0.0	0.0	0.0	0.0	-1.6	-0.1
Interest on investment by silent partners	8.4	8.4	0.0	0.0	0.0	0.0	8.4	8.4
Profit before taxes and profit and loss transfer	104.9	61.8	136.5	119.6	28.3	-12.1	-59.8	-45.7
CIR	37.8 %	35.6 %	23.1 %	22.7 %	35.8 %	17.6 %	>100.0 %	> 100.0 %
RoRaC / RoE *)	12.3 %	7.4 %	35.3 %	29.5 %	24.0 %	-7.9 %	<- 100.0 %	<- 100.0 %

*) on business area level disclosure of RoRaC, on level of whole bank disclosure of RoE

RoRaC business area = Profit before taxes and profit and loss transfer/fixed capital (= 9% of yearly average risk-weighted assets)

RoE whole bank = Profit before taxes and profit and loss transfer/yearly average of capital under commercial law (= subscribed capital + capital and profit reserves)

Deutsche Hypo generated a result from normal operations of € 115.0 million in the financial year 2016. The previous-year result of € 70.3 million was considerably exceeded. This favourable result is accounted for by the solid earnings base and unusually good risk result in the core business area of commercial real estate finance. The result for the business area increased significantly again to € 136.5 million. At the same time, the precautionary reserves pursuant to Section 340f German Commercial Code (HGB) were strengthened, with an adverse effect on results from other business. Multiple special effects influenced the result of the capital market business. Write-ups related to the exchange of the impaired Heta receivables and securities for a zero coupon KAF bond were the leading factor here, accounting for most of the increase in the result for the business area to € 28.3 million (2015: € - 12.1 million). Expenditures for repurchasing issued Pfandbriefe in the course of market servicing had the opposite effect.

As expected, the net interest income for the Bank as a whole at € 202.1 million was below the previous year's figure of € 224.5 million. Against the background of a stable real estate finance portfolio, slightly decreasing margins and high fees earned, earnings in commercial real estate finance were nearly at the previous year's level. While comparatively high earnings from prepayment penalties led to an extraordinarily high interest income in 2015, these earnings returned to a normal level in the financial year. In keeping with the major reduction of the capital market portfolio, the margin result generated by the portfolio was correspondingly lower.

Net commission income improved to approximately € 3.7 million (2015: € 0.5 million). This was due mainly to the fees Deutsche Hypo was able to collect as an arranger in the course of larger transactions.

Administrative expenses at around € 76.4 million were about € 1.4 million below the previous-year level of € 77.8 million notwithstanding the increase in bank levies. This declining trend encompasses both personnel and operating expenses, and is indicative of functioning, successful cost management by Deutsche Hypo. Personnel expenses were also reduced by the lesser increase in pension provisions. The CIR, which remained significantly below 40 %, substantiated the operating efficiency of Deutsche Hypo as well. Other operating income improved to around € – 3.5 million (2015: € – 6.3 million). This was due to reduced expenses for the discounting of pension provisions.

Consistently quality-oriented lending policies in combination with stable real estate markets led to a net release of loan loss provisions in commercial real estate finance. Precautionary reserves in accordance with Section 340f German Commercial Code (HGB) were further strengthened at the same time. The risk result allocated to the capital market business was defined on the one hand by write-ups on the exchange of Heta securities at € 20.4 million. On the other hand, the effects of repurchasing public Pfandbriefe with high coupons compared to current interest rates had a negative impact on the risk result. The repurchase satisfied investor offers and simultaneously accelerated the reduction of total assets and reduced future funding costs by reducing cover pool requirements.

The income from securities and participatory interest was around € 55.7 million. Here too the write-up from the exchange of the Heta securities at € 54.6 million was the major factor behind the increase in results. Write-downs on these securities decreased the income from securities and participatory interest in the two previous years.

From an overall Bank point of view, profit before taxes and profit and loss transfer was unusually high at € 104.9 million (2015: € 61.8 million) thanks to the special effects in the capital market business. This led to a significant increase in RoE to 12.3 % (2015: 7.4 %). The profitability increase was also reflected by the return on risk capital tied up in commercial real estate finance. The corresponding RoRaC indicator increased to 35.3 % (2015: 29.5 %).

Net assets

Development of the balance sheet

in € millions	31.12.2016	31.12.2015
Receivables		
Mortgage loans	11,977.0	11,953.6
Loans to local authorities	4,815.5	5,588.6
Other receivables	1,457.3	2,138.1
Securities	6,720.3	7,038.0
Other assets	232.5	225.4
Total assets	25,202.6	26,943.7

Deutsche Hypo's balance sheet total fell again slightly compared to the previous year to € 25,202.6 million (2015: € 26,943.7 million). This decrease was due to the Bank's strategic direction with a further reduction of the public sector finance business.

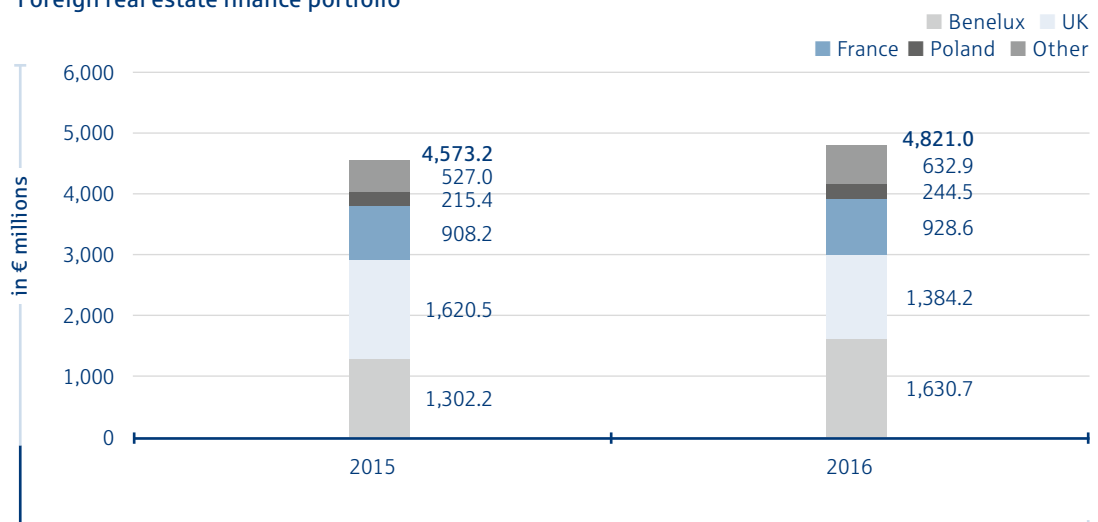
Development of portfolio in commercial real estate finance

Despite the increase in the new business volume, the commercial real estate finance portfolio remained practically unchanged compared to the previous year at € 11,977.0 million (2015: € 11,953.6 million). This was mainly because a large portion of the new business had not yet been paid out and was therefore not transferred to the portfolio. Irrevocable loan commitments at € 1,809.7 million were much higher than the previous-year value (2015: € 1,245.0 million). On the other hand, the high early loan repayments reported in the previous 2015 financial year fell back to a normal level in the past financial year.

Maintaining the good portfolio quality in commercial real estate finance was once again the Bank's focus in 2016. The average rating in the real estate finance portfolio was actually improved again compared to the previous year thanks to a further reduction of financing in default. For more detailed information, please refer to the descriptions on the analysis of credit risk in the expanded risk report. The credit exposures mentioned there are not exactly comparable to the balance sheet portfolios of real estate finance due to the reliance on the nominal volume including the share of loan commitments.

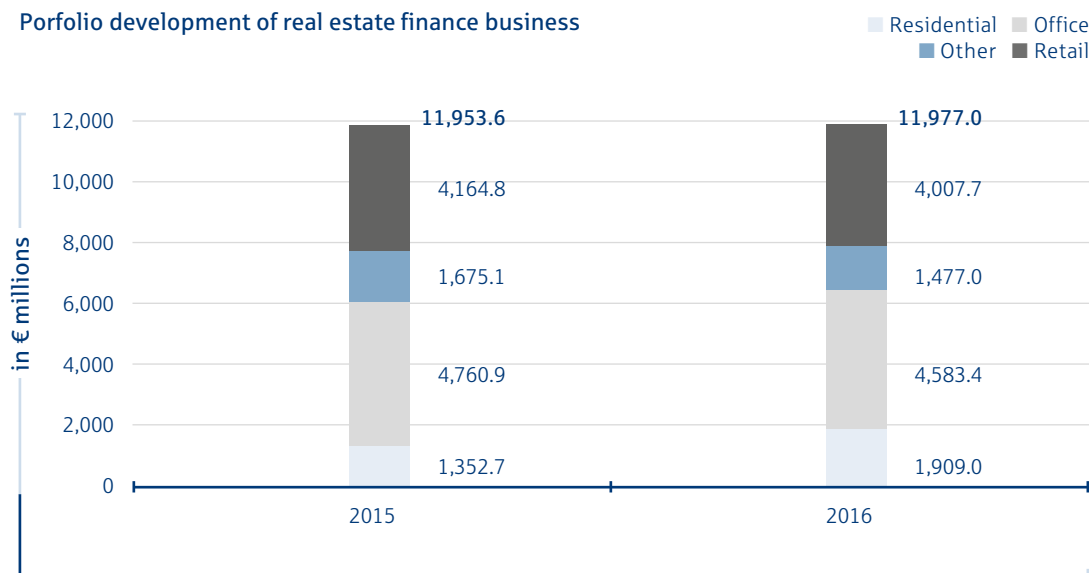
There was a slight shift within the portfolio in favour of the foreign markets. Despite a slight decrease in domestic financing to € 7,156.0 million (2015: € 7,380.3 million), this continued to represent about 60.0 % of the Bank's total real estate finance portfolio. In the foreign markets, the increase to € 4,821.0 million (2015: € 4,573.2 million) was mainly due to the significant expansion of financing in the Benelux target market. Thanks to the high volume of new business, portfolios there increased considerably to € 1,630.7 million (2015: € 1,302.2 million). As a result, the Benelux target market had the largest financing portfolio among the foreign markets on the reporting date. Larger decreases were seen in Great Britain. Despite the stable new business volume, the financing portfolio at the end of the past financial year decreased to € 1,384.2 million (2015: € 1,620.5 million), mainly due to the weakness of the British pound. Smaller portfolio increases were seen in France, Poland and regions not belonging to the direct target markets.

Foreign real estate finance portfolio



In the segmentation of portfolios by asset classes, slight decreases were noted for office properties to € 4,583.4 million (2015: € 4,760.9 million) and retail properties to € 4,007.7 million (2015: € 4,164.8 million). Financing portfolios for other real estate also fell slightly to € 1,477.0 million (2015: € 1,675.1 million). Residential financing portfolios on the other hand increased markedly to € 1,909.0 million (2015: € 1,352.7 million). The Bank significantly expanded the rented flat financing portfolio in the past financial year. This is due to the intended further improvement of diversification in the overall portfolio.

Portfolio development of real estate finance business



Development of portfolio in capital market business

Deutsche Hypo continued the strategic decrease of the public sector finance portfolio in the past financial year. In addition to the portfolio decrease due to scheduled maturities, the holdings of specific high-risk addresses were also reduced by means of disposals. Among other things, holdings in the PIIGS countries were further reduced overall in the past financial year.

Disposals were replaced with high quality securities to the extent required in the course of liquidity and cover pool management. Here, German borrowers accounted for a large proportion of the new business. The quality of the public sector finance portfolio was thereby further improved slightly in the course of active portfolio management. For detailed information, please refer to the discussions on the analysis of credit risk within the expanded risk report.

Overall, the portfolio of receivables and securities in the capital market business fell to € 11,535.8 million (2015: € 12,626.6 million) on the reporting. This includes the municipal loan business that has been significantly reduced to € 4,815.5 million (2015: € 5,588.6 million) and foreign securities that have decreased to € 6,720.3 million (2015: € 7,038.0 million).

Financial position

in € millions	31.12.2016	31.12.2015
Liabilities		
Mortgage Pfandbriefe	8,286.9	8,486.5
Public Pfandbriefe	5,378.5	7,028.5
Unsecured bonds	2,740.5	2,606.9
Other liabilities	7,087.5	7,121.8
Subordinated liabilities	395.0	320.0
Jouissance right capital	60.0	83.0
Funds for general banking risks	14.4	14.4
Equity	913.2	913.2
Other liabilities	326.6	369.4
Total liabilities	25,202.6	26,943.7
Contingent liabilities	1,029.3	1,127.0
Other obligations	1,809.7	1,245.0

On the liabilities side of the balance sheet, the decrease in balance sheet total is associated with a reduction in the portfolio of revolving public Pfandbriefe. The expected decrease to € 5,378.5 million (2015: € 7,028.5 million) continued, also against the background of the strategic portfolio reduction in the public sector finance business. Here, the Bank repurchased own public Pfandbriefe before they matured, also in the course of regular secondary market servicing.

The portfolio of mortgage Pfandbriefe on the other hand decreased only slightly compared to the previous year to € 8,286.9 million (2015: € 8,486.5 million). At the same time, the portfolio of unsecured bonds increased to € 2,740.5 million (2015: € 2,606.9 million) on the reporting date. Regarding the terms and maturities of the liabilities, please refer to the maturity breakdown for liabilities in sections 15 and 16 of the notes. The expanded risk report also includes discussions of the Bank's liquidity situation. Information about Deutsche Hypo's funding activity in the past financial year is found in the descriptions of the course of business.

Balance sheet equity remained unchanged at € 913.2 million in comparison to the previous year. Total equity on the balance sheet plus jouissance right capital, subordinate liabilities and the funds for general banking risks in accordance with Section 340g German Commercial Code (HGB) at € 1,382.6 million slightly exceeded the previous year's value of € 1,330.6 million due to the increase in subordinated liabilities. Please see the explanations in the expanded risk report of this management report regarding the regulatory equity resources.

Off-balance-sheet obligations in the form of irrevocable loan commitments increased significantly compared to the previous year to € 1,809.7 million (2015: € 1,245.0 million). This was due in particular to new loan commitments at the end of the past financial year that will only be transferred to the real estate financing portfolio when they are paid out. Contingent liabilities on the other hand decreased considerably to € 1,029.3 million (2015: € 1,127.0 million), once again mainly due to the maturities of credit derivatives. Please see the notes for further information about off-balance-sheet obligations.

Rating

	Mortgage Pfandbriefe	Public Pfandbriefe	Short-term liabilities	Long-term liabilities	Baseline Credit Assessment (BCA)
Moody's	Aa1	Aa1	Prime-2	Baa1	ba3
			until 15 September 2016 Prime-1 until 26 January 2016 Prime-2	until 15 September 2016 A3	until 15 September 2016 b1

The high quality of the cover pools was reflected by Deutsche Hypo's ongoing very good Pfandbrief rating. Moody's recognised the sustained good asset quality and low NPL ratios in Deutsche Hypo's real estate finance business in the year under review. Furthermore, the rating agency expressly emphasised the Bank's positive earnings trend. Some ratings for the unsecured bonds were adjusted by one notch in the past financial year due to the close relationship between Deutsche Hypo and NORD/LB. To date, the downgrade had virtually no impact on the Bank's relationships with investors.

Comparison of the developments with the forecast from last year

Last year's forecast was based on the assumption of a fundamentally positive market environment for Deutsche Hypo. Ongoing attractiveness of commercial real estate investments due to sustained low interest rates, high liquidity and a lack of investment alternatives for investors was assumed overall for Deutsche Hypo's commercial real estate finance business.

Deutsche Hypo therefore predicted a slight increase in the new business volume for the commercial real estate finance business and a slight expansion of the real estate finance portfolio for 2016 compared to 2015. Ongoing stiff competition in the commercial real estate finance area was expected at the same time, which could in some cases affect the attainable margins.

Due to falling earnings from principal repayments before maturity compared to 2015, Deutsche Hypo expected interest income in commercial real estate finance to decrease slightly. Against the background of conservative risk result planning, a development of the risk result at the normal level was predicted as well. Consequently, a significant reduction of results in commercial real estate finance with a slightly lower RoRaC was expected.

For the capital market business, Deutsche Hypo anticipated a noticeable normalisation of inflation and slightly higher yields towards the end of 2016. Due to the ongoing portfolio decrease in the public sector finance business and a reduction of effects caused by principal repayments before maturity, the interest result was also expected to drop considerably. Overall, a slightly positive result and corresponding positive RoRaC were expected.

From an overall Bank point of view, Deutsche Hypo expected to generate a result only slightly below the 2015 level. In regards to administrative expenses, a moderate increase and therefore also a slight increase in the CIR was predicted against the background of stricter regulatory requirements and higher bank levies. Deutsche Hypo expected a slightly lower RoE compared to 2015. Write-ups of the Heta engagement were identified as an income opportunity.

The described predictions of developments in the business and framework conditions were fundamentally accurate. Strong demand for commercial real estate financing was noted in the real estate markets and reflected primarily by a significant increase in the new business volume compared to the previous year. On the other hand, the portfolio did not increase slightly as predicted but remained approximately at the previous year's level. Under consideration of the contracted financing volume that has not yet been transferred to the portfolio however, the forecast would be accurate. The interest result in the commercial real estate finance business was slightly below the previous year's value as predicted, since earnings from principal repayments before maturity decreased significantly in 2016 as expected. The predicted result was exceeded, especially because risk provisioning in the loan business was lower than expected. Consequently, the RoRaC also improved more than expected.

In the capital market business, the prediction of significantly lower net interest income against the background of the portfolio decrease and lower earnings from prepayment penalties was accurate. Special effects from the write-up of Heta receivables and securities led to a significant improvement of the income from securities and participatory interest in particular. Overall, a higher than predicted result and RoRaC above expectations were therefore generated in the capital market business.

From an overall Bank point of view, the predicted result from normal operations was significantly exceeded. This was due on the one hand to the much more favourable risk result in the commercial real estate finance business. On the other hand, results in the capital market business increased considerably due to special effects from the exchange of the Heta receivables and securities.

The development of administrative expenses was also better than expected thanks to good cost management and special effects. The expected CIR development was accurate. Since the operating result was better than expected, the RoE was much higher than predicted.

Overall statement on the course of business and the Bank's situation

Deutsche Hypo generated an extremely good result that was far above expectations in the past financial year. This was due, among other things, to the positive one-time effect of write-ups related to the exchange of the Heta receivables and securities. The highly positive development of the risk result in the commercial real estate finance business was another key driver of this result. Even when adjusting for the described one-time effect and notwithstanding the expected decrease in the interest result, the development of the result was correspondingly very positive. This applies in particular against the background of a significant strengthening of precautionary reserves.

The development of existing and new business is considered positive as well. New business volumes in commercial real estate finance increased considerably compared to the previous year. While portfolios in the commercial real estate finance business only remained constant at the same time, this is merely a delay of the predicted portfolio increase based on the significant increase in the portfolio of irrevocable loan commitments. Meanwhile, the quality of the real estate finance portfolio remained at the previous year's level. The strategic public sector finance portfolio decrease continued in the capital market business. The quality of the portfolio further improved in the course of active portfolio management. On the funding side, the Bank was able to carry out its issuing activities well and as planned.

Against the background of some existing uncertainties regarding external framework conditions, business development in the past financial year is considered highly positive.

Report on subsequent events

There were no events of particular significance that occurred after the end of the financial year and could have a sustained impact on the Bank's net assets, financial or income position.

Forecast, opportunity and risk report

Forecast report

The following section should be read in the context of the remaining sections of this management report. The future-oriented statements in this forecast report are based on estimates and conclusions on the basis of the information that is currently available. These statements are supported by a number of assumptions regarding future events that were included in Deutsche Hypo's corporate planning. There are uncertainties, risks and other factors related to the occurrence of future events, many of which the Bank is unable to influence. Actual events may therefore deviate from the predictions that follow. The assumptions made in the course of planning are described in greater detail in the forecast report.

Developments in past years have shown that the ability to make predictions in a volatile environment is limited. Deutsche Hypo discusses key opportunities and risks for central management in detail in this section. Opportunities are defined here as possible future developments or events that may lead to positive forecast or target deviations for Deutsche Hypo. Risks, on the other hand, are defined for the purpose of the forecast report as possible future developments or events that may lead to negative forecast or target deviations for Deutsche Hypo. Bank-specific risk types are separately explained in the expanded risk report.

Development of business and framework conditions

Forecast for economic development

Germany's economy became noticeably more dynamic by the end of 2016. In view of very high values for economic confidence and consumer sentiment until most recently, solid growth is expected for the first quarter of 2017 as well. The ongoing highly expansive monetary policy of the ECB and moderate energy prices along with a relatively weak external value of the Euro mean the initial conditions for continued growth are good. However, it is not yet possible to assess to what extent political risks could lead to a worsening of sentiments in the course of the year. The outlook for private consumption remains fundamentally positive. Although inflation is increasing considerably due to base effects, NORD/LB expects the rate of inflation to remain below 2.0 % on the annual average. Real wages will therefore continue to increase, but no longer quite as quickly as in previous years. Public consumption should also expand noticeably again. The economic performance in 2017 is expected to increase by a good 1.5 % compared to the previous year.

The economic outlook for the Bank's foreign markets is favourable as well. NORD/LB expects overall GDP growth of more than 1.6 % for the Eurozone overall in 2017 compared to the previous year. The domestic economy remains the most important pillar, in particular private and public consumption. However, significantly higher inflation due to base effects means that the growth of real disposable

income is going to be less dynamic. Further noticeable improvements are expected in the decrease of unemployment while the speed of public finance consolidation is going to be moderate. Progress here is expected to be mainly dependent on market conditions as previously in 2016. However, the forecast is once again subject to significant risks: In addition to the ongoing risk factors of global terrorism and geopolitical trouble spots, political risks in particular have to be mentioned here.

Forecast for the development of the target real estate markets

The attractiveness of global commercial real estate investments will continue in 2017. However, the market environment is more challenging. Political risks are going to have a greater influence on investment decisions going forward. The ongoing high risk of terrorist attacks bears continued uncertainty for world events.

Demand in the European real estate markets is expected to continue developing positively notwithstanding the existing political risks since the ECB's monetary policy course remains decisive for investment decisions in 2017. Demand from cross-border investors for core properties in Europe and yield compression will continue in 2017. Excessively high prices could develop locally. Germany is expected to remain a safe haven for real estate investments.

The favourable fundamental framework conditions in Germany will have a positive impact on the real estate market in 2017 as well. Real estate-specific indicators such as buying power and income are going to move with a tailwind. As a result, the future prospects of the established assets classes fundamentally continue to be stable, with varying developments expected within the asset classes that are important for the Bank. Based on the level that has already been reached, the price trend for core properties is expected to weaken or slow. In fact, the price peak appears to have been fundamentally reached already for retail properties in top locations. On the other hand, growth of around 3 % is once again expected for peak rents in the office property market in German A cities for 2017. Yields should fall again as a result. The residential property market in major cities will also continue to be defined by a supply shortage and accompanying rent and purchase price increases. Continued very high demand for hotel investments is expected as well. Whether another record year will build on the current successful trend remains to be seen. Increased demand for space close to urban centres can be expected in the area of logistics.

Forecast for developments on international financial markets

NORD/LB generally expects interest rates to increase moderately against the background of positive economic signals from the USA and rising inflation in the Eurozone. This should be flanked by the US Federal Reserve that has already begun increasing the prime rate. Further small interest increments are expected here for 2017. On the other hand, despite rising inflation, the ECB is expected to take its time with concrete statements regarding an end to the bond purchase program. These conflicting factors will affect the financial markets overall in 2017. It is already apparent today that the new US government will provide some surprises. This means there is a rather high probability that the markets will be exposed to fluctuations. Forecasting is much more difficult as a result.

Forecast for the development of business with significant opportunities and risks

Significant assumptions in the forecast

Deutsche Hypo's multi-year plan, which is compiled annually, provides the basis for the statements on the earnings forecast. Its foundation consists of economic assumptions, expectations with regard to developments on real estate markets, forecasts on financial market developments and regulatory requirements. On the basis of this, factors such as new business, the development of the portfolios and the resulting margins are planned.

In terms of macroeconomic framework data, planning is based on market mechanisms that are largely fully functional. The prevailing low-interest environment ensures ongoing high liquidity in the markets, which is going to underpin the attractiveness of commercial real estate. For Deutsche Hypo, this means the environment is expected to be stable with strong competition on the lender side and numerous business opportunities. It is assumed that Deutsche Hypo will continue to have access to funding on a sufficient scale and on the basis of standard market conditions at all times.

The income forecast also takes into account Deutsche Hypo's structural and business policy measures for strengthening its position over the long term:

- Utilisation and further development of the structuring competence
- Continuation of the product development business
- Strengthening the acquisition capacities and expansion of further sales initiatives (development of business relationships with new partners and segments)
- Depletion of the public sector finance portfolio with an accompanying reduction of hidden burdens and credit spread risks
- Investments in the organisational and technical infrastructure to realise opportunities in the context of digitalisation and for the implementation of regulatory requirements
- Ongoing constant optimisation of the processes and structures

Existing and new business development in the commercial real estate finance business

Deutsche Hypo will continue to apply high quality standards and appropriate yield criteria in lending. In real estate finance business, Deutsche Hypo once again expects positive new business development in 2017 and, compared to the high level of the previous year, predicts only a minor decrease in the new business volume. A slight increase in the portfolios is expected on the other hand based on the high volume of contracted financing that has not yet been transferred to the portfolio at the end of 2016. Pressure on margin development is expected as well against the background of ongoing intense competition. Deutsche Hypo will address this with the further development of the structuring competence.

Opportunities and risks

It is conceivable that unexpectedly high credit demand in the real estate finance sector may lead to the opportunity for new business considerably above the expectations. This could, for example, be caused by a further perceptible increase in economic growth or also an additional significant interest rate decrease, which would have a positive impact on real estate markets and therefore on credit demand.

Furthermore, higher than expected new business in commercial real estate finance may result from better acquisition performance, for example in the context of various sales initiatives planned for 2017. Higher than expected new business closings are associated with the opportunity of a real estate finance portfolio in excess of the forecast. The opportunity for higher than expected margins may arise from competitive advantages over competitors, for example in the course of structuring or a decrease in overall competition.

On the other hand, there are risks of lower demand for real estate financing due to reduced growth in the real estate markets, caused for example by weakening economic growth or a considerable interest rate increase. Possible uncertainties resulting from the Brexit and the upcoming elections in France and the Netherlands also have to be mentioned in this context. Against the background of the currently volatile market environment, there is an overall risk that further isolation tendencies of some European countries may be realised, leading to negative effects on their real estate markets at least in the medium term and therefore on Deutsche Hypo's planned new business activities. An unexpectedly sharp increase in competition on the lender side is also possible, which could have a corresponding impact on the realisable margins and new business.

Additional opportunities and risks regarding portfolio development are found in the actual extension and unplanned repayment behaviour of the customers.

Income forecast

Deutsche Hypo expects the development of earnings in commercial real estate finance to be stable, in particular based on the previously described new business and portfolio trend. Along with the further depletion of the capital market portfolio and lower revenue from capital employed on the Bank's equity, a slight decrease in earnings will likely be seen at the overall Bank level.

An ongoing favourable risk result in the commercial real estate finance business is expected against the background of assumed stable real estate markets and the ongoing focus on real estate financing of high quality. With the predicted approach to a level that is expected over the long term, the risk result of the past financial year that is considered unusually good is, however, not expected to be reached again in the commercial real estate finance business. Special effects of write-ups in the capital market business like those seen in 2016 are not expected either based on the current state of knowledge.

Administrative expenses are also expected to increase in financial year 2017. This is due to investments to strengthen Deutsche Hypo's brand image and the organisational and technical infrastructure. Opportunities related to digitalisation are to be realised and regulatory requirements will be implemented. Under consideration of these developments, Deutsche Hypo will also continue striving to maintain the cost discipline it has demonstrated in past years.

Accordingly, a solid result is expected overall in 2017. Since no special effects are expected, it will be considerably below the unusually favourable result in the previous year. This result will also be reflected by a significantly lower RoE. The contribution to operating income by the commercial real estate finance business will continue to be the key driver of a good result at the overall bank level.

The expected increase in administrative expenses in 2017 will lead to a significant CIR increase. In the industry comparison, the expected CIR level will nevertheless continue to stand out favourably.

Opportunities and risks

Limited predictability of developments in the capital market business constitutes a key risk regarding the result. Unexpected developments of external economic, geopolitical and industry-specific framework conditions and trends in the international financial markets may have a significant influence on the development of Deutsche Hypo's results. They could drive the worsening of borrower creditworthiness and therefore lead to a need for higher loan loss provisions compared to the forecast. For example, a potential drifting apart of the EU countries could reveal payment difficulties of some capital market customers and lead to higher than planned loan loss provisions. Negative effects from unexpected developments of external framework conditions may result from a worsening of borrower creditworthiness or a reduction in the value of financed assets, also for the risk result in the commercial real estate finance business.

Weaker than planned portfolio and margin developments also bear earnings risks. Furthermore, it is conceivable that the terms for unsecured funding may become more costly and that these costs cannot be passed on within the framework of conditions. The senior unsecured asset class is currently affected by new legal and regulatory framework conditions. Their effect on the behaviour of market participants is difficult to assess. An increase in costs due to a rating downgrade is possible as well.

Furthermore, new regulatory changes may be associated with restrictions and therefore with earnings risks as well as additional administrative expenses. There are also risks due to the Bank's membership in the Sparkassen-Finanzgruppe's institute-specific protection scheme. Special payments could be demanded from the institutes under the protection scheme in the course of compensation and support measures, impacting the Bank's result. This applies correspondingly to possible supplementary payment obligations to the restructuring fund for financial institutions. Whether and in what amount such payments will occur cannot be predicted at this time.

Opportunities for higher than forecast earnings result mainly from a bigger portfolio and/or higher margins in commercial real estate finance. Higher fees also constitute earnings and therefore income opportunities.

It is also conceivable that, given constant or improving economic framework conditions, the risk result in the commercial real estate finance business will be close to as good as in the past financial year, and therefore significantly better than the planning assumptions. The same applies to possible positive effects on the result due to better than expected developments of external framework conditions for the capital market business, which would lead to a better risk result and/or income from securities and participatory interest.

Regarding the development of administrative expenses, there is an opportunity in that investments may lead to lower expenses, thereby increasing the result. Income opportunities arising from regulatory changes, for example in the form of lower banking levies, are considered comparatively unlikely on the other hand.

Effects on the result in the context of negative interest rates or also interest rate changes are considered comparatively minor in terms of both their risk and opportunity potential.

The aforementioned income opportunities and risks also constitute opportunities and risks in regards to the performance indicator RoE.

Regarding the CIR, opportunities mainly result from a positive forecast deviation in reference to costs and earnings. Negative deviations in these result components constitute a risk leading to a less favourable cost/earnings ratio.

Expanded risk report

Risk management

Fundamentals of risk management

Deutsche Hypo made use of the waiver rule in accordance with Art. 7 (1) CRR, formerly Section 2a (1) of the German Banking Act (KWG), in 2013. For this reason, the bank regulatory provisions concerning the requirements for equity on the institute level, the requirements for large exposure notification and the calculation and securing of the risk bearing capacity, the determination of the strategies and the establishment of processes for the identification, assessment, control, monitoring and communication of risks (Section 25a (1) clause 3 no. 1 of the German Banking Act) were transferred to NORD/LB as the parent company.

As a Pfandbrief bank within the meaning of Section 1 of the German Pfandbrief Act (PfandBG), the Bank is subject to the requirements of the PfandBG which set forth in Section 27 a suitable risk management system for the identification, assessment, control and monitoring of all risks connected with the Pfandbrief business. The implementation of existing requirements from the Pfandbrief Act is an integral part of the existing risk management and requires the control of the counterparty, market price and liquidity risks on the level of the cover pools.

Deutsche Hypo has implemented, on the one hand, an inter-divisional risk management process and is included, on the other, in the risk management process of the NORD/LB Group. The risk management process at Deutsche Hypo includes identifying, assessing, reporting, managing and monitoring risk and is subject to continual review and refinement.

As a material subsidiary of the NORD/LB Group from a risk point of view, Deutsche Hypo has implemented a risk organisation that meets the risk strategy principles on both the level of the individual institute and at the Group level.

Risk management – strategies and goals

The strategic orientation of the NORD/LB Group is determined in compliance with Section 25a (1) of the German Banking Act (KWG), among others, on the basis of a consistent compendium of strategies. This is based on all the significant (in terms of risk) subordinate companies of the NORD/LB Group and thus Deutsche Hypo. Deutsche Hypo prepares an institute-specific, concrete and consistent risk strategy for the Group risk strategy and for the business and IT strategy of the Bank, which is oriented

to the overall risk profile. Independently of the regulatory requirements, Deutsche Hypo attaches great importance to an appropriate risk management system from a business perspective and such a system is anchored in its corporate culture.

In 2016, the risk strategy was overhauled as usual. At the same time, compliance with the existing risk strategy requirements was checked. In this connection, it was discovered that the risk strategy goals were complied with.

Risk management – structure and organisation

The risk organisation of Deutsche Hypo corresponds to the risk-strategic goals and includes an efficient risk management process with clearly defined responsibilities and competencies. Furthermore, there is an established organisational separation between the market and risk management function up to and including the level of management.

The Board of Managing Directors sets framework conditions, jurisdictions and risk tolerances for the main types of risks and is responsible for the design of the risk strategy and the effective implementation of the risk management. The Board of Managing Directors is advised and monitored by the Supervisory Board. At the same time, the Supervisory Board is directly included in decisions that are of major significance for Deutsche Hypo.

The risk management process is supported by an adequate IT infrastructure and an appropriate team of qualified employees, ensuring systematic interaction between involved divisions and smooth processes. The risk-related organisational structure and the functions, roles and powers of the areas of the Bank involved in the risk processes are clearly defined down to the level of individual employees.

On the level of NORD/LB as the parent institution, boards have been established for handling the risk management process and exercising the consulting, monitoring, control and coordination functions. This involves, among others, the Erweiterter Konzernvorstand (Extended Group Board of Managing Directors), the Konzernsteuerungskreise (Group Control Committee) and the Group Risk Committee. Due to the integration of Deutsche Hypo in the risk management process on the group level, the results of the previously mentioned boards have an impact on Deutsche Hypo. Deutsche Hypo is included by sending representatives to these boards. Furthermore, there are the Method Board for Risk Management and various working groups on the level of the NORD/LB Group. Deutsche Hypo is also represented on this Method Board and in the working groups.

The process-independent review of the effectiveness and appropriateness of risk management is carried out by Deutsche Hypo's Internal Audit department. On account of the outsourcing of significant responsibilities in Internal Audit to NORD/LB, Deutsche Hypo's Internal Audit is represented by an audit officer who bears responsibility for proper internal audit.

With regard to activities in new products or new markets, a "New Product Process" (NPP) is in place throughout Deutsche Hypo. As a standard process, the NPP regulates the development of new products and the approach taken to new markets, new sales channels and new services. The early identification of risks, the appropriate assessment of their impact on the overall risk profile of the Bank and the determination of reasonable measures to manage the risks take precedence. After the successful conclusion of the NPP, it is possible to include the product in running business operations.

Over the course of time, the framework conditions considered in the NPP can change and have an impact on the proper handling of the product without this leading directly to a case-by-case product review. For this reason, a product review is carried out annually, on the basis of the current product catalogue, for all products permitted for running business operation.

Risk management – reporting

The quarterly risk report on different types of risk is a central report for the Board of Managing Directors and the Supervisory Board. It provides a complete and comprehensive overview of the risk situation at Deutsche Hypo. Furthermore, the Board of Managing Directors is informed at various intervals (daily to quarterly, depending on the requirements) about the situation in major types of risks for the Bank. Besides these regular reports, the Board of Managing Directors and – depending on the severity of the event – the Supervisory Board also receive ad-hoc information in the case of material events.

Management of risks affecting cover pool

The goal of the risk management system is to control the counterparty, market price and liquidity risks on the level of the cover pools, to ensure high quality standards for the cover assets of public Pfandbriefe and the high security of the collateral in the mortgage business. That ensures a stable and cost-affordable funding basis by achieving a high quality rating for the Pfandbriefe from rating agencies, thereby securing the long-term value and the profitability of the Bank.

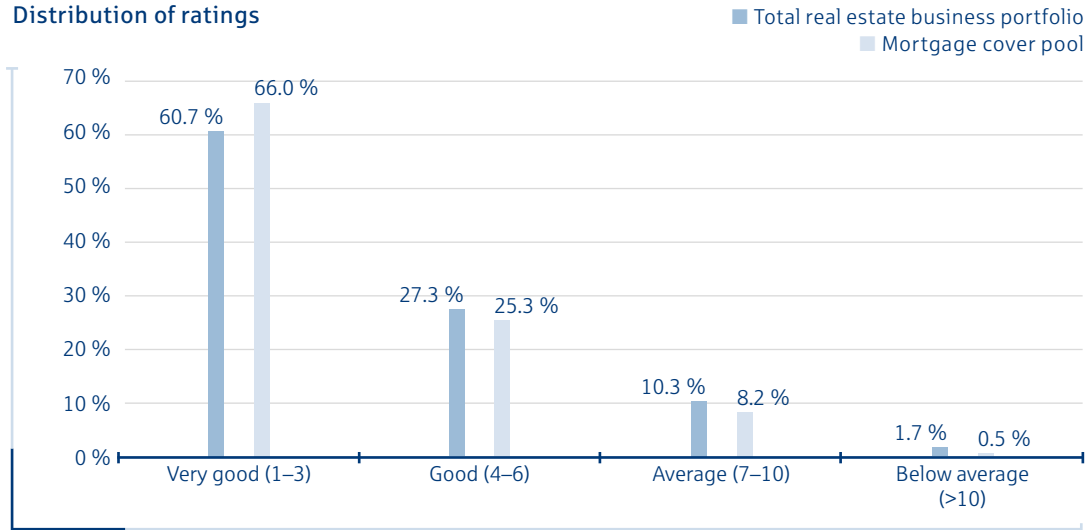
Besides permanent compliance with the cover principles and the permanent ensuring of sufficient cash coverage (Section 4 (1) of the German Pfandbrief Act) and the ensuring of the liquidity over the next 180 days (Section 4 (1a) of the German Pfandbrief Act), the Bank regularly analyses the quality and the value of the loan receivables used as the cover portfolio. This includes internal rating processes, the analysis of external ratings and the regular monitoring of the performance of the real estate serving as collateral.

To comply with the requirements of the transparency provision in Section 28 of the German Pfandbrief Act, Deutsche Hypo publishes the appropriate information in the notes to the financial statements and – together with the historical values – on the Bank's website.

Cover pool of mortgage Pfandbriefe

The proportion of good and very good credit ratings in the mortgage cover pool amounted to 91.3 % as of 31 December 2016 (2015: 90.1 %). In terms of the total real estate business portfolio, this share was 88.0 % (2015: 85.8 %). The distribution of ratings in the mortgage cover pool reflects the good quality of the Pfandbriefe.

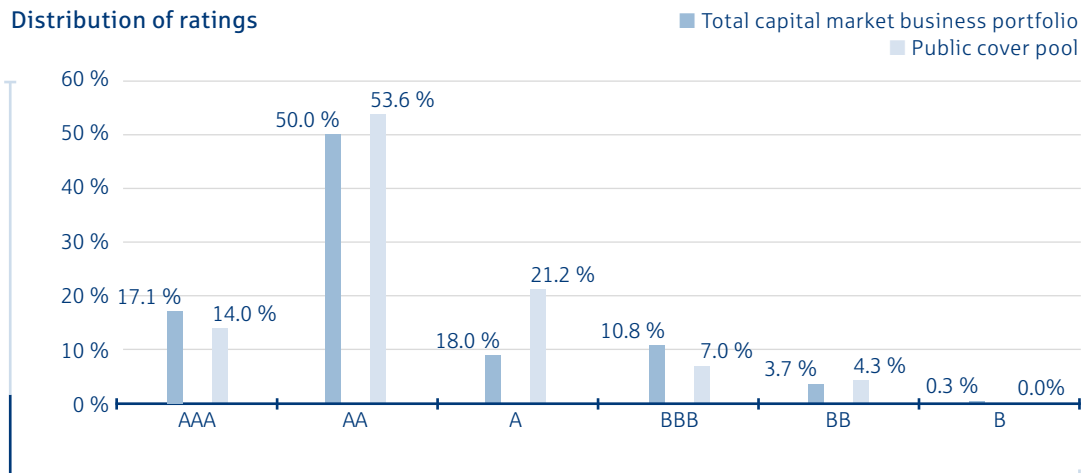
Distribution of ratings



Cover pool for public Pfandbriefe

The share of loans with a very good rating of AAA or AA in the cover pool of public Pfandbriefe was 67.6 % as of 31 December 2016 (2015: 69.0 %). The average rating in the cover pool amounted to AA- and signals the high quality of the cover pool for issued Pfandbriefe.

Distribution of ratings



Risk management – risk bearing capacity

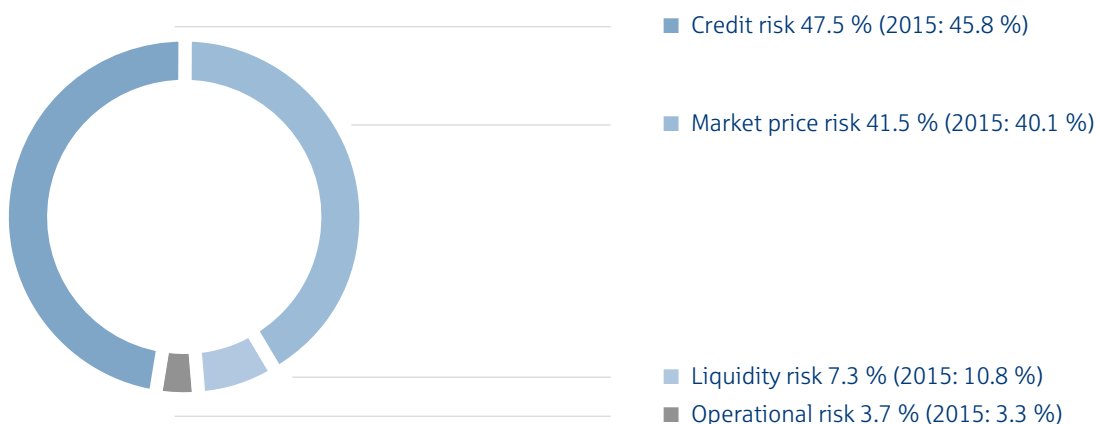
The risk bearing capacity (RBC) of Deutsche Hypo is monitored on the level of the NORD/LB Group due to the exercising of the simplification rules under Section 2a (1) of the German Banking Act or Art. 7 CRR. The RBC model of the NORD/LB Group consists of three levels of analysis: the going concern (authoritative level of analysis for evaluating the risk bearing capacity), gone concern (secondary condition) and regulatory (strict secondary condition) in which the significant risks (risk potential) are viewed in each case in relation to the defined risk capital of the individual bank or the Group. Deutsche Hypo supplies the required information that is consolidated within the scope of the risk bearing capacity calculation of NORD/LB for the Group. The risk bearing capacity of the NORD/LB Group was met as of 31 December 2016. The securing of the risk bearing capacity on the Group level is supported by the use of institute limits for the significant types of risk at Deutsche Hypo. These limits are set by the NORD/LB Group. While compliance with the institute limits assumes a place of particularly high strategic relevance for Deutsche Hypo, they represent an early warning instrument from the perspective of the NORD/LB Group. Corresponding escalation mechanisms have been established for the exceeding of limits.

The monitoring of limits entails that the risk potential for the major risk types is calculated quarterly according to the uniform Group methodology and compared to the respective limits for the Bank. The risk potential is fundamentally based on a value-at-risk approach with a confidence level of 95 % (going concern) and a confidence level of 99.9 % (gone concern), each with a holding period of 250 trading days.

Current developments

The year 2016 was largely characterised by positive sentiment on the relevant money and capital markets, and the low level of interest rates. The low level of interest rates and stable real estate markets, together with ongoing quality-oriented lending policies, contributed to reduced risk in the real estate finance portfolio. Maturities, the narrowing of spreads and the disposal of individual items in the capital market business led to a significant decline in exposure and hidden charges. The risk potential in the going concern (confidence level of 95 %, time horizon of fundamentally 1 year) from the significant risk types was as follows on 31 December 2016:

Composition of risk potential from the significant risk types in the going concern as of 31.12.2016



The level of risk potential overall did not change significantly compared to the previous year.

Counterparty risk

Deutsche Hypo's counterparty risk consists of the credit risk, including the country risk. The financial investment risk does not have any strategic meaning and is insignificant as a result. The credit risk refers in general to the possibility that a loss may be incurred that is not covered by securities as a result of an external counterparty defaulting or suffering a deterioration in creditworthiness. As well as the classic default risk, collateral risk is a further component of credit risk. This is understood as the risk that it might not be possible to recover the assumed fair values of loan collateral in the event of realisation. The counterparty risk is also assigned to the credit risk and includes the risk that if a contractual party defaults it might no longer be possible to collect an as yet unrealised gain from pending transactions (replacement risk) or that, in the case of a transaction requiring contemporaneous performance, the instance of a counterparty defaulting might mean that the counter-performance can no longer be fulfilled (performance risk).

Another component of the credit risk in the case of cross border transactions can be the related sovereign risk. This is the risk that state-imposed obstacles (transfer risk) could prevent repayment despite the individual borrower being able and willing to make a payment.

Counterparty risk – goals and strategies

Credit risks are handled on the basis of the Bank's risk strategy for credit which, in turn, is part of the overall risk strategy. Deutsche Hypo's aim is to achieve a competitive level of profitability and take into account efficiency and flexibility in terms of active management of the credit risk items in order to minimise the unanticipated losses. Lending operations and controlling credit risk are a core competency at Deutsche Hypo, and one that is permanently being developed and expanded.

In accordance with the part of the risk strategy for credit risks, the focus in the new credit business is on lending to borrowers with a good credit rating and securities in the form of senior mortgages for the amount of the financing for the property. In the capital market business, Deutsche Hypo also concentrates on doing business with good counterparties with a minimum rating of investment grade, but on average "A" or with a comparable rating. Deutsche Hypo only pursued business with customers and counterparties that lie outside of the aforesaid credit rating focus after careful consideration of the opportunities and risks.

Furthermore, no individual credit exposure should reach an order of magnitude that can significantly compromise the economic stability of the Bank. For the early identification and reduction of credit risks, the Bank identifies all borrowers and counterparties that exhibit an elevated level of risk in an early warning process defined for this purpose.

In order to meet the specific requirements for each business area, the Bank has drawn up financing principles that take the form of binding guidelines for new business for the Bank in the strategic business area that was classified as relevant for risk. The risk-related assessment of the commitments was handled on the basis of a procedure specifically developed for the business areas (e.g. rating module).

Counterparty risk – structure and organisation

All the organisational structures derived from the framework conditions and the processing procedures are included in the written policy of Deutsche Hypo. The credit-risk-related organisational structure and the functions, responsibilities and competencies of the divisions involved in the risk processes are clearly defined down to the level of individual employees. The processes in the credit business are characterised by a clear structural and organisational separation of the market division and the back office division up to and including the level of management. In the back office division, there is a separation between the credit risk controlling, the credit risk management and the special credits management.

Credit decisions as defined in MaRisk are all decisions on new loans, loan increases, loan takeovers, loan extensions and significant changes to risk-relevant properties of loans. Loan decisions are always made by two authorised employees or, for specific sizes of loans, by decision-making committees (e.g. the full Board of Managing Directors). One person is always from the market division and one person from the back office division. The authorised employees responsible for making the decision must be on the same functional or hierarchical level as each other. The market division has no authority to approve credit on its own.

Before the loan decision is made by the responsible employee, two additional votes, namely one vote from the market division and one from the back office division must first be present. The responsibility of the authorised employees is basically based around the total commitment of the group of affiliated customers in accordance with Art. 4 (39) CRR to which the customer is to be allocated and around the rating class as determined in the credit review. This ensures that the basis of the loan decision is not simply the amount of the requested loan. Rather, the risk potential inherent in the total commitment is taken into account.

Counterparty risk – controlling and monitoring

Deutsche Hypo's credit risk is controlled and monitored primarily through the stipulation of financial principles, the limit system and the rating system. The Bank also operates a portfolio management for the optimisation of the income and risk structure. As portfolio-improving measures, not only a controlling of the new business, but also placements through syndication, direct sales of receivables or the divestiture of problematic exposures can be considered on a case-by-case basis. Additionally, hedging transactions in the form of cash collateral guarantees for the takeover of mezzanine risks exist in the underlying portfolio. In the reporting year, the Bank supplemented one of the existing transactions. Future new business may also be included in the hedging transaction in the scope of a replenishment period to 2018. The total value of the guarantees included is € 77.3 million (2015: € 61.5 million).

Financing principles

The financing principles are an instrument in the risk management and must be applied by all the institutions affiliated with the Group. The financing principles are set ex ante by the back office division and the market division, and should at least meet the expectations for potential business. The financing principles document the uniform, Bank-internal understanding of the necessary benchmarks for starting business and contracting in a certain market area. They are intended for effective pre-selection and do not anticipate definitive decisions in individual cases. The annually checked financing principles are reviewed by the respective analysts by means of a check list.

For Deutsche Hypo, the following criteria apply as a minimum risk standard in the real estate finance business. In the event of non-compliance, the next higher competency level must be included in the back office:

- The redemption structures and the loan maturities ensure the redemption of the loans within the remaining term of the financed real estate.
- The real estate and the overwhelming share of the portfolio in the case of apartment portfolios are inspected by a Bank employee or an expert hired by the Bank prior to the credit decision.
- The financing must run off within the market values upon the initial decision with due regard for the mitigants and/or additional securities.
- On the part of the borrower, it is usually necessary to contribute an appropriate amount of equity in the form of cash and/or individual performance of 20 % of the total cost (orientation amount) in advance. A substitute in the form of perfect (in terms of credit rating) co-liability conditions/recoverable guarantees/recoverable additional collateral is possible.

The focus is on the property types of office, retail and shopping centre, multi-family homes and properties with a mix of the aforementioned types of use and on hotel and logistics real estate.

Limit system

Deutsche Hypo is included in the limit systems for risk concentrations of the NORD/LB Group as part of strategic limiting. There are limits on the concentration of counterparty, country and sector risks. This system combines, monitors and controls all the counterparty risk concentrations in the Group. The Group-wide binding limits are considered. Deutsche Hypo supplies the information required for this and, in turn, is informed about Group-wide concentrations of risk with regard to its own borrowers. If the limits are exceeded, uniform Group rules for the monitoring and reduction of the affected unit shall apply. In this case, there are various limits for each business area at Deutsche Hypo. The limiting of risk is handled on the level of the country risk, sector risks and on the basis of individual risk bearers all the way to limiting the risk on an individual mortgage property. In order to avoid concentrations of risk at the borrower level, limits are in place for economic units that extend beyond the rules for borrower units (borrower unit in terms of Section 19 (2) of the German Banking Act (KWG) and the group of affiliated customers in terms of Article 4 CRR). The actual form of the limits for real estate areas is governed in the Bank's guidelines.

Rating system

The rating system calculates a rating score for each borrower, expressing the individual probability of default over the next 12-month period. This is then updated as part of the annual credit rating assessment and any assessment carried out following a particular occurrence. The rating modules in use were developed as part of cooperation projects involving the savings bank group and the Landesbanks. The assessment of the credit rating of customers in combination with a risk-adjusted pricing of the loan leads to the compensation of the expected losses.

Treatment of conspicuous exposures

The use of sophisticated credit rating assessment processes cannot prevent the credit ratings of individual borrowers from deteriorating over time. Exposures are monitored using early warning criteria and, where anomalies are identified, are included in the early warning list. The early warning list fundamentally includes all the claims that do not develop in accordance with the plan at the time of the original credit decision and represent an elevated risk that requires special credit monitoring.

Exposures in certain risk classes are transferred to Special Credit Management and can be assumed by this department (drawing right). The goal is proactive avoidance or reduction of potential capital losses. This department is responsible for having an influence early on and introducing a restructuring process in order to ensure the servicing of the contractually agreed interest and capital payments or to develop and implement alternative options for action. If there is no longer any ability to restructure, an effort is made to optimise the income from the collateral in the case of unwinding. The Special Credit Management is also the centre of competence for risk provisioning and has to ensure a reasonable measurement of the risk provision at all times. In order to ensure the latter, the Special Credit Management Department sets the amount of the risk provisioning within the scope of the competency rules.

The early identification of crisis situations forms the basis for the risk-conscious and efficient control of credit risks. For this reason, Deutsche Hypo has a series of processes, systems and requirements that represent a system for the early identification of various risks in combination and facilitates the systematic controlling and early introduction of measures for their limiting.

Framework conditions for the credit business with the public sector and banks

The general procedures and methods described above for controlling and managing credit risk also apply to the credit business conducted with public institutions and banks. In addition to counterparty limits, the limit system also comprises limits for business type (capital market, money market, derivatives, repo transaction performance risks) and sub-limits for individual countries. A minimum rating of A (or comparable internal rating) remains the general requirement for all new business. As a general rule, Deutsche Hypo only enters into derivative transactions with suitable bank partners that meet the high credit rating requirements. Deutsche Hypo also enters into collateral arrangements, which secure the counterparty risk.

Counterparty risk – collateral

Deutsche Hypo accepts collateral in order to reduce its credit risk. With regard to area of commercial real estate finance, loans are generally secured by means of a mortgage in the amount of the loan. In exceptional cases, mortgage collateral can be omitted. A requirement for this is a good credit rating and the observance of the limit for financing not collateralised by mortgages.

The value of the property and thus the value of the related securities are monitored on a regular basis, generally at least annually. If there have been any influential factors that are of relevance to the value of the security, a revaluation must be carried out. Deutsche Hypo's credit guidelines and lending principles set out definitions of the basic types of securities and properties being mortgaged that may be used as collateral, and the maximum share of the value of the collateral or of the financed property that can be lent. Both the fair value and the lending value calculated in accordance with the strict provisions of the German Regulation on the Determination of Mortgage Lending Value (BelWertV) are applied. The latter has a direct impact on the eligibility as cover of the loan and thus influences the volume of the collateral pool available as security for Pfandbriefe issued by Deutsche Hypo, in accordance with the terms of the Pfandbrief Act (PfandBG). Mortgages, guarantees and similar collateral, assignments of claims and other rights, liens on property, claims and other rights and transfers of ownership as security are all basically accepted as loan security. Only mortgage liens and guarantees from suitable credit institutes and liquid funds provided as collateral are taken into account for the purposes of risk assessment in the loan portfolio and the easing of capital requirements as stipulated in the CRR.

Counterparty risk – measurement

The direct quantification of the credit risk takes place for the Bank on the one hand on the level of the NORD/LB Group and on the other on the level of the individual institute of Deutsche Hypo. The explanations below on the measurement of the credit risk include the general description of the methods and processes that are used on the level of NORD/LB for the measurement of the credit risk. Credit risk is measured using the risk key figures of expected loss and unexpected loss. These are calculated on the basis of the probability of default that is determined from the rating scores and the anticipated loss amount per loan, taking account of any collateral. The expected loss is the expected defaults in the loan portfolio over the next twelve months. To cover expected losses, the Bank collects a risk premium as part of its margin. The amount of this premium for each individual loan depends on the rating or probability of default and on the expected loss ratio. The unexpected loss for the credit risk is quantified using an economic credit risk model for different confidence levels and a time horizon of one year. The credit risk model used by the NORD/LB Group incorporates correlations and concentrations into the risk assessment. The credit risk model calculates the unexpected loss at the level of the portfolio as a whole. Incorporated into these calculations are the probability of default (PD) and loss given default (LGD) ratio calculated using internal ratings and determined for each individual transaction taking the security situation into account.

The credit risk model can be used to study sub-portfolios and their share of the unexpected loss. Such analysis also has a direct impact on the fundamental structure of the limit system and on the setting of specific individual limits. In this way, it is possible to manage risk concentrations in the portfolio appropriately. Deutsche Hypo uses the internal ratings based approach (IRBA) to calculate the regulatory capital backing required for credit risks pursuant to the CRR.

In addition, scenario calculations for the individual institute's portfolio in the form of stress test analyses are performed. The design of the Group-wide stress scenario and its ongoing monitoring take place with the inclusion of Deutsche Hypo. Authoritative stress is a serious recession. This case is calculated quarterly by the Group, and the results are then placed at the disposal of Deutsche Hypo for its own analysis on the level of the individual exposure. This makes it possible to carry out a risk-causing assignment of the credit risk potential to the business areas. The sensitivity analyses can be used as early warning instruments.

Counterparty risk – reporting

This quarterly risk report also includes the credit risk sub-report. It contains a summary and analysis of all material structural characteristics and parameters that are of relevance to the controlling of the credit portfolio. Furthermore, a portfolio report for the Board of Managing Directors is prepared on the portfolio of problematic exposures for the real estate finance and capital market business. In addition, there are quarterly reports on the monitoring of project developments, syndication and monthly reports on conspicuous exposures as part of the early warning system and on the development of the risk provisioning.

Counterparty risk – analysis of the credit exposure

The credit exposure, a key reference indicator in credit risk controlling, represents the quantification of all risk-encumbered transactions. Its calculation is based on drawdowns – at nominal value in the case of guarantees or carrying amount in the case of securities, or on the credit equivalent amounts of derivatives, including add-ons and taking account of netting agreements. Irrevocable credit commitments are usually included in the credit exposure at 75 %. Irrevocable credit commitments or internal credit lines are not

taken into account. As part of the internal reporting process, the Board of Managing Directors and the Supervisory Board are kept informed at all times of the development and analysis of the credit exposure.

Deutsche Hypo's credit exposure as of 31 December 2016 was € 27,368.1 million, down € 1,363.4 million as compared to the end of 2015. Volume increased by € 422.8 million to € 13,680.0 million in the commercial real estate financing business. Credit exposure to loans to local authorities fell significantly, by € 776.1 million, to € 4,827.1 million, in accordance with the reduction of the portfolio as planned in the strategic focus. There was an overall decline of € 1,010.3 million in the portfolio of securities and derivatives and in the other financing products. This development reflects the business policy of the Bank, which aims to turn the Bank into a pure real estate finance bank.

The focus of the credit exposure continued to be on the very good to good IFD classes. This classification corresponds to the standard IFD ratings scale as agreed on by the banks, Sparkassen and associations that together form the Initiative Finanzstandort Deutschland (IFD). The aim of this scale is to make it easier to compare the ratings awarded by individual credit institutions. The rating classes of the 18-level DSGV rating master scale used throughout Deutsche Hypo can be translated directly into the IFD classes. The proportion of total exposures in the rating class "very good to good" was 81.5 %, which was almost unchanged from the good level of 81.8 % in 2015. The reason was the high shares of exposure to governments, public authorities and financial institutes that have a good credit rating and other improvements in the real estate finance area.

The share of non-performing loans (NPL) fell from 1.5 % to 0.8 % of total exposure. The absolute volume fell by € 203.0 million to € 228.9 million.

In the following, the breakdown of the credit exposure by rating categories is described in table form. The hedging transactions completed for the purpose of active RWA control in recent years were for the credit portfolios in commercial real estate finance and involved cash-covered guarantees.

Breakdown of total credit exposure by rating category

31.12.2016 in € millions	Real estate finance	Loans to local authorities	Securities	Deriva- tives	Other	Total exposure	Share in total exposure
Very good to good	9,404.4	4,775.1	6,118.5	1,420.5	596.2	22,314.7	81.5 %
Good / satisfactory	2,667.9	0.2	265.8	0.0	0.0	2,933.8	10.7 %
Still good / sufficient	1,037.9	51.8	190.2	0.0	75.1	1,355.0	5.0 %
Elevated risk	344.3	0.0	149.7	0.0	6.0	500.0	1.8 %
High risk	19.0	0.0	2.9	0.0	0.0	21.9	0.1 %
Very high risk	13.8	0.0	0.0	0.0	0.0	13.8	0.1 %
Default (=NPL)	192.8	0.0	0.0	36.1	0.0	228.9	0.8 %
Total	13,680	4,827.1	6,727.0	1,456.6	677.3	27,368.1	100.0 %

31.12.2015 in € millions	Real estate finance	Loans to local authorities	Securities	Deriva- tives	Other	Total exposure	Share in total exposure
Very good to good	9,326.3	5,508.5	6,038.5	1,485.0	1,154.2	23,512.6	81.8 %
Good / satisfactory	2,018.1	0.3	444.1	0.0	0.8	2,463.2	8.6 %
Still good / sufficient	1,151.2	1.3	331.9	0.0	151.7	1,636.1	5.7 %
Elevated risk	417.3	51.2	118.9	0.0	0.0	587.4	2.0 %
High risk	35.2	0.0	3.4	34.8	0.0	73.4	0.3 %
Very high risk	27.1	0.0	0.0	0.0	0.0	27.1	0.1 %
Default (=NPL)	282.0	41.9	108.0	0.0	0.0	431.9	1.5 %
Total	13,257.2	5,603.2	7,044.7	1,519.8	1,306.7	28,731.5	100.0 %

The Bank's credit exposure in the real estate finance business amounted to roughly € 13,680.0 million at year end (2015: € 13,257.2 million), and 95.8 % of it (2015: 94.2 %) consisted of financing for customers that have a rating of at least satisfactory. As a result of the ongoing improvement, NPLs totalled 1.4 % of the total loan exposure, after being 2.1 % in 2015. The overwhelming majority of the NPL portfolio was filled by foreign financing, largely in the Netherlands and Spain. In total, the development of the NPL exposure showed that the level had again fallen below the long-term average that was observed before the crisis.

Breakdown of the total credit exposure by class and region

31.12.2016 in € millions	Real estate finance	Loans to local authorities	Securities	Deriva- tives	Other	Total exposure	Share in total exposure
Eurozone	11,639.7	4,748.2	5,365.1	1,012.6	637.9	23,403.4	85.5 %
<i>of which, Germany</i>	8,418.9	3,422.5	2,180.1	297.9	616.3	14,935.6	54.6 %
Other EU	1,737.0	8.2	321.6	33.3	0.0	2,100.1	7.7 %
Other Europe	0.0	70.7	50.6	58.5	0.0	179.7	0.7 %
North America	303.3	0.0	721.3	352.2	7.4	1,384.2	5.1 %
Central America	0.0	0.0	0.0	0.0	0.0	0.0	0.0 %
Middle East / Africa	0.0	0.0	0.0	0.0	0.0	0.0	0.0 %
Asia	0.0	0.0	262.7	0.0	0.0	262.7	1.0 %
Other	0.0	0.0	5.9	0.0	32.1	38.0	0.1 %
Total	13,680.0	4,827.1	6,727.0	1,456.6	677.3	27,368.1	100.0 %

31.12.2015 in € millions	Real estate finance	Loans to local authorities	Securities	Deriva- tives	Other	Total exposure	Share in total exposure
Eurozone	10,969.5	5,424.8	5,733.4	1,017.7	1,236.6	24,382.0	84.9 %
<i>of which, Germany</i>	8,209.9	4,049.2	2,284.0	266.4	1,109.2	15,918.7	55.4 %
Other EU	1,996.5	8.2	295.3	38.9	0.0	2,338.9	8.1 %
Other Europe	0.0	170.2	50.6	30.8	0.0	251.6	0.9 %
North America	291.2	0.0	697.5	432.3	32.2	1,453.2	5.1 %
Central America	0.0	0.0	0.0	0.0	0.0	0.0	0.0 %
Middle East / Africa	0.0	0.0	0.0	0.0	0.0	0.0	0.0 %
Asia	0.0	0.0	261.1	0.0	0.0	261.1	0.9 %
Other	0.0	0.0	6.8	0.0	37.9	44.7	0.2 %
Total	13,257.2	5,603.2	7,044.7	1,519.8	1,306.7	28,731.5	100.0 %

The breakdown of the credit exposure by classes and regions shows that 93.9 % (2015: 93.9 %) of the entire exposure is in Europe. The credit exposure in Germany as a percentage of all exposure decreased slightly to 54.6 % (2015: 55.4 %).

The Bank's exposure to countries referred to as the PIIGS countries decreased significantly to € 1,882.4 million (2015: € 2,189.6 million). This included the use of credit plus full inclusion of existing payout obligations. The Bank's aforementioned exposure to the PIIGS countries did not include the existing real estate finance business in these countries with a volume of € 227.9 million (2015: € 183.7 million). The exposure was distributed with € 1,182.6 million (2015: € 1,306.3 million) for governments, public authorities and municipalities, and € 699.8 million (2015: € 883.3 million) for banks and other institutions. Portugal accounted for € 198.7 million (2015: € 197.9 million), Ireland for € 217.3 million (2015: € 212.3 million),

Italy for € 760.1 million (2015: € 878.1 million), Spain for € 706.3 million (2015: € 901.4 million). In the case of receivables from Italian public debtors, the Bank was able to run-off securities as planned and use available market opportunities to correct overweightings. In Spain the exposure to companies totalled € 288.4 million (2015: € 376.0 million), to public debtors € 110.2 million (2015: € 118.1 million), to banks € 307.7 million (2015: € 407.3 million).

Currently, Deutsche Hypo does not see any acute risk of default. Nonetheless, the exposure to the PIIGS countries and other financing is a permanent focus of risk monitoring. The strategic orientation continues to envisage the planned phase out. If developments go as planned, by 2018 the portfolio will have decreased by more than half.

Non-performing loans

Where there are objective indications of acute default risks affecting the balance-sheet credit business, Deutsche Hypo establishes specific loan loss provisions. The write-down requirement is based on an analysis of the expected interest and principal payments and the proceeds from the realisation of collateral, and also on the extent to which claims can be serviced. Risk provisioning for off-balance-sheet business (guarantees, credit commitments and loan collateral) is carried out by creating a provision for risks from the credit business. Any claims that cannot be recovered and for which there are no specific loan loss provisions are written off directly. Incoming payments toward written-down claims are recorded in the income statement.

The total loan loss provisions and provisions for the commercial real estate finance business fell compared to the previous year, to € 77.2 million (2015: € 109.1 million). This amount was attributable to the countries of the Eurozone and North America. Of the overall NPL portfolio exposure of € 228.9 million (2015: € 431.9 million), € 153.7 million (2015: € 288.3 million) related to impaired loans in the core divisions, while € 36.1 million (2015: € 108.0 million) related to impaired transactions in the capital market business. The amount of loan loss provisions and provisions as a percentage of the total credit exposure as of 31 December 2016 was 0.28 % (2015: 0.38 %). The portfolio of overdue, unimpaired credits rose slightly year on year to € 39.0 million (2015: € 35.6 million). The period of default for this credit exposure was less than 90 days. The overdue or impaired loans are secured by standard collateral, which is valued using the applicable lending principles.

Counterparty risk – outlook

The positive development on real estate markets also continued in 2016. The Bank assumes that this will not change in 2017 and therefore expects risk provisioning corresponding to the long-term average as required for this business area.

Even if the capital market was largely attractive in 2016, it cannot be ruled out entirely that individual capital market counterparties could face payment difficulties. Depending on the specific general conditions of the individual countries and their public authorities, this can lead to substantially different developments with regard to country-specific credit risks. Deutsche Hypo will monitor the performance of real estate and capital markets attentively and take suitable measures, if need be.

Market price risk

Market price risk refers to the potential losses that could be incurred following changes in the market parameters.

Market price risk – goals and strategies

Deutsche Hypo does not currently have a trading book in accordance with Article 4 (86) CRR. The Bank also does not currently plan to engage in trading book activities in the future. In accordance with its strategic focus, the assumption of market price risks is of secondary importance. Overall, the market price risk in the going concern primarily arises from interest risks in euros, the majority of which are from the investment of the perpetually available equity and thus not from the operating activity of the Bank. Deutsche Hypo's positioning in the money, currency and capital markets is primarily based on the needs of customers, and the support of the market divisions and overall Bank management. The requirements of the risk strategy, and the importance and size of the bank are taken into account here. Further opportunistic positioning – particularly with the goal of achieving the short-term realisation of speculative profits – is not pursued and is also not planned.

To reduce credit spread risks, Deutsche Hypo has been pursuing the strategy of successively reducing the existing capital market portfolio to protect the income statement for some years now.

Market price risk – structure and organisation

Against the background of the risk-related organisational structure, diverse divisions are involved in the management of market price risks. The controlling of the strategic market price risk banking book positions is handled by the Bank's Asset-Liability Committee (ALCO) and the operative implementation by Treasury. In the context of the requirements laid down by ALCO and in accordance with the market price risks and counterparty limits as well as the risk strategy requirements, Treasury decides on and manages the business activities in the capital market business. The ensuring of the correctness of the transaction data in the data processing systems and the proper processing of the financial market business is handled by the Treasury Operations in the market price risk management process. Controlling is responsible for the tasks involved with risk assessment, the controlling and monitoring process and the reporting. Controlling and Treasury Operations are functionally and organisationally independent of Treasury.

Market price risk – controlling and monitoring

A major component of the monitoring process is the audit of compliance with the pre-set limits and early identification of risks, e.g. through traffic light systems or P&L analyses. Escalation processes are implemented for violations of the limit. In addition to compliance with the already described institute limits, other institute-individual limits are used for market price risks that may refer both to economic and to balance sheet positions. The limits for market price risks are measured such that the support of the customer business and the liquidity management are ensured through the business strategy. The limits also cover the risks resulting from the investment of equity. Furthermore, the impact of stress tests is analysed regularly.

The value-at-risk (VaR) figures are calculated on the basis of an historical simulation process. The portfolio is valued on the basis of the historical changes in the market price. VaR figures are calculated for interest rate risks. In addition, the VaR performance indicators for the risk of a change in interest rates are calculated with due regard for credit spread risks in the banking book. Furthermore, interest rate shocks (+/- 100 BP) are monitored daily.

The management of currency risks is primarily handled by limiting currency profits/losses in the income statement in accordance with the German Commercial Code. To achieve these goals, the open nominal overhangs per currency are closely controlled. Compliance with the aforementioned limits is monitored daily.

To control or reduce risks, positions are hedged in order to counter the impact of disadvantageous market movements (e.g. in interest rates or currency exchange rates) concerning the Bank's own positions. Primarily derivatives such as interest and currency swaps as well as forwards are used as hedging instruments. Additional information regarding hedging and the reporting of hedging relationships in the balance sheet is provided in the notes to the financial statements.

Market price risk – reporting

The quarterly risk report includes a partial report on the market price risk, which includes all the important information on the strategic controlling of the market price risks.

Furthermore, the Board of Managing Directors is briefed on a daily basis on interest rate risks, income from the Bank's interest maturity transformation, and risk concentrations relating to individual currencies and maturities. In addition, there is daily reporting on the credit spread risks in the banking book. Daily reports on foreign currency risks are also sent to Treasury. The hidden charges in the banking book are calculated and reported on at least quarterly.

Market price risk – developments and outlook

The development of the risk of a change in interest rates at Deutsche Hypo was on a moderate level in the year under review, as expected. The very low, partially negative interest rates observed on markets had a negligent impact on the Bank's income and risk position due to the business model. The following table shows the development of the Bank's market price risks in comparison to the previous year:

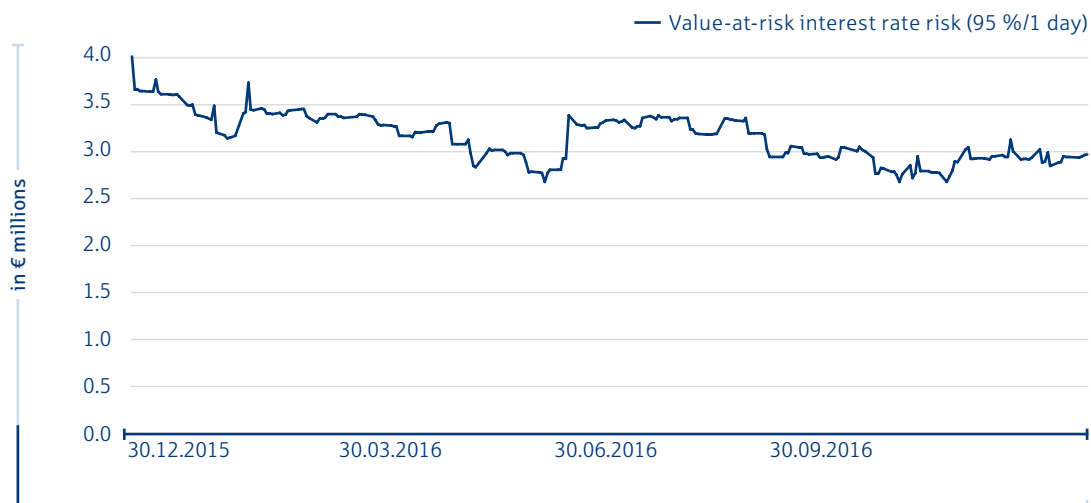
Market price risks in € thousands	31.12.2016	31.12.2015
VaR*) Interest rate risk (going concern) portfolio of "entire bank"	2,767	3,950
Standard risk **) Interest rate risks portfolio "operating"	6,364	19,842

*) Confidence level 95 %, 1 day holding period

**) Parallel shift 100BP

Interest rate risk largely relates to the investment of perpetually available equity. The reduction in the VaR in the going concern as compared to the previous year was within the expected ranges and largely resulted from a reduction in the open position. The almost complete closing out of the risk position in the operational portfolio with regard to terms of more than one year (excluding the investment of the perpetually available equity) meant that standard risk fell significantly relative to the previous year, to a very low level. The daily calculated VaR for the interest rate risk fluctuated between € 2.4 million and € 4.0 million in the reporting period. The average value of € 3.0 million for the year confirms Deutsche Hypo's low risk appetite. The utilisation of the VaR limit for interest rate risks averaged 68 % over the year (2015: 65 %). At no time was the limit exceeded. The development of the VaR in the going concern in 2015 (95 % confidence level, 1 day holding period) is shown in the chart below. There are no credit spread risks in the banking book.

Change in value-at-risk interest rate risks (95 %/1 day)



The majority of all credit spread risks related to bonds and loans (Schuldscheindarlehen). The nominal volume of the exposure that involves credit spread risks totalled € 11,868.4 million as of 31 December 2016 (2015: € 12,898.2 million), a decrease of € 1,029.8 million over the course of the year. An ongoing improvement in portfolio quality and a reduction in hidden charges were also achieved together with this.

The systematic pursuit of the conservative risk-strategic goals and the attentive monitoring of the market developments in 2017 are also the focal points of controlling for the market price risk at Deutsche Hypo. In this context, this includes the strategy for a reduction in the positions that have credit spread risks in a way that protects the income statement, among others. For 2017, Deutsche Hypo continues to expect a low risk of a change in interest rates. The focus of the further development of the risk management process at Deutsche Hypo in 2017 will, among other things, be on the requirements of the European regulatory authorities with regard to CRR II and "interest rate risk in the banking book" for example.

Liquidity risk

Liquidity risk includes risks that may arise as a result of disruptions in the liquidity of individual market segments, unexpected events in the credit, deposit or issuing business, or changes to the Bank's own funding conditions.

Liquidity risk – goals and strategies

For the Bank, the securing of liquidity available at any time, both under normal and stress scenarios, is a strategic necessity. In the funding of the business activities in the market areas, Deutsche Hypo fundamentally pursues the strategy of term-congruent funding. Involvement in open funding positions has low strategic significance for the Bank. The intraday liquidity risk is very closely controlled at Deutsche Hypo and therefore has no appreciable impact. Liquidity risk limits cap the risk of a negative impact on income due to a change in the liquidity spreads related to an open liquidity risk position. The factors of securing sufficient liquidity and the risk bearing capacity of the NORD/LB Group are taken into account in the measurement of liquidity risk limits.

Global Liquidity Policy (GLP) at the Bank describes the strategic framework for securing sufficient liquidity. In the case of a liquidity crisis, the management of the liquidity risk in accordance with the GLP concept is assumed by an independent team in close coordination with the Board of Managing Directors and – depending on the type of crisis – with crisis managers from NORD/LB.

In terms of a complete consideration of the liquidity costs, benefits and risks in the income and risk management, the Bank offsets these components internally in accordance with their cause. The business policy principles and the responsibilities arising from the liquidity transfer pricing system, both in regard to application and refinement, are formulated in the binding Group-wide Group Transfer Pricing Policy.

Liquidity risk – structure and organisation

The process of liquidity risk management must include the entire Board of Managing Directors and Treasury and Controlling. The ALCO at Deutsche Hypo assumes responsibility for the management of the banking book positions, which includes in particular the liquidity positions. Treasury handles the operating liquidity risk management. It is also responsible for the management of the intraday liquidity positions. As an independent monitoring unit, Controlling defines the applied processes for the measurement, limiting and monitoring of liquidity risks and carries out the operative monitoring and reporting functions. Credit Risk Controlling is responsible for the determination, monitoring and reporting of key liquidity indicators to the regulators in accordance with the German Liquidity Regulation (LiqV). Controlling handles the liquidity notifications in accordance with CRR.

Liquidity risk – controlling and monitoring

In addition to compliance with the institute's limit, the Bank also uses volume structure limits to control and monitor the funding risks. The monitoring of the limit utilisation of the volume structure limits takes place on the basis of the liquidity outflow statement of the entire position. The calculated balances for the individual maturity bands from one month to 30 years may not exceed the approved volume structure limits. If limits are exceeded, the Board of Managing Directors is informed immediately. Furthermore, the funding risks from significant foreign currencies are determined and capped through volume structure limits.

The classic liquidity risk is limited by a dynamic stress test scenario. The Distance to Illiquidity (DtI) performance indicator is used in the internal management and limiting of such risk. The scenario describes the most likely crisis situation from an expert's point of view. A difference is made between deterministic payment flows and variable or unforeseeable payment flows. The amount and maturity of the deterministic payment flows is known at the time of the report, whilst the amounts and/or maturities of the variable payment flows are unknown and modelled by using suitable stress assumptions. Compliance with the limits is monitored daily. To assess the materiality of individual foreign currencies, a standardised process is used. If individual foreign currencies are classified as significant, the classic liquidity risk is also monitored in these foreign currencies.

In addition, there are further static stress tests. They model both the institution-specific and market crisis scenarios. The goal is to avoid liquidity shortages in cases of crises. Additional liquidity may be secured in the case of stress by maintaining a liquidity buffer consisting of free, highly liquid securities in accordance with the requirements of MaRisk.

Besides compliance with the different economic liquidity risk limits, compliance with the requirements for the liquidity coverage ratio (LCR) is also a focus of liquidity management at all times. In 2016, Deutsche Hypo integrated processes in internal liquidity in order to ensure daily compliance with both the regulatory minimum ratio and the intentionally higher internal target ratios.

The market liquidity risks are implicitly considered according to their market liquidity by differing between the securities in the calculation of the classical liquidity risk. By using the detailed security classes concept, the classification takes place on the basis of the degree of liquidity in the individual security, with assignment to various main classes with multiple sub-classes (depending on e.g. central bank eligibility and rating). In addition, the market liquidity in the calculation of the market price risk is considered.

Liquidity risk – reporting

The quarterly risk report provides the Board of Managing Directors and the Supervisory Board with comprehensive information about the current situation in the classical liquidity risk and funding risk. The report on the dynamic stress scenario is also provided daily to Treasury and the Board of Managing Directors. The utilisation of the required liquidity buffer, the liquidity outflow statement, the utilisation of the volume structure limits and the institute limit for the cash value funding risk are also provided to Treasury daily.

Liquidity risk – developments and outlook

Deutsche Hypo had sufficient access to the money market and capital market with acceptable conditions at all times in 2016. The total issue volume presented in the economic report and measured in terms of the Bank's need made it possible to place sufficiently covered and uncovered issues on the market.

All the volume structure limits were complied with in the past financial year as a result of forward-looking liquidity management. The DtI metric from the dynamic liquidity stress test used for internal controlling and limiting was within the existing required range in 2016. The green phase in the traffic light system was

maintained throughout the year. As of 31 December 2016, Dtl was 319 days (2015: 295 days). Likewise, the Bank met the requirements for the maintained liquidity buffer in accordance with MaRisk throughout the course of 2016.

The liquidity performance indicator in accordance with the German Liquidity Regulation (LiqV) was always significantly above the required regulatory minimum amount of 1.00 and amounted to 1.98 as of 31 December 2016 (2015: 1.50). The LCR based on European regulatory law has also been complied with daily since September 2016. The applicable minimum requirements of 70.0 % were met continuously in 2016. As of 31 December 2016 the ratio was 147.7 %.

In the context of new legal framework conditions regarding the asset class senior unsecured, particularly with regard to questions of liability in the context of MREL and bail-in, the liquidity situation will be monitored closely in 2017. Further investment was also made in the implementation of requirements in the area of European liquidity reporting.

Operational risk

According to this definition, operational risks include legal risks and the risks of changes in laws, compliance risks, outsourcing risks, insourcing risks, conduct risks, fraud risks, model risks, IT risks, vulnerability risks in emergency and crisis management, and HR risks.

Operational risk – goals and strategies

The guidelines for dealing with operational risks are formulated in Deutsche Hypo's risk strategy. Operational risks should generally be avoided or transferred if this is economically sensible. There are framework conditions in the form of technical and organisational measures, contractual provisions and working instructions to reduce the operational risk as much as possible and to guarantee business security. Not only specific contingency plans and appropriate insurance coverage, but also every employee's sensibility for risks play a key role here.

The causes of risks and the concentration of risk should be identified through a continuous analysis of cases involving losses and risk indicators as well as the application of the risk assessment methods. A functioning internal control system (ICS) prevents operational risks. The appropriateness and effectiveness of the ICS is checked with regard to risk at regular intervals.

Deutsche Hypo uses the possibilities of outsourcing processes with due regard for the regulatory requirements in accordance with MaRisk. The outsourced functions should continue to meet the Bank's performance and quality standards. The goal in this context is to increase efficiency, optimise processes, concentrate on core competencies, reduce risk potential, lower costs and make costs more flexible. Processes that represent strategic core competencies usually remain within Deutsche Hypo. The operational risk of outsourcing is kept as low as possible by taking suitable measures.

Operational risk – structure and organisation

The Board of Managing Directors and all other departments are included in the process of managing operational risks. Within the set framework conditions, responsibility for the controlling of the operational risks is decentralised and lies with the individual divisions. The initiation of the Risk Round Table committee in the reporting year created a platform for the discussion and evaluation of important matters of relevance to OpRisk at the Bank at the level of departmental heads and experts. Controlling handles the central tracking of operational risks and the independent reporting. Some tasks are also assumed by NORD/LB within the scope of outsourcing.

Operational risk – controlling and monitoring

As a result of inclusion in standardised Group methods, the methods and processes for the management of operational risks developed by NORD/LB are also applied at Deutsche Hypo. They are adjusted to the extent that they are appropriate with regard to the bank's type and scope, structure and operational risk situation.

The management of operational risks is supported in this context by a methodological framework for risk assessment. The constantly updated assessment of the risk situation entails the assessment of ongoing extensive information such as cases of loss, risk indicators and the results of scenario analyses. Suitable measures are taken by the responsible divisions if the occasion requires it. For example, in the past financial year investment in the IT systems was initiated with the aim of sustainably strengthening the level of IT security, among other things. The plans for continuing business, the emergency plans and the appropriateness of the insurance coverage are checked at regular intervals. Escalation processes have been set to ensure the prompt introduction of countermeasures.

Inclusion in risk management at the Group level means that the operational Value-at-Risk limits (OpVaR) for Deutsche Hypo are determined by NORD/LB in light of the risk bearing capacity on the level of the NORD/LB Group, and compliance with them is a risk-strategic goal at the Bank.

Operational risk – reporting

In the course of the ongoing risk management process, the results from the recorded loss events in terms of risk indicators and risk assessment are analysed and communicated quarterly to the Board of Managing Directors. The regular reports contain not only the limit utilisation of the OpVaR limit set by the NORD/LB Group, but also, among others, the information from the loss event database on the status of the risk indicators, the results of the scenario analyses and the risk assessment of the ongoing legal disputes and externally outsourced significant activities. The Board of Managing Directors and the Supervisory Board remain completely informed through the quarterly risk report.

Operational risk – developments

In 2016 there were no significant cases of loss, and it was not necessary to set up provisions for legal risks.

Accounting-related internal control system (ICS) and risk management system

The accounting-related internal control system ICS is a part of Deutsche Hypo's overall ICS concept. This is based on the requirements of the internationally recognised COSO framework for ensuring an appropriate and effective ICS. Key controls and simple controls have been implemented in all the accounting-relevant processes. These controls are to be performed periodically or on certain occasions, their results documented and their appropriateness checked at regular intervals. They include ongoing manual control work within the work process and programmed controls within the IT systems. In particular, controls have been implemented at the interfaces between the involved departments and between the Bank's IT systems. This ensures that the clearly defined specifications within the accounting process are implemented.

The individual material characteristics of the ICS in relation to the Bank's accounting process can be described as follows:

- Deutsche Hypo's Accounting is responsible for the preparation of the annual financial statements and the management report. The accuracy and completeness of the obligatory accounting circumstances from supplying departments is handled there and subject to adequate controls. The functions of the Bank's departments involved in the accounting process are separated. Areas of responsibility are clearly allocated.
- The IT systems and files used in the accounting process are protected against unauthorised access, manipulation and loss by means of regular data backups and corresponding access restrictions.
- The permanent monitoring of the IT systems by appropriately trained employees of the Bank and external systems partners reduces the risk of downtime and ensures high availability.
- The Bank has implemented an appropriate system of guidelines and instructions in an organisational manual that takes the form of an organised structure and workflows.
- All accounting processes are subject to consistent manual and automated controls according to the four eyes principle.
- Bookkeeping files that are received or forwarded are checked for completeness and accuracy, for example by means of random sampling. Programmed plausibility tests take place as a result of the used software.
- The plausibility of the data that is calculated in the accounting process is regularly checked.
- Internal Audit checks the observance of the ICS independently of processes.

The control activities specified above serve to ensure that transactions are adequately assessed and entered correctly and promptly. The qualified technical personnel, appropriate IT systems and legislative and internal company specifications form the basis for a proper accounting process. Report recipients are therefore provided with accurate and reliable information.

Regulatory equity resources

Due to the exercising of the waiver rule, the obligations to provide individual bank reports and compliance with the equity and capital requirements in accordance with CRR, part 2 and 3, do not apply to Deutsche Hypo on the level of the individual institute. For the reports on the equity resources on the Group level and for internal controlling, Deutsche Hypo calculates, after exercising the waiver rule, the equity and risk-weighted assets (RWA) that are consolidated in the reports prepared by NORD/LB for the Group. The Bank also calculates the equity ratio, which compares all the existing capital components with the Bank's equity requirements calculated in accordance with the regulatory provisions.

In accordance with the regulatory requirements, a total of € 1,182.4 million (2015: € 1,227.4 million) could be included for regulatory minimum capital requirements in the Group as of 31 December 2016. This means a decline of € 45.0 million relative to the end of 2015 due to the scheduled run-off of components in equity. At the same time, the RWA fell by 1.5 %. As a result, the equity ratio improved to 18.9 % (2015: 19.4 %).

Summary of the risk position

Deutsche Hypo's conservative risk policy was also systematically continued in 2016. Furthermore, not only the risk limits in the NORD/LB Group, but also the Bank's additional risk-strategic objectives and compliance with them play an important role for Deutsche Hypo. Besides the Group strategy specifications, all requirements contained in the rules of the German Pfandbrief Act, which are binding for the Bank, were also met at all times.

The economic development of real estate markets continued to be positive, and offered good sales opportunities. That was due, in particular, to the low level of interest rates. Together with consistently quality-oriented lending policies, that allowed the proportion of defaulted counterparties in Deutsche Hypo's total portfolio to be further significantly reduced.

The favourable capital market environment led to further improvement in spreads, which had a positive effect on the overall risk situation in the area of capital market business. The reduction of public sector finance business continued. That contributed to a further decrease in hidden charges in the banking book in 2016. Interest rate risk at the bank also remained very low as a result of Deutsche Hypo's low risk appetite.

The Bank's liquidity situation in the past financial year was also consistently good. It complied with the regulatory minimum liquidity requirements at all times.

Significant cases of damage involving operational risks were not noted.

Deutsche Hypo will continue its strategy of reducing its public sector finance portfolio to protect the income statement and further reduce the risks in the banking book. The liquidity situation will also be monitored closely with regard to new legal framework conditions regarding the asset class senior unsecured.

Hanover, 28 February 2017

The Board of Managing Directors



Pohl



Barthauer



Rehfus

ANNUAL FINANCIAL STATEMENTS

Balance sheet as of 31 December 2016

**Income statement for the period
from 1 January to 31 December 2016**

Statement of changes in equity

Cash flow statement

Notes

BALANCE SHEET AS OF 31 DECEMBER 2016

ASSETS

	€	€	€	31. Dezember 2015 (in € thousands)
1. Cash reserve				
b) Credit with central banks		50,540,971.02		90,940
of which:				
with the "Deutsche Bundesbank"				
€ 50,540,971.02 (PY € 90,940 thousand)				
			50,540,971.02	90,940
2. Receivables from financial institutions				
a) Mortgage loans		13,276,715.99		16,867
b) Loans to local authorities		588,294,593.36		947,047
c) Other receivables		1,402,643,217.44		2,084,594
of which: due daily				
€ 1,179,926,182.39 (PY € 1,227,938 thousand)				
			2,004,214,526.79	3,048,508
3. Receivables from customers				
a) Mortgage loans		11,963,723,493.76		11,936,683
b) Loans to local authorities		4,227,233,537.96		4,641,580
c) Other receivables		54,624,443.42		53,533
			16,245,581,475.14	16,631,796
4. Bonds and other fixed interest securities				
b) Bonds and debentures				
ba) from public issuers				
of which:				
borrowed from "Deutsche Bundesbank"	3,406,872,962.57			3,486,986
€ 1,970,427,334.05 (PY € 1,896,960 thousand)				
bb) from other issuers	3,313,398,517.19			3,551,031
of which:				
borrowed from "Deutsche Bundesbank"				
€ 2,806,383,169.14 (PY € 2,978,966 thousand)				
c) Own bonds		6,720,271,479.76		50,651
Nominal amount :		39,366,612.06		
€ 39,197,000.00 (PY € 24.483 thousand)				
			6,759,638,091.82	7,088,668
5. Participatory interest			76,949.43	77
6. Shares in affiliated companies			0.00	51
7. Intangible assets				
b) Purchased licenses, industrial property, as well as licenses to those rights and assets		583,990.00		654
d) Payments made on account		483,481.42		75
			1,067,471.42	729
8. Tangible assets			2,175,692.03	2,237
9. Other assets			87,114,995.72	22,393
10. Accrued and deferred items				
a) from the issue and loan transaction		43,436,395.30		47,667
b) others		8,764,474.93		10,679
			52,200,870.23	58,346
Total assets			25,202,611,043.60	26,943,745

Balance sheet as of 31 December 2016 | Income statement for the period from 1 January to 31 December 2016 | Statement of changes in equity | Cash flow statement | Notes

LIABILITIES

	€	€	€	31. Dezember 2015 (in € thousands)
1. Liabilities to financial institutions				
a) Issued registered mortgage Pfandbriefe		138,306,265.43		183,827
b) Issued registered public Pfandbriefe		255,527,197.19		386,601
c) Other liabilities		4,943,157,316.85		4,659,548
of which: due daily				
€ 474,929,049.89 (PY € 380,396 thousand)				
			5,336,990,779.47	5,229,976
2. Liabilities to customers				
a) Issued registered mortgage Pfandbriefe		660,310,500.74		768,883
b) Issued registered public Pfandbriefe		4,312,536,210.96		5,500,452
d) Other liabilities		2,144,342,519.89		2,462,295
with which: due daily				
€ 902,406.59 (PY € 6,047 thousand)				
			7,117,189,231.59	8,731,630
3. Securitised liabilities				
a) Assigned bonds				
aa) mortgage Pfandbriefe	7,488,251,848.02			7,533,804
ab) public Pfandbriefe	810,429,629.74			1,141,423
ac) other bonds	2,740,481,464.06			2,606,916
		11,039,162,941.82		
			11,039,162,941.82	11,282,143
4. Other liabilities				
			198,409,914.80	252,181
5. Accrued and deferred items				
a) from the issue and loan transaction		40,795,230.37		44,544
b) other		11,209,754.72		10,866
			52,004,985.09	55,410
6. Provisions				
a) Provisions from pensions and similar obligations		44,863,072.29		40,524
b) Tax provisions		2,369,876.76		907
c) Other provisions		29,048,618.59		20,402
			76,281,567.64	61,833
7. Subordinated liabilities			395,000,000.00	320,000
8. Jouissance right capital			60,000,000.00	83,000
9. Funds for general banking risks			14,400,000.00	14,400
10. Equity				
a) Subscribed capital		80,640,000.00		80,640
Capital held by silent partners		75,000,000.00		75,000
b) Capital reserves		481,313,877.23		481,314
c) Profit reserves				
ca) statutory reserves	18,917,799.60			18,918
cd) other profit reserves	257,299,946.36			257,300
		276,217,745.96		
			913,171,623.19	913,172
Total liabilities			25,202,611,043.60	26,943,745
1. Contingent liabilities				
b) Liabilities arising from sureties and guarantee agreements		1,029,309,015.32		1,126,952
			1,029,309,015.32	1,126,952
2. Other obligations				
c) Irrevocable credit commitments		1,809,697,113.85		1,245,029
			1,809,697,113.85	1,245,029

INCOME STATEMENT

FOR THE PERIOD FROM 1 JANUARY TO 31 DECEMBER 2016

	€	€	€	1 January 2015 – 31 Dezember 2015 (in € thousands)
1. Interest earnings from				
a) Credit and money market transactions	520,008,987.32			639,435
less negative interest from money market transactions	<u>- 1,819,176.90</u>			- 494
		518,189,810.42		
b) Fixed interest bearing securities and book-entry securities		<u>185,352,658.53</u>		236,692
			703,542,468.95	875,633
2. Interest expenses				
Interest expenses from the banking business	510,135,132.97			653,212
less positive interest from the banking business	<u>- 8,688,902.10</u>			- 2,121
			<u>501,446,230.87</u>	
			202,096,238.08	224,542
3. Commission income			13,624,784.80	11,610
4. Commission expenses			<u>9,935,371.70</u>	11,115
			3,689,413.10	495
5. Other operating income			2,164,737.53	4,753
6. General administrative expenses				
a) Personnel expenses				
aa) wages and salaries	36,885,309.64			36,275
ab) social security and expenses for pension plans and for support of which: for pension plans € 897,421.26 (PY € 2,336 thousand)		6,116,164.98		7,478
b) Other administrative expenses			<u>43,001,474.62</u> <u>32,673,993.54</u>	33,330
			75,675,468.16	77,083
7. Write-downs and value adjustments of intangible assets and tangible fixed assets			697,935.11	690
8. Other operating expenses			5,670,403.04	11,043
9. Write-downs and value adjustments on receivables and specific securities as well as allocations to provisions in credit business			<u>66,572,706.22</u>	41,293
			66,572,706.22	41,293
10. Write-downs and value adjustments on participatory interest, shares in affiliated companies and on securities treated as fixed assets			<u>0.00</u>	29,421
			0.00	29,421
11. Income from write-ups of participatory interest, shares in affiliated companies and securities treated as fixed assets			<u>55,658,469.18</u>	0
			55,658,469.18	0
12. Result from normal operations			114,992,345.36	70,260
13. Extraordinary income			3,507,017.00	713
14. Extraordinary expenses			<u>5,152,288.06</u>	807
15. Extraordinary result			- 1,645,271.06	- 94
16. Taxes on income			3,376,020.21	- 98
17. Other taxes not included under item 8			<u>- 37,690.64</u>	14
			3,338,329.57	- 84
18. Profits surrendered under partial surrender agreements or a profit and loss transfer agreement			110,008,744.73	70,250
19. Profit for the period			0.00	0
20. Transfer to profit reserves			0.00	0
21. Balance sheet profit			0.00	0

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STATEMENT OF CHANGES IN EQUITY

in € thousands	Subscribed capital	Capital held by silent partners	Capital reserves	Profit reserves	Equity difference from currency conversion	Profit/loss carried forward	Profit/loss for the period	Total
As of 1 January 2016	80,640	75,000	481,314	276,218	0	0	0	913,172
Capital increase / reduction	0	0	0	0	0	0	0	0
Allocation to / withdrawal from reserves	0	0	0	0	0	0	0	0
Distribution	0	0	0	0	0	0	0	0
Currency conversion	0	0	0	0	0	0	0	0
Other changes	0	0	0	0	0	0	0	0
Profit/loss for the period	0	0	0	0	0	0	0	0
As of 31 December 2016	80,640	75,000	481,314	276,218	0	0	0	913,172

in € thousands	Subscribed capital	Capital held by silent partners	Capital reserves	Profit reserves	Equity difference from currency conversion	Profit/loss carried forward	Profit/loss for the period	Total
As of 1 January 2015	80,640	75,000	481,314	276,218	0	0	0	913,172
Capital increase / reduction	0	0	0	0	0	0	0	0
Allocation to / withdrawal from reserves	0	0	0	0	0	0	0	0
Distribution	0	0	0	0	0	0	0	0
Currency conversion	0	0	0	0	0	0	0	0
Other changes	0	0	0	0	0	0	0	0
Profit/loss for the period	0	0	0	0	0	0	0	0
As of 31 December 2015	80,640	75,000	481,314	276,218	0	0	0	913,172

CASH FLOW STATEMENT

in € thousands	2016	2015
1. Net result	0	0
2. Write-downs, value adjustments and write-ups to receivables and tangible fixed assets	-10,129	86,170
3. Increase/decrease in reserves	11,341	5,959
4. Other non-cash expenses/income	0	0
5. Profit/loss from the disposal of tangible fixed assets	-52,682	-250,142
6. Profit to be surrendered under a profit and loss transfer agreement	101,609	61,850
7. Other adjustments (balance)	9,307	10,101
8. Increase/decrease of receivables from financial institutions	975,039	-159,932
9. Increase/decrease of receivables from customers	329,649	855,660
10. Increase/decrease of securities (if not financial assets)	10,275	15,786
11. Increase/decrease of other assets from current operations	-78,897	57,913
12. Increase/decrease of liabilities to financial institutions	85,693	-2,285,186
13. Increase/decrease of liabilities to customers	-1,582,148	-361,968
14. Increase/decrease of securitised liabilities	-207,217	-342,139
15. Increase/decrease of other liabilities from current operations	-25,389	-7,605
16. Interest expenses/income	-202,096	-224,543
17. Expenses/income from extraordinary items	1,645	94
18. Income tax expenses/income	3,376	-98
19. Interest and dividend payments received	763,892	947,460
20. Interest paid	-548,882	-708,170
21. Extraordinary deposits	0	0
22. Extraordinary disbursements	0	0
23. Income tax payments	-372	-2,684
24. Cash flow from current operations (total of items 1 to 23)	-415,986	-2,301,474
25. Deposits from disposals of financial assets	1,033,105	3,659,692
26. Disbursements for investments in financial assets	-615,346	-1,243,172
27. Deposits from disposals of tangible fixed assets	14	129
28. Disbursements for investments in tangible fixed assets	-419	-459
29. Deposits from disposals of intangible fixed assets	0	0
30. Disbursements for investments in intangible fixed assets	0	-51
31. Deposits from disposals from the consolidated group	0	0
32. Disbursements for additions to the consolidated group	0	0
33. Changes in funds from other investment activities (balance)	-517	416
34. Deposits from extraordinary items	0	0
35. Disbursements for extraordinary items	0	0
36. Cash flow from investment activities (total of items 25 to 35)	416,837	2,416,555
37. Deposits from equity contributions by shareholders of the parent company	0	0
38. Deposits from equity contributions by other shareholders	0	0
39. Disbursements for equity reductions to shareholders of the parent company	0	0
40. Disbursements for equity reductions to other shareholders	0	0
41. Deposits from extraordinary items	0	0
42. Disbursements for extraordinary items	0	0
43. Dividends paid to shareholders of the parent company	0	0
44. Dividends paid to other shareholders	0	0
45. Other disbursements to company owners	-31,400	-31,207
46. Profit and loss transfer	-61,850	-28,818
47. Changes in funds from other capital (balance)	52,000	-6,000
48. Cash flow from financing activities (total of items 37 to 47)	-41,250	-66,025
49. Cash changes in finance funds (total from 24, 36, 48)	-40,399	49,056
50. Exchange-rate and valuation-related change in finance funds	0	0
51. Consolidation-related change in finance funds	0	0
52. Finance funds at the start of the period	90,940	41,884
53. Finance funds at the end of period (total of items 49 to 52)	50,541	90,940

NOTES

The figures in the tables in the notes are expressed in thousand euros (€ thousands) or million euros (€ millions). It should be noted that the amounts quoted in the tables and text are rounded figures, resulting in rounding differences in some cases.

General information on annual financial statements and accounting and valuation principles

1. General information on the company and on group affiliation

Name:	Deutsche Hypothekbank (Actien-Gesellschaft)
Headquarters:	Hanover
Registry court:	Hanover District Court
Commercial register number:	5602

According to Section 271 (2) of the German Commercial Code (HGB), Deutsche Hypo (Actien-Gesellschaft), Hanover, (Deutsche Hypo or the Bank) is a company affiliated to Norddeutsche Landesbank Girozentrale (Anstalt öffentlichen Rechts), Hanover, Braunschweig and Magdeburg (NORD/LB), and is included in the consolidated financial statements of NORD/LB. NORD/LB's consolidated financial statements as of 31 December 2015 were published in the federal gazette on 6 June 2016.

Pursuant to an existing profit and loss transfer agreement between Deutsche Hypo and NORD/LB, Deutsche Hypo is obligated to transfer all of its profits to NORD/LB. The profit and loss transfer agreement leads to a fiscal tax unit.

2. Accounting regulations

The annual financial statements of Deutsche Hypo for the 2016 financial year have been prepared in accordance with the provisions of the HGB in conjunction with the German Ordinance on Accounting of Financial Institutions (RechKredV) and with due adherence to the provisions of the German Stock Corporation Act (AktG) and the German Pfandbrief Act (PfandBG). The annual financial statements comprise the balance sheet, the income statement, the cash flow statement, the statement of changes in equity and the notes. The breakdown of the balance sheet and the income statement is based on forms 1 and 3 of the RechKredV.

Due to the fiscal tax unit with NORD/LB, Deutsche Hypo only reports income taxes that relate to financial years up to and including 2012 or that relate to a foreign branch. The latter are calculated on the basis of the taxable result at the applicable income tax rate.

3. Accounting and valuation principles

Receivables from institutions and customers are reported at their nominal value (Section 340e (2) of the HGB). Any differences between the nominal value and the payout value, as far as similar in nature to interest, are reported under accrued and deferred items, which are released on a straight-line basis.

Appropriate loan loss provisions and provisions according to cautious criteria are formed to cover identifiable risks in the credit business. Irrecoverable receivables are written off. Latent credit risk is accounted for in the form of general loan loss provisions. The general loan loss provisions are calculated in accordance with the requirements of the Federal Ministry of Finance Circular dated 10 January 1994.

Debenture bonds and other fixed interest securities are reported at cost if they involve securities held as fixed assets. If a permanent impairment is considered likely, unscheduled write-downs are performed pursuant to Section 253 (3) clause 5 of the HGB. Write-ups are performed pursuant to Section 253 (5) clause 1 of the HGB, provided that the reasons for the write-down no longer exist. Securities from the liquidity reserve are valued in accordance with the lower-of-cost-or-market-principle pursuant to Section 253 (4) of the HGB. There continues to be no trading portfolio. If there are securities transferred under repurchase agreements, this is conducted as part of real securities repurchase transactions, which are reported in accordance with the requirements of Section 340b (4) of the HGB.

Structured financial instruments are reported pursuant to IDW RS HFA 22, reviewed in terms of the obligation to separate such from the host instrument and of embedded derivatives; in the case of an obligation to separate, they are reported according to the respective applicable general principles.

Participatory interest and shares in affiliated companies are measured at cost or the lower-of-cost-or-market value pursuant to Section 253 (3) clause 5 of the HGB. Write-ups are performed pursuant to Section 253 (5) clause 1 of the HGB, provided that the reasons for a write-down cease to apply.

Applying Section 340c (2) clause 1 of the HGB, the expenses from write-downs on participatory interest, shares in affiliated companies and securities treated as fixed assets are offset against write-ups on these assets. The resulting income or expense is reported under income from financial assets in the income statement. There is no individual table of write-ups and write-downs in the notes to the financial statements due to the application of Section 34 (3) of the RechKredV.

Tangible assets and intangible fixed assets are carried at their acquisition cost less the straight-line scheduled depreciation over their ordinary useful life. Low-value assets are depreciated for reasons of materiality in accordance with Section 6 (2a) of the German Income Tax Act (EStG).

Deutsche Hypo does not recognise deferred taxes on account of the existing fiscal tax unit.

The tax claim based on the amendment to Section 37 of the German Corporate Tax Act (Körperschaftsteuergesetz (KStG)) is reported at its net present value applying an interest of 3.9 %. The payout commenced in 2008 with ten equal annual instalments to be paid.

Liabilities, as a general rule, are reported at their settlement amount or nominal value. Any difference between the nominal value and payout amount is reported under accruals and deferrals, which are released on a scheduled basis.

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The pension provisions are calculated by independent actuaries using an expectancy cash-value method, the projected unit credit method. In this process, the pensions being paid on the reporting date and the share of entitlements accrued (or earned) during the service period as of the reporting date are evaluated. Increases based on salary trends or pension adjustments expected in the future are also taken into account.

The cash value of the obligation is calculated by discounting the expected future benefits (settlement value) pursuant to Section 253 (2) clause 1 of the HGB at the average market rate of interest over the past ten years in view of their residual term. The average market rate of interest over the past seven years has been applied in the past. As of the date of conversion on 1 January 2016, there was an adjustment of pension provisions in the amount of € 3,507 thousand to be taken into account in profit and loss during the past financial year as extraordinary income due to the higher discounting rate. As of 31 December 2016, the differing amount pursuant to Section 253 (6) clause 1 of the HGB totalled € 6,533 thousand.

When discounting pension provisions, use is made of the simplification rule set out in Section 253 (2) clause 2 of the HGB and the average market interest rate is applied on a flat-rate basis for a residual term of 15 years. The calculations of the pension provisions for the period ended 31 December 2016 are based on the following actuarial assumptions:

	31.12.2016	31.12.2015
Actuarial interest	4.01 %	3.89 %
Mortality tables	Heubeck RT 2005 G	Heubeck RT 2005 G
Expectancy dynamics	2.00 % p.a.	2.00 % p.a.
Pension dynamics	2.75 %; 2.87 %; 1.00 %	2.75 %; 2.87 %; 1.00 %

For a small portion of the calculated obligation, there is a fund asset in the amount of € 4,288 thousand (2015: € 4,584 thousand), that is netted with the pension provision under application of Section 246 (2) clause 2 of the HGB.

The residual amount of the higher cash value obligation pursuant to Section 67 (1) of the Introductory Act to the German Commercial Code (EGHGB), which resulted from the application of the BilMoG compared with the rules under commercial law before initial application of the BilMoG, was added in full to pension provisions in the past financial year. This produced an extraordinary expense in the amount of € 5,131 thousand. As of 31 December 2016, there was no longer a shortfall (2015: € 5,131 thousand).

The other provisions, which are mainly provisions in human resources and tax provisions, are set at the level of the settlement amount that is required on the basis of a reasonable commercial assessment. Pursuant to Section 253 (2) clause 1 of the HGB, if there is a residual term of more than one year, they are discounted at the average market rate of interest for the past seven year. The applicable discount interest rate is determined by Deutsche Bundesbank in accordance with the German Provision Discounting Ordinance (RückAbzinsV) and announced monthly. The disclosure of expenses and income from the compounding or discounting of provisions takes place in the net interest result for provisions from the credit business and in other operating result for provisions from the non-banking business.

Contingent liabilities and other liabilities are reported at their nominal amounts on the balance sheet, provided that provisions have not been formed in this respect. Other liabilities relate to irrevocable loan commitments. Contingent liabilities are based on guarantees and collateral provided. Within the framework of these agreements, Deutsche Hypo undertakes to issue payments to beneficiaries if an issuer of reference or borrower does not fulfil their obligations. The decision whether contingent liabilities and other commitments are to be reported in the balance sheet at nominal value or reduced by a necessary provision amount is based on the estimation of the credit risk. The assessment is based on the estimated creditworthiness of the issuers of reference or of the borrowers on the reporting date.

The Bank has expenses and income from negative interest as a result of both receivables and liabilities. Negative interest income primarily results from the provision of collateral for derivative transactions; positive interest expenses result largely from pension transactions. Positive interest expenses were generated from collateral provided for derivative transaction as well as day-to-day money and fixed-term deposits. Unlike in prior years, the amount of negative interest in the items of "interest income" and "interest expenses" is reported in the income statement.

4. Currency conversion

The assets, liabilities and off-balance-sheet transactions denominated in foreign currencies are converted in line with the principles stipulated in Sections 256a and 340h of the HGB ("special cover"). All of the Bank's foreign currency transactions are subject to the special cover. Excesses in the total positions per currency are as a rule insignificant amounts and have a term of up to one year. If an asset in a foreign currency is at acute risk of default, it will be reduced by the amount in question, so that it is no longer taken into consideration in the special cover.

Receivables and liabilities in a foreign currency are converted at the mean spot exchange rate on the reporting date. Forward transactions are valued using the split forward price method (spot price and swap rate), as they are concluded to hedge interest-bearing items. All exchange rates are calculated by and taken from the European System of Central Banks.

The adjusting items created from valuing swap and forward exchange transactions at current rates are reported as net amounts in relation to the currency and disclosed under other assets or other liabilities as appropriate. Expenses arising from currency conversion are included in the income statement. Income arising from the currency conversion is taken into consideration insofar as it is based on specially covered transactions, or if the assets and liabilities being converted have a residual term of one year or less. These expenses and this income are reported either under "other operating expenses" or under "other operating income". In the past financial year, there was other operating income from currency conversion in the amount of € 170 thousand (2015: € 554 thousand).

The amount of net assets denominated in foreign currency totalled €3,321.9 million as of the reporting date (2015: € 3,570.2 million); the amount of the liabilities denominated in a foreign currency was € 544.3 million (2015: € 573.3 million).

5. Derivatives

All derivatives of Deutsche Hypo are assigned to the non-trading portfolio and are therefore governed by the principle of non-accounting of pending transactions. The Bank checks the requirement for provisions for contingent losses with regard to the banking book on the respective reporting date. Please refer to the next section of the notes to the financial statements for more information.

In the past financial year, the Bank formed a balance sheet valuation unit for an economic hedge relationship. The book value of the hedged asset amounted to € 221.8 million; the interest risk, which was hedged nearly in full against changes in market interest rates via an interest swap within the framework of a micro-hedge relationship, amounted to € 7.7 million. This corresponded to the decrease in fair value of the hedged underlying transaction as a result of interest effects. The net hedge presentation was applied in the balance sheet.

The effectiveness of the hedge relationship was determined prospectively by forming a valuation unit through regression analysis. As a result of the structure of the underlying and hedge transaction, the changes in value up to maturity were nearly equal. This was reported retrospectively as of the respective balance sheet dates.

Accrued or deferred interest from derivatives is reported mainly under receivables from financial institutions or liabilities to financial institutions. Upfronts from derivatives are reported under accrued and deferred items.

The Bank also has credit derivatives in its portfolio, both as the collateral-taker and collateral-provider. With regard to the credit derivatives where the Bank is the collateral-provider, these qualify as issued loan collateral. They are reported under contingent liability, provided that no provision was formed for them. The credit derivatives, where the bank is the collateral-taker, qualify as loan collateral received. They are not reported separately, but taken into account when measuring the risk provision for the loan business.

6. Loss-free valuation of interest-related transactions for the banking book

In accordance with the requirements of IDW RS BFA 3 "Individual questions on the loss-free measurement of interest-related transactions for the banking book (interest book)", a calculation from the income statement point of view verifies that the creation of a provision in accordance with Section 340a in conjunction with Section 249 (1) clause 1 alternative 2 of the HGB is not required for excess liability from the business with interest-related financial instruments in the banking book as of the reporting deadline. The entire banking book was included in the calculation for the balancing – in accordance with the context of funding. In the calculation, future results of the banking book for subsequent periods are determined from the contributions to income by the closed and open fixed-income positions, taking into account the anticipated risk and administrative costs still to be incurred. The periodic impact on income from the open fixed-interest positions was calculated via fictitious closing transactions on the basis of the current money and capital market interest rates. In the process, Deutsche Hypo's individual funding surcharge is taken into account.

Notes on the balance sheet

7. Receivables from financial institutions

in € thousands	31.12.2016	31.12.2015
Breakdown of residual maturities		
due daily	1,179,926	1,227,938
up to three months	118,596	233,085
between three months and one year	17,515	718,008
between one year and five years	284,202	389,527
more than five years	202,286	208,983
proportionate interest in total	201,690	270,967
Balance sheet item	2,004,215	3,048,508
of which from affiliated companies	51,270	632,021

8. Receivables from customers

in € thousands	31.12.2016	31.12.2015
Breakdown of residual maturities		
up to three months	584,419	728,460
between three months and one year	1,305,707	1,974,216
between one year and five years	6,070,303	6,083,091
more than five years	8,179,570	7,730,389
proportionate interest in total	105,582	115,640
Balance sheet item	16,245,581	16,631,796
of which from investors and investees	463	1,068

9. Bonds and other fixed interest securities

in € thousands	31.12.2016	31.12.2015
Balance sheet item	6,759,638	7,088,668
of which from affiliated companies	1,044,864	1,044,174
due in the following year	586,758	762,253
of which exchange eligible	6,759,638	7,088,668
of which listed on exchanges	5,849,351	6,143,548
of which not listed on exchanges	910,287	945,120
of which not valued at the lower of cost or market value*)	846,642	1,181,679
fair value of securities not valued at lower of cost or market value	774,280	1,117,108

*) In these cases, a long-term impairment was not anticipated, as the individual review of the relevant issuer's credit rating did not reveal any signs that would justify a long-term impairment.

10. Participatory interest

in € thousands	31.12.2016	31.12.2015
Balance sheet item	77	77
of which exchange eligible	0	0

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11. Shares in affiliated companies

in € thousands	31.12.2016	31.12.2015
Balance sheet item	0	51
of which exchange eligible	0	0

12. Fixed asset schedule

in € thousands	Intangible Assets	Tangible Assets*)
Balance sheet date 31.12.2015	729	2,237
Historical costs 01.01.2016	8,121	5,369**)
Change in additions	568	419
Change in disposals	-27	-1,087
Historical costs 31.12.2016	8,662	4,700
Accumulated depreciation as of 01.01.2016	7,392	3,133**)
Depreciation current financial year	229	469
Change in disposals	-27	-1,077
Accumulated depreciation as of 31.12.2016	7,595	2,525
Balance sheet date 31.12.2016	1,067	2,176

*) Tangible assets involve only business and office equipment,

**) Adjustment of prior-year-end figure necessary as the disposals were reported at book value in 2015.

in € thousands	Securities in fixed assets	Participatory interest	Shares in affiliated companies
Balance sheet date 31.12.2015	7,038,017	77	51
Change*)	-317,746	0	-51
Balance sheet date 31.12.2016	6,720,271	77	0

*) The simplification rule pursuant to Section 34 (3) of the RechKredV was applied.

13. Other assets

in € thousands	31.12.2016	31.12.2015
Balance sheet time	87,115	22,393
of which adjustment items from foreign currencies	75,441	16,055

14. Accrued items

in € thousands	31.12.2016	31.12.2015
Balance sheet item	52,201	58,346
of which premium on claims	17,008	23,814
of which issuing discount from bonds	26,428	23,852

15. Liabilities to financial institutions

in € thousands	31.12.2016	31.12.2015
Breakdown of residual institutions		
due daily	474,929	380,396
up to three months	1,926,488	2,076,936
between three months and one year	1,464,679	1,252,099
between one year and five years	945,045	992,207
more than five years	300,036	285,338
proportionate interest in total	225,814	243,000
Balance sheet item	5,336,991	5,229,976
of which to affiliated companies	1,402,247	1,419,281
Assets pledged as collateral	2,395,500	2,703,888
of which within the context of real pension transactions	2,395,500	1,732,088

16. Liabilities to customers

in € thousands	31.12.2016	31.12.2015
Breakdown of residual maturities		
due daily	902	6,047
up to three months	609,283	975,746
between three months and one year	671,564	1,216,497
between one year and five years	1,740,221	1,837,143
more than five years	3,962,266	4,531,102
proportionate interest in total	132,953	165,095
Balance sheet item	7,117,189	8,731,630
of which to affiliated companies	–	1,017

17. Securitised liabilities

in € thousands	31.12.2016	31.12.2015
Balance sheet items	11,039,163	11,282,143
of which due in following year	2,321,699	3,004,662
of which to affiliated companies	1,106,561	1,543,492

18. Other liabilities

in € thousands	31.12.2016	31.12.2015
Balance sheet items	198,410	252,181
of which adjustment items from foreign currencies	176,917	229,455
of which pro-rata interest on subordinated liabilities and capital held by silent partners	15,271	15,163

19. Deferred items

in € thousands	31.12.2016	31.12.2015
Balance sheet items	52,005	55,410
of which discounts on claims	8,170	10,573

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20. Subordinated liabilities

Subordinated liabilities stood at € 395.0 million as of the balance sheet date (2015: € 320 million). Two subordinated liabilities exceeded 10.0 % of the total amount reported. This involved an amount of € 90.0 million subject to an interest rate of 6.12 % and due on 27 January 2020 as well as an amount of € 75.0 million subject to an interest rate of 5.00 % and due on 23 December 2026. Early repayment will only be possible in the event of additional payments to the lender or its legal successor due to changes in taxation or negative developments in supervisory-law recognition. In the event of dissolution, liquidation or insolvency of the Bank, or in the case of a settlement or procedure aimed at preventing the Bank's insolvency, the liabilities are subordinate to other non-subordinated liabilities. A conversion in balance sheet equity or another form of debt is not intended. These conditions also relate to other borrowings.

Interest expenses related to subordinated liabilities amounted to € 18.0 million in the reporting period (2015: € 18.2 million). As of the balance sheet date, there were subordinated liabilities to affiliated companies in the amount of € 165.0 million (2015: € 90.0 million).

21. Jouissance right capital

Reported jouissance right capital totalled a nominal amount of € 60.0 million (2015: € 83.0 million). The terms run to 31 December 2016 (€ 40.0 million) and 31 December 2017 (€ 20.0 million), whereby the repayment of the jouissance right capital falls due roughly 6 months after the end of the term. The jouissance right is associated with the right to distribution within the meaning of these jouissance right conditions.

22. Notes on the development of equity

Deutsche Hypo held subscribed capital of € 80.6 million on 31 December 2016, which is divided into 13,440,000 individual shares and is the same as in 2015. The contract for an investment held by silent partners in the amount of € 75.0 million was terminated. Repayment will take place during the 2017 financial year.

23. Contingent liabilities and other obligations

in € thousands	31.12.2016	31.12.2015
Liabilities from sureties and guarantee agreements	1,029,309	1,126,952
of which credit default swaps	598,452	590,931
of which total return swaps	263,408	348,288
of which sureties in the mortgage business	167,449	187,733
of which assets pledged as collateral	12,119	12,730

Other liabilities relate exclusively to irrevocable credit commitments.

24. Transactions not included on the balance sheet and other financial obligations

Deutsche Hypo is a member of the security reserve of Landesbanks and giro centres. The membership amounts are measured on the basis of the risk-oriented principles in accordance with the Articles of Association. Furthermore, the Bank is obligated to make annual contributions to the restructuring funds for financial institutions (bank levy). The Bank did not make use of the option to provide a portion of the annual contributions to the restructuring funds in the form of irrevocable payment obligations. Accordingly, there are no financial obligations in terms of Section 285 (3a) of the HGB. However, the Bank is also obligated to provide reserve liability, if requested. This represents a risk for the financial position in terms of Section 285 (3) of the HGB.

Deutsche Hypo concluded rental and lease agreements for buildings the Bank uses and the fleet of vehicles and certain business and office equipment. There are no significant risks with an impact on the assessment of the Bank's financial position. All agreements concluded by the Bank in this form fall within the norm both individually and collectively.

25. Derivative financial instruments

The Bank uses derivative financial instruments to manage the general interest rate risk (overall bank management) as well as to hedge foreign currency risks. Forward exchange transactions to hedge against foreign currency positions (currency-related transactions) are reported under forward transactions. Other reported items include exclusively swap transactions to hedge against interest rate risk (risk-related transactions) and changes in interest rate and currency risk (currency and interest rate-related transactions). The bank also has credit derivatives in its portfolio related to the credit substitution business. According to IDW RS BFA 1, these represent collateral issued and received; as a result, they are not included in the presentation below.

Market values represent the current value of the derivatives at market conditions (yield curves, forex rates, etc.). In deviation from the prior year, the values are presented without accrued interest. The book values are comprised of pro-rata interest and upfronts. The figures determined in this way are summarised in the following tables by product group.

31.12.2016						
in € millions	Nominal amount	Market value		Book value		Balance sheet item
		positive	negative	positive	negative	
Currency-related transactions	1,121	18	33	0	0	
Interest rate-related transactions	33,557	1,712	2,248	5	6	Assets 2 and 10; Liabilities 5
Interest rate-currency related transactions	2,366	104	358	3	5	Assets 10; Liabilities 5
Total	37,044	1,834	2,639	8	11	

31.12.2015						
in € millions	Nominal amount	Market value*)		Book value*)		Balance sheet item
		positive	negative	positive	negative	
Currency-related transactions	951	8	8	0	0	
Interest rate-related transactions	31,887	1,812	2,167	6	5	Assets 2 and 10; Liabilities 5
Interest rate-currency related transactions	2,150	51	446	4	6	Assets 10; Liabilities 5
Total	34,988	1,871	2,622	10	11	

*) In deviation from the prior year, the figures are presented without pro-rate interest. The prior-year figures were adjusted accordingly.

Balance sheet as of 31 December 2016 | Income statement for the period from 1 January to 31 December 2016 | Statement of changes in equity | Cash flow statement | Notes

Notes on the income statement

26. Other operating income

in € thousands	31.12.2016	31.12.2015
Income statement item	2,165	4,753
of which significant items:		
income from the release of provisions	1,258	1,290
ongoing income from leases	411	836
exchange rate profits from currency transactions	170	554
VAT reimbursements including interest	0	1,853

27. Other operating expenses

in € thousands	31.12.2016	31.12.2015
Income statement item	5,670	11,043
of which significant items:		
discounting of provisions*)	4,913	7,297
expenses for buildings managed by third parties	423	2,864

*) The amount also includes the effect of the interest rate change related to the discounting of provisions.

28. Extraordinary income

in € thousands	31.12.2016	31.12.2015
Income statement item	3,507	713
of which significant items:		
release of pension provisions following the revision of Section 253 (2) clause 1 of the HGB*)	3,507	0
release of provisions in connection with the efficiency improvement programme	0	713

*) For more information, please refer to the explanation on pension provisions provided in the section on accounting and valuation methods.

29. Extraordinary expenses

in € thousands	31.12.2016	31.12.2015
Income statement item	5,152	807
of which significant items:		
Allocations to pension provisions pursuant to Art, 67 (1) clause 1 EGHGB*)	5,131	570

*) For more information, please refer to the explanation on pension provisions provided in the section on accounting and valuation methods.

Other disclosures

30. Services rendered to third parties for management and brokerage

Deutsche Hypo continues to manage the real estate finance business in the portfolio of NORD/LB. For this service, the Bank received service fees that were included in the net commission income.

Deutsche Hypo also structured financing for customers and assumed management of all loans for the bank consortium as the lead manager of the consortium of banks. For this service, the Bank receives ongoing remuneration for loan management in addition to the one-off fee for establishing the financing structure.

31. Cover analysis (in accordance with Section 28 of the PfandBG)

Revolving Pfandbriefe and the cover assets used with disclosure of the maturity structure
(Section 28 (1) of the PfandBG):

Mortgage Pfandbriefe:

in € millions	Nominal		Net present value		Risk net present value *)	
	31.12.2016	31.12.2015	31.12.2016	31.12.2015	31.12.2016	31.12.2015
Mortgage Pfandbriefe	8,243	8,409	8,571	8,820	7,591	8,514
of which derivatives	–	–	25	54	2	7
Cover pool	9,151	9,397	10,282	10,293	8,902	9,749
of which derivatives	–	–	29	5	80	35
Excess cover	908	988	1,711	1,473	1,311	1,235

*) For the calculation of the risk net present value, the dynamic approach in accordance with the PfandBarwertV is used.

in € millions	31.12.2016		31.12.2015	
	Pfandbriefe in circulation	Cover pool	Pfandbriefe in circulation	Cover pool
up to 0.5 years	821	743	1,738	1,381
more than 0.5 years up to 1 year	364	579	227	808
more than 1 year up to 1.5 years	875	573	821	516
more than 1.5 years up to 2 years	1,108	508	364	499
more than 2 years up to 3 years	1,491	1,012	1,683	956
more than 3 years up to 4 years	530	1,093	1,491	1,294
more than 4 years up to 5 years	550	943	530	608
more than 5 years up to 10 years	2,339	3,139	1,271	2,910
more than 10 years	167	561	284	425
Total	8,243	9,151	8,409	9,397

Balance sheet as of 31 December 2016 | Income statement for the period from 1 January to 31 December 2016 | Statement of changes in equity | Cash flow statement | Notes

Public Pfandbriefe:

in € millions	Nominal		Net present value		Risk net present value *)	
	31.12.2016	31.12.2015	31.12.2016	31.12.2015	31.12.2016	31.12.2015
Public Pfandbriefe	5,266	6,883	6,643	8,445	5,728	7,835
of which derivatives	–	–	6	2	–5	–13
Cover pool	6,108	7,395	7,606	8,988	6,584	8,114
of which derivatives	–	–	–	–	–	–
Excess cover	843	512	964	543	856	279

*) For the calculation of the risk net present value, the dynamic approach in accordance with the PfandBarwertV is used.

in € millions	31.12.2016		31.12.2015	
	Pfandbriefe in circulation	Cover pool	Pfandbriefe in circulation	Cover pool
up to 0.5 years	385	714	481	1,171
more than 0.5 years up to 1 year	419	492	565	432
more than 1 year up to 1,5 years	431	531	400	588
more than 1.5 years up to 2 years	118	198	468	391
more than 2 years up to 3 years	416	509	545	879
more than 3 years up to 4 years	336	328	528	606
more than 4 years up to 5 years	255	120	386	427
more than 5 years up to 10 years	1,471	1,487	1,583	1,323
more than 10 years	1,436	1,729	1,927	1,578
Total	5,266	6,108	6,883	7,395

Other cover assets for mortgage Pfandbriefe (Section 28 (1) clauses 4 to 6 of the PfandBG in conjunction with Section 19 (1) clauses 1 to 3 of the PfandBG):

in € millions (as of 31 December each)	Germany		Belgium		EU		France	
	2016	2015	2016	2015	2016	2015	2016	2015
Equalisation claims in terms of Section 19 (1) clause 1 of the PfandBG	–	–	–	–	–	–	–	–
Claims in terms of Section 19 (1) clause 2 of the PfandBG	–	450	–	–	144	45	–	–
of which: uncovered debt securities in terms of Art. 129 of Regulation (EU) No. 575/2013	–	–	–	–	144	45	–	–
Claims in terms of Section 19 (1) clause 3 of the PfandBG	273	592	75	110	–	–	82	–
Total	273	1,042	75	110	144	45	82	–

in € millions (as of 31 December each)	Italy		Japan		Luxembourg		Netherlands	
	2016	2015	2016	2015	2016	2015	2016	2015
Equalisation claims in terms of Section 19 (1) clause 1 of the PfandBG	–	–	–	–	–	–	–	–
Claims in terms of Section 19 (1) clause 2 of the PfandBG	289	–	–	–	40	–	–	–
of which: uncovered debt securities in terms of Art. 129 of Regulation (EU) No. 575/2013	289	–	–	–	40	–	–	–
Claims in terms of Section 19 (1) clause 3 of the PfandBG	11	21	149	149	–	55	25	25
Total	300	21	149	149	40	55	25	25

in € millions (as of 31 December each)	Austria		Spain		Other*)		Total	
	2016	2015	2016	2015	2016	2015	2016	2015
Equalisation claims in terms of Section 19 (1) clause 1 of the PfandBG	–	–	–	–	–	–	–	–
Claims in terms of Section 19 (1) clause 2 of the PfandBG	60	25	–	–	135	131	668	651
of which: uncovered debt securities in terms of Art. 129 of Regulation (EU) No. 575/2013	60	25	–	–	135	131	668	201
Claims in terms of Section 19 (1) clause 3 of the PfandBG	–	–	46	54	–	–	660	1,006
Total	60	25	46	54	135	131	1,328	1,657

*) Other supranational organisations

Other cover assets for public Pfandbriefe (Section 28 (1) clauses 4 and 5 of the PfandBG in conjunction with Section 20 (2) clauses 1 and 2 of the PfandBG) were not available in either the previous year or as of 31 December 2016.

Disclosures in connection with receivables used as cover for mortgage Pfandbriefe (Section 28 (2) clause 1 of the PfandBG):

Breakdown by size groups:

in € millions	31.12.2016	31.12.2015
up to and including € 0.3 million	22	28
from € 300.000 up to and including € 1 million	66	84
from € 1 million up to and including € 10 million	1,505	1,752
more than € 10 million	6,230	5,876
Total	7,823	7,740

Breakdown of receivables by areas and types of use:

in € millions (as of 31 December each)	Germany		Belgium		France	
	2016	2015	2016	2015	2016	2015
Residential						
Apartments	6	8	–	–	0	–
Detached family homes	7	11	–	–	–	–
Multifamily homes	553	551	–	–	156	158
New buildings, not yet completed or not yet a source of income	21	33	–	–	–	–
Total residential	587	602	–	–	156	158
Commercial						
Office buildings	1,403	1,414	18	18	310	285
Commercial buildings	1,793	1,950	–	–	327	261
Industrial buildings	17	17	–	–	–	–
Other commercially used buildings	518	450	–	–	–	–
New buildings, not yet completed or not yet a source of income	189	324	–	–	–	–
Building sites	38	16	–	–	–	–
Total commercial	3,958	4,171	18	18	637	546
Total value of cover	4,545	4,774	18	18	793	704

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in € millions (as of 31 December each)	UK		Ireland		Netherlands	
	2016	2015	2016	2015	2016	2015
Residential						
Apartments	–	–	–	–	16	16
Detached family homes	–	–	–	–	1	1
Multifamily homes	–	–	–	–	364	289
New buildings, not yet completed or not yet a source of income	–	–	–	–	–	–
Total residential	–	–	–	–	381	306
Commercial						
Office buildings	541	505	24	24	176	213
Commercial buildings	306	278	–	–	229	179
Industrial buildings	–	–	–	–	–	–
Other commercially used buildings	21	24	–	–	231	165
New buildings, not yet completed or not yet a source of income	17	–	–	–	–	26
Building sites	–	24	–	–	–	–
Total commercial	884	831	24	24	635	583
Total value of cover	884	831	24	24	1,016	889

in € millions (as of 31 December each)	Austria		Poland		Spain	
	2016	2015	2016	2015	2016	2015
Residential						
Apartments	–	–	–	–	–	–
Detached family homes	–	–	–	–	–	–
Multifamily homes	–	–	–	–	–	–
New buildings, not yet completed or not yet a source of income	–	–	–	–	–	–
Total residential	–	–	–	–	–	–
Commercial						
Office buildings	63	47	153	120	–	11
Commercial buildings	10	11	51	50	56	56
Industrial buildings	–	–	–	–	–	–
Other commercially used buildings	–	–	–	–	11	11
New buildings, not yet completed or not yet a source of income	–	–	–	–	–	–
Building sites	–	–	–	–	–	–
Total commercial	73	58	203	170	66	78
Total value of cover	73	58	203	170	66	78

in € millions (as of 31 December each)	USA		Total – all countries	
	2016	2015	2016	2015
Residential				
Apartments	–	–	22	24
Detached family homes	–	–	9	12
Multifamily homes	–	–	1,072	998
New buildings, not yet completed or not yet a source of income	–	–	21	33
Total residential	–	–	1,125	1,067
Commercial				
Office buildings	186	180	2,872	2,816
Commercial buildings	15	15	2,786	2,800
Industrial buildings	–	–	17	17
Other commercially used buildings	–	–	780	650
New buildings, not yet completed or not yet a source of income	–	–	206	350
Building sites	–	–	38	40
Total commercial	201	194	6,699	6,673
Total value of cover	201	194	7,823	7,740

Total amount of payments overdue by at least 90 days (Section 28 (2) clause 2 of the PfandBG):

in € millions	31.12.2016		31.12.2015	
	Total amount of payments overdue by at least 90 days	Total amount of these claims if the overdue amount totals at least 5 % of the claim	Total amount of payments overdue by at least 90 days	Total amount of these claims if the overdue amount totals at least 5 % of the claim
Germany	0.4	0.3	0.4	0.3
France	3.3	5.1	2.5	5.1
Netherlands	0.7	8.6	–	–
Total	4.4	14.0	2.9	5.4

Foreclosure / sequestration (Section (2) clause 4 of the PfandBG):

in € millions	As of 31 December					
	Foreclosures pending		Sequestration pending		Foreclosures executed	
	2016	2015	2016	2015	2016	2015
Properties used for residential purposes	–	–	–	–	–	1
Properties used for commercial purposes	–	1	–	–	1	1
Total	–	1	–	–	1	2

In the 2016 financial year, Deutsche Hypo did not possess any property to save existing mortgages, as in the prior year.

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Total overdue interest (Section 28 (2) clause 4 of the PfandBG):

in € millions	31.12.2016	31.12.2015
Properties used for residential purposes	–	0.1
Properties used for commercial purposes	2.1	4.2
Total	2.1	4.3

Disclosures in connection with receivables used as cover for public Pfandbriefe (Section 28 (3) of the PfandBG):

in € millions (as of 31 December)	Germany		Belgium		EU		Finland	
	2016	2015	2016	2015	2016	2015	2016	2015
Central state	–	101	–	–	60	72	–	–
Regional authority	2,212	2,438	105	105	–	–	12	13
Local authority	53	55	–	–	–	–	–	–
Other	1,249	1,831	140	140	170	243	–	–
Total	3,514	4,425	245	245	229	315	12	13

in € millions (as of 31 December)	France		UK		Italy		Japan	
	2016	2015	2016	2015	2016	2015	2016	2015
Central state	–	–	–	–	61	224	–	–
Regional authority	22	22	–	–	113	118	10	10
Local authority	–	–	–	–	–	–	–	–
Other	13	26	58	68	103	100	–	–
Total	35	48	58	68	278	442	10	10

in € millions (as of 31 December)	Canada		Latvia		Netherlands		Austria	
	2016	2015	2016	2015	2016	2015	2016	2015
Central state	–	–	–	–	–	–	574	596
Regional authority	153	160	16	17	130	130	41	42
Local authority	–	–	–	–	–	–	–	–
Other	86	83	–	–	290	290	–	–
Total	238	243	16	17	420	420	614	638

in € millions (as of 31 December)	Poland		Sweden		Switzerland		Spain	
	2016	2015	2016	2015	2016	2015	2016	2015
Central state	118	95	–	–	–	–	–	–
Regional authority	–	–	16	17	70	69	50	50
Local authority	–	–	–	–	–	–	–	–
Other	–	–	–	–	–	100	48	48
Total	118	95	16	17	70	169	98	98

in € millions (as of 31 December)	Hungary		USA		Total	
	2016	2015	2016	2015	2016	2015
Central state	28	27	–	–	840	1,115
Regional authority	–	–	109	105	3,058	3,296
Local authority	–	–	–	–	53	55
Other	–	–	–	–	2,157	2,929
Total	28	27	109	105	6,108	7,395

In the 2016 financial year, Deutsche Hypo did not possess any property to save existing mortgages, as in the prior year.

Breakdown by size groups:

in € millions	31.12.2016	31.12.2015
up to and including € 10 million	390	445
from € 10 million up to and including € 100 million	5,582	6,663
more than € 100 million	136	287
Total	6,108	7,395

Key figures about the Pfandbriefe in circulation and the cover assets used:**Mortgage Pfandbrief:**

		31.12.2016	31.12.2015
Pfandbriefe in circulation	in € millions	8,243	8,409
of which share of fixed-rate Pfandbriefe (Section 28 (1) clause 9 of the PfandBG)	%	94.33	89.26
Cover pool	in € millions	9,151	9,397
of which total amount of claims that exceeds the limits in accordance with Section 13 (1) of the PfandBG (Section 28 (1) clause 7 of the PfandBG)	in € millions	–	–
of which total amount of claims that exceed the limits of Section 19 (1) clause 2 of the PfandBG (Section (1) clause 8 of the PfandBG)	in € millions	–	–
of which total amount of claims that exceed the limits of Section 19 (1) clause 3 of the PfandBG (Section 28 (1) clause 8 of the PfandBG)	in € millions	–	–
of which share of fixed-rate cover pool (Section 28 (1) clause 9 of the PfandBG)	%	65.47	65.00
Net cash value in accordance with Section 6 of the PfandBarwertV for each foreign currency (in € millions)	AUD	–	–
	CAD	–	–
	CHF	161.2	19.1
Section 28 (1) clause 10 of the PfandBG (net of assets and liabilities)	GBP	459.8	441.9
	JPY	0.9	1.7
	SEK	–	–
	USD	133.2	97.8
Volume-weighted average of age of claims (past term since credit award seasoning (Section 28 (1) clause 11 of the PfandBG)	years	4.3	4.4
Average weighted loan-to-value ratio (Section 28 (2) no. 3 of the PfandBG)	%	58.21	58.04
Average weighted loan-to-value ratio on a market basis	%	42.52	43.95

Public Pfandbriefe:

		31.12.2016	31.12.2015
Pfandbriefe in circulation	in € millions	5,266	6,883
of which share of fixed-rate Pfandbriefe (Section 28 (1) clause 9 of the PfandBG)	%	90.75	92.95
Cover pool	in € millions	6,108	7,395
of which total amount of claims that exceed the limits of Section 20 (2) of the PfandBG (Section 28 (1) clause 8 of the PfandBG)	in € millions	–	–
of which share of fixed-rate cover pool (Section 29 (1) clause 9 of the PfandBG)	%	83.51	79.02
Net cash value in accordance with Section 6 of the PfandBarwertV for each foreign currency (in € millions)	AUD	–	–
	CAD	68.6	38.1
	CHF	–99.2	52.7
	GBP	78.1	162.9
Section 28 (1) clause 10 of the PfandBG (net of assets and liabilities)	JPY	–153.2	–21.4
	SEK	7.6	7.6
	USD	411.7	403.6

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32. Cover for bonds in circulation

in € million	Mortgage Pfandbriefe		Public Pfandbriefe	
	31.12.2016	31.12.2015	31.12.2016	31.12.2015
Ordinary cover				
Receivables from financial institutions				
Mortgage loans	–	1	–	–
Public sector loans	–	–	572	911
Receivables from customers				
Mortgage loans	7,823	7,739	–	–
Public sector loans	–	–	4,266	4,634
Bonds of public sector issuers	–	–	1,270	1,850
	7,823	7,740	6,108	7,395
Substitute cover				
Other receivables from financial institutions	518	939	–	–
Bond and other fixed income securities	810	718	–	–
	1,328	1,657	–	–
Total value of cover	9,151	9,397	6,108	7,395
Total amount in circulation requirement cover	8,243	8,409	5,266	6,883
Surplus cover	908	988	843	512

33. Members of the Board of Managing Directors

ANDREAS POHL

(Chairman of the Board of Managing Directors, since 1 July 2016; Speaker of the Board of Managing Directors, until 30 June 2016)

SABINE BARTHAUER

(since 17 August 2016)

ANDREAS REHFUS

34. Members of the Supervisory Board

DR. GUNTER DUNKEL

(until 31 December 2016)

Chairman of the Board of Managing Directors of NORD/LB
– Chairman of the Supervisory Board –

ECKHARD FORST

(until 31 October 2016)

Member of the Board of Managing Directors of NORD/LB
– Vice Chairman of the Supervisory Board –

THOMAS S. BÜRKLE

Member of the Board of Managing Directors of NORD/LB (until 31 December 2016);
Chairman of the Board of Managing Directors of NORD/LB (from 1 January 2017)
– Vice Chairman of the Supervisory Board – (1 November 2016 – 31 December 2016)
– Chairman of the Supervisory Board – (from 1 January 2017)

GÜNTER TALLNER

(from 1 January 2017)

Member of the Board of Managing Directors of NORD/LB (from 1 January 2017)
– Vice Chairman of the Supervisory Board –

CHRISTOPH DIENG

(from 1 January 2017)

Member of the Supervisory Board of NORD/LB (from 1 January 2017)

THOMAS KRÜGER

Member of the Supervisory Board VGH Versicherungen (retired)

DIRK METZNER

Bank employee, Deutsche Hypo

ANDREA BEHRE

Bank employee, Deutsche Hypo

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35. Emoluments of the Board of Managing Directors and Supervisory Board

in € thousands	2016	2015
Total emoluments		
Board of Managing Directors	1,171	872
Former members of the Board of Managing Directors and their surviving dependants	1,143	1,064
Supervisory Board	113	116

In € millions	2016	2015
Provisions for pension obligations owed to former members of the Board of Managing Directors and their surviving dependants		
Of which in reserves	13,453	13,681
Shortfall*)	0	1,212

*) The existing shortfall arising from the valuation of pension provisions according to the BilMoG was added in full to provisions during the past financial year.

36. Size of workforce on average over the year

	2016	2015
Female employees	174	169
Male employees	221	221
Total	395	390

37. Auditor's fees

in € thousands	2016	2015
Audit financial statements	773	674
Other confirmations	285	291
Other services	250	8
Total	1,308	973

Hanover, 28 February 2017

The Board of Managing Directors


Pohl


Barthauer


Rehfus

RESPONSIBILITY STATEMENT

“We affirm that, to the best of our knowledge and pursuant to the applicable accounting principles, the annual financial statements provide a true and fair view of net assets, financial and income position of the Bank and that the management report presents the business development, including the Bank’s results and position, such that an accurate picture is presented, with a suitable description of the opportunities and risks linked to future development of the Bank.”

Hanover, 28 February 2017

The Board of Managing Directors



Pohl



Barthauer



Rehfus

AUDITOR'S REPORT

We have audited the annual financial statements – comprising the balance sheet, the income statement and the notes to the financial statements, the cash flow statement and the statement of changes in equity – together with the bookkeeping system, and the management report of the Deutsche Hypothekenbank (Actien-Gesellschaft), Hannover, for the business year from January 1 to December 31, 2016. The maintenance of the books and records and the preparation of the annual financial statements and management report in accordance with German commercial law are the responsibility of the Company's management. Our responsibility is to express an opinion on the annual financial statements, together with the bookkeeping system, and the management report based on our audit.

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

Our audit has not led to any reservations.

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

Hanover, 28 February 2017

KPMG AG
Wirtschaftsprüfungsgesellschaft

Thiede
Wirtschaftsprüfer
(German Public Auditor)

Dr. Röhrich
Wirtschaftsprüferin
(German Public Auditor)

PERSONNEL REPORT

Value creation at Deutsche Hypo traces back to the performance of its employees. Among other things, the Human Resources department is responsible for ensuring the right conditions that will enable colleagues to act with excitement and enthusiasm on behalf of the Bank. The Bank strives to be an attractive employer and supports this day after day with the latest offerings and measures in human resources. At the heart of these efforts is the unwavering conviction that only satisfied, motivated and qualified employees will be able to ensure the Bank's long-term success and its future through their performance.

Remuneration system

Deutsche Hypo's remuneration system supports the current business and risk strategy. It aims at sustainability and continuity to promote responsible and risk-conscious behaviour on the part of employees and to ensure business success. The configuration of the remuneration system is also intended to guarantee appropriate staffing in both qualitative and quantitative terms, and especially to improve the attractiveness of the Bank as an employer, in line with the Group remuneration strategy.

Under the Remuneration Ordinance for Institutions (Institutsvergütungsverordnung – InstitutsVergV), the Bank is classified as a significant institution. A risk analysis has therefore been carried out in accordance with Section 18 of the Remuneration Ordinance for Institutions (identification of risk takers). Deutsche Hypo also had to comply with other provisions of the Remuneration Ordinance for Institutions applicable to significant institutions.

Deutsche Hypo is bound by collective bargaining agreements; as a result, collective bargaining agreements for the private banking sector and public banks apply. Besides fixed remuneration in twelve equal parts, employees under the collective bargaining agreement receive a special bonus equal to an additional month's salary. Employees who are not part of the collective pay scale receive a fixed basic annual salary in twelve equal parts.

Variable remuneration is determined for all employees in a transparent process defined by the Bank and the Works Council. For risk takers, executives and acquisitions officers, the overall success of the Bank, the profit contribution of the organisational unit and the individual profit contribution are duly taken into account when determining variable remuneration. Variable remuneration is limited to 100 % of fixed remuneration.

Personnel development

Personnel development activities at Deutsche Hypo in 2016 continued to pursue the aim of creating added value by leveraging synergies within the Group based on the introduction of the Group competency model, which has been adapted to the qualities that make Deutsche Hypo special. Building on this, the revision of the criteria of the employee appraisal process, which is part of the annual performance appraisal, is currently being negotiated with the Works Council. Furthermore, the introduction of 360° feedback for managers and the establishment of individual assessment centres as a standard selection tool for managers are among the measures planned in 2017.

A programme to train an internal sales trainee was launched in 2016 to promote the advancement of internal sales talents selected through a specially designed sales assessment centre. Plans are in place to systematically identify and qualify internal sales talents in the future.

In addition to training courses, seminars and numerous on-the-job development measures, ongoing training and education play a key role in personnel development at Deutsche Hypo. As a result, Deutsche Hypo supports employees who are obtaining additional professional or bank-related training. In 2016, a total of 15 Bank employees took advantage of ongoing training and education opportunities, such as master's degree programmes, certified banking professional (Bankbetriebswirt) training or gaining specific professional qualifications. To underpin the importance of ongoing training and education in employee qualification, the company agreement on the promotion of corresponding measures, which was originally set to expire on 31 December 2016, was extended indefinitely at the end of the year.

An additional workshop with female Bank employees was held in the reporting year with the aim of getting more women into leadership positions in the medium term. The event served to gauge participants' interest in leadership positions as well as their perception of the status quo and the current conditions. The findings of this and the previous analysis of the status quo are being used to derive future measures. In addition, the Bank plans to work with NORD/LB to focus more attention and energy on the issue of women in leadership.

A leadership programme for departmental managers was successfully completed in 2016 as part of the management development programme. Having been preceded by a development series for group leaders, consistent leadership goals and models on which all (future) elements are to be based have therefore been anchored at management level. In addition, managers who are new in their role have taken part in the NORD/LB leadership workshop since 2016.

Encouraging/attracting the next generation

In the financial year 2016, Deutsche Hypo also provided training in traditional banking professions. This training has been expanded to include the international Bachelor of Arts (B.A.) course of study, which is offered in association with the Leibniz-FH (University of Applied Sciences). The Bank had a total of 13 trainees and work-study students in the reporting year. Thanks to targeted campaigns aimed at recruiting young talent, Deutsche Hypo has succeeded in further raising the quality and quantity of job applications.

The training partnership with NORD/LB was successfully continued in the reporting year. Trainees from the parent company helped support Deutsche Hypo's real estate banking business activities, while trainees from Deutsche Hypo had the opportunity to shadow staff in various divisions at NORD/LB. In addition, trainees at Deutsche Hypo can take advantage of the wide range of options offered by NORD/LB to help them prepare for tests as well as a selection of seminars.

Alongside traditional vocational training, Deutsche Hypo offered qualified university graduates and internal employees the opportunity to participate in trainee programmes. By doing so, the Bank offers an attractive way of preparing up-and-coming staff for challenging responsibilities in a targeted and practical manner.

Deutsche Hypo offers students the opportunity to get a first look at the workings of a real estate and Pfandbrief bank through appealing work placement programmes. Under certain conditions, students can even partner with the Bank to complete their thesis work. In the reporting year under review, a total of six students participated in a work placement programme.

Work-life balance

The compatibility of family and career enjoys high priority at Deutsche Hypo and is reinforced by a company agreement. Through an external service provider, the Bank offers its employees places in a crèche, holiday childcare, emergency care options and care for the elderly.

Digitalisation and advancing technological progress are changing the possibilities and conditions in the working world. For example, the option of alternating telecommuting was further expanded in the reporting year. A total of 38 employees took advantage of the opportunity of doing part of their work at home.

In addition to the compatibility of family and career, the health of its employees is important to the Bank. To promote health, Deutsche Hypo offers a company counselling service through an external service provider, for example. The Bank also offers all employees over the age of 45 a medical check-up and health coaching programme every three years. Furthermore, the Bank makes efforts to further promote measures aimed at sensitising and qualifying management staff with regard to “healthy” leadership. In 2017, the Bank plans to establish the model it has developed to help it analyse mental health risks throughout the company.

Cooperation with the works Council

The constructive partnership with the Works Council founded on trust made it possible to find good solutions and answer to the various challenges, for which we would like to sincerely thank Deutsche Hypo’s social partner for this.

	31.12.2016	31.12.2015	31.12.2014	31.12.2013
Employees	395	390	387	410
of which: male	221	221	220	237
of which: female	174	169	167	173
Employee structure				
Trainees	13	11	12	11
Average age	44.0	43.6	44.4	43.5
Other				
Illness rate (in %)	3.31	3.67	3.03	4.49
10-year service anniversary (number of employees)	13	4	6	7
25-year service anniversary (number of employees)	5	7	4	4
40-year service anniversary (number of employees)	1	2	4	2

CORPORATE GOVERNANCE REPORT

Deutsche Hypo reaffirms its full commitment to the principles of good corporate governance. Corporate governance characterised by a sense of responsibility and transparency is the foundation on which our sustainable success as a company is built. It also strengthens the trust of owners, customers, business partners, employees and financial markets in our Bank. Against this backdrop, we are committed to upholding the aims and intents of the German Corporate Governance Code, which contains recommendations and suggestions and is reviewed and adapted as necessary once a year by the Government Commission on the German Corporate Governance Code.

As the Government Commission did not make any changes or amendments to the Code last year, the version published in the official part of the federal gazette on 12 June 2015 continues to apply. The Government Commission announced at its meeting last year that changes to the Code were to be expected in 2017.

The Supervisory Board uses a questionnaire to regularly check the efficiency of its work and the work of the Board of Managing Directors. The Chairman of the Supervisory Board presented the results of the 2016 efficiency audit at the meeting of the Appointments Committee on 30 November 2016 and at the meeting of the Supervisory Board on 1 December 2016, discussing them in detail with the members of the respective boards. The findings indicated that the members of the Supervisory Board were satisfied to very satisfied with the structure, size, composition and performance of the Supervisory Board and the Board of Managing Directors. Significant measures to increase efficiency and/or improve the work of the Supervisory Board or cooperation between the Supervisory Board and the Board of Managing Directors were not identified.

The German Corporate Governance Code as amended on 5 May 2015 and the Declaration of Conformity of Deutsche Hypo, which the Supervisory Board adopted on 1 December 2016, have been made available on the Deutsche Hypo website at www.deutsche-hypo.de. The text is worded as follows:

Declaration of Conformity 2016
on the part of Deutsche Hypothekbank (Actien-Gesellschaft) Hanover
in respect of the recommendations of the
Government Commission on the German Corporate Governance Code

Since the last Declaration of Conformity dated 26 November 2015, Deutsche Hypothekbank (Actien-Gesellschaft) Hanover has implemented or is implementing the recommendations of the current Government Commission on the German Corporate Governance Code dated 5 May 2015 with the following exceptions:

Code section 2.3

The recommendations of the Code are based on the holding of Annual General Meetings of stock corporations which have various different shareholders. This is not the case for Deutsche Hypo as 100 % of the shares of Deutsche Hypo are held by NORD/LB. There are no “free” shareholders. For that reason these recommendations have not been and will not be implemented.

Code section 3.8

In accordance with the principles of equal treatment, a deductible ought to be identical for all Members of the Supervisory Board in terms of its economic effects. The Code recommends that the regulation on deductibles for the Board of Managing Directors in accordance with Article 93 (2) of the German Stock Corporation Act (AktG) be correspondingly applied in respect of the Members of the Supervisory Board. However, this would affect the Members of the Supervisory Board to varying degrees, depending on their personal economic circumstances. In extreme cases, it could be, for example, that less well financially situated Members of the Supervisory Board might find themselves in existential difficulties. Against this background a D&O policy without an appropriate deductible is in place for the Members of the Supervisory Board.

Code section 4.2.3

Pension commitments are basically granted to Members of the Board of Managing Directors taking into account the specific individual circumstances. The Supervisory Board will seek a pension level which takes into account these circumstances (including area of responsibility, position on the Board of Managing Directors and length of service on the Board of Managing Directors) and is also in reasonable proportion with other existing pension commitments. The assessment of the individual case is influenced by various factors which are difficult to define within a standard framework. The Supervisory Board has therefore not defined standard framework conditions regarding the pension commitments for the Members of the Board of Managing Directors.

Code sections 4.2.4 / 4.2.5 / 5.4.6

The Extraordinary General Meeting of Deutsche Hypothekbank held on 13 November 2006 adopted a resolution with the requisite majority as per Section 286(5) of the German Commercial Code (HGB) to the effect that individualised disclosure of the compensation of Members of the Board of Managing Directors would not be undertaken. At the Annual General Meeting of Deutsche Hypothekbank held on 25 May 2011, a resolution was adopted to the effect that the details on the compensation of each individual Member of the Board of Managing Directors as required by Section 4.2.4 of the German Corporate Governance Code will not be disclosed in the company's annual financial and consolidated statements.

In accordance with Deutsche Hypothekbank's articles of association, the Annual General Meeting passes resolutions on the compensation of the Members of the Supervisory Board. The Supervisory Board's overall compensation is reported in the Annual Report. There is no further identifiable benefit from any individualised disclosure by name of said compensation. For that reason the individual statement of the remuneration of the Members of the Board of Managing Directors and the Supervisory Board and the individual presentation of the respective remuneration components using the intended code sample tables have not been produced.

Code section 5.3.2

The recommendations of the Code provide inter alia that the Chair of the Audit Committee should be independent. Independence will not be given where there is a personal or commercial relationship with a controlling shareholder. In view of the fact that the Chairman of the Audit Committee is at the same time a Member of the Board of Managing Directors of the parent company NORD/LB, Deutsche Hypo does not comply with this recommendation. As, however, there is no doubt that the Chairman of the Audit Committee is guided by corporate interest in performing the role, the Supervisory Board is happy to go along with the current employment until further notice.

Code section 5.4.1

In May of last year the Code was amended in that the Supervisory Board should specify not only an age limit for Supervisory Board Members, but also a limit on the tenure within the Supervisory Board in terms of its composition. Against the background of affiliation to the 100 % parent company NORD/LB, Deutsche Hypo is interested in a Group-wide policy. As this is currently still being developed, the Bank does not comply with the recommendation to have a limit for tenure on the Supervisory Board in its articles of association.

Code section 7.1.2

As a subsidiary of NORD/LB, Deutsche Hypo is incorporated into the Group procedure in terms of the publication of interim reports, financial reports and annual statements; This is based on the statutory deadlines in accordance with section 325 German Commercial Code (HGB), section 37v and section 37w German Securities Trading Act (WpHG). Against this background the recommended deadlines of 90 and 45 days for the publication of the management report and the half-yearly financial report were not complied with in 2016. It cannot be ruled out that this will also be the case in the coming year 2017.

Hanover, 1 December 2016

The Supervisory Board

The Board of Managing Directors

REPORT BY THE SUPERVISORY BOARD

The Supervisory Board of Deutsche Hypo and its committees performed the tasks required of them by law, the Bank's articles of association and the German Corporate Governance Code in 2016. In turn, the Board of Managing Directors informed the Supervisory Board regularly, promptly and comprehensively about the development of business and the risk situation, as well as about the strategic focus and economic position of the Bank. Regular information was also provided in the form of quarterly risk reports in accordance with the provisions of MaRisk and monthly reports on the business development and income position of the Bank. Furthermore, topics of fundamental importance, such as changes to the business and risk strategy, were discussed in detail with the Board of Managing Directors.

The Supervisory Board and its committees advised management, monitored its actions and passed resolutions on the issues and transactions requiring their approval under the articles of association and the rules stipulated within their framework. The corresponding drafts for resolution were at all times presented to the Supervisory Board sufficiently in advance for it to make a decision. Resolutions were adopted by way of a written circulation procedure if their adoption became necessary between meetings.

Deutsche Hypo's committees – the Lending and Risk Committee, the Audit Committee, the Appointments Committee and the Remuneration Committee – enhance the efficiency of the Supervisory Board's work. They address specific, business-related matters and usually prepare the Supervisory Board resolutions.

The Supervisory Board held four ordinary meetings and one constitutive meeting in 2016, which – with the exception of the absence of one member at one meeting – were attended by all members of the Supervisory Board. At the meetings, the respective chairs of the committees briefed the Supervisory Board on the work of their committees at regular intervals. There was also a constant exchange of information between the Supervisory Board chairman and the committee chairs between the meetings. In addition, the Chairman of the Board of Managing Directors was in regular and close contact with the Chairman of the Supervisory Board in order to discuss important questions and decisions in one-on-one meetings.

The Supervisory Board was made up of just five members for two months after Mr Eckard Forst resigned from the Supervisory Board effective 31 October 2016. Because the Chairman of the Supervisory Board, Dr Gunter Dunkel, stepped down from the Supervisory Board at his own request effective 31 December 2016, the Annual General Meeting of Deutsche Hypo was tasked with appointing two new Supervisory Board members. The decision was made at an extraordinary Annual General Meeting on 1 December 2016, at which the then designated and now incumbent members of the Board of Directors of NORD/LB Günter Tallner and Christoph Dieng were elected to the Supervisory Board of Deutsche Hypo effective 1 January 2017. Mr Thomas S. Bürkle was elected Chairman of the Supervisory Board at the constitutive meeting of the Supervisory Board on 1 December 2016. At the same meeting, Günter Tallner was elected Vice-Chairman of the Supervisory Board. Furthermore, the meeting also passed a resolution on the reorganisation of the committees.

The Lending and Risk Committee, which mainly deals with the performance of the loan portfolio and its risks, met four times last year. The Audit Committee met twice, in particular to discuss the annual financial statements and half-yearly financial report as well as the findings of the internal and external audits and compliance issues. In addition, four meetings of the Remuneration Committee and three meetings of the Appointments Committee were held. The Remuneration Committee focuses on monitoring the appropriate structuring of the remuneration system for management staff and employees, whereas the Appointments Committee is mainly concerned with nominating appropriate candidates for election to the Supervisory Board by the Annual General Meeting and examining the findings of the annual efficiency audit of the Supervisory Board and the Board of Managing Directors. The committee members fundamentally attended all committee meetings in 2016, with the exception of two Lending and Risk Committee meetings and two Remuneration Committee meetings. One member was absent from each of these meetings and was either represented by a proxy or submitted his or her votes prior to the meeting.

The auditor KPMG AG Wirtschaftsprüfungsgesellschaft, Hanover, which was elected by the Annual General Meeting and subsequently appointed by the Supervisory Board, audited the financial statements for the financial year 2016 and issued an unqualified audit certificate. This confirms that the bookkeeping and annual financial statements comply with the statutory requirements. The audit did not lead to any objections.

The auditor was available to the members of the Supervisory Board and of the Audit Committee to take questions and provide additional information. The auditor took part in the Supervisory Board meeting on the annual financial statements in March 2016 and in the meetings of the Audit Committee in March and August 2016, reporting on the findings of the audit during these sessions.

The audit report was discussed in depth by the members of the Supervisory Board. The Supervisory Board agreed to the findings of the auditor's report. At its meeting on 22 March 2017, the Supervisory Board approved the management report and the annual financial statements as of 31 December 2016, which are hereby adopted.

The Supervisory Board would like to expressly acknowledge Deutsche Hypo's successful financial year and thank the members of the Board of Managing Directors as well as all employees for their outstanding commitment and excellent work in 2016.

Hanover, 22 March 2017

The Supervisory Board



Thomas S. Bürkle
Chairman of the Supervisory Board

CORPORATE BODIES

Supervisory board

DR. GUNTER DUNKEL

Hanover

Chairman of the Board of Managing Directors of Norddeutsche Landesbank Girozentrale

– Chairman until 31 December 2016 –

ECKHARD FORST

Hanover

Member of the Board of Managing Directors of Norddeutsche Landesbank Girozentrale

– Vice chairman until 31 October 2016 –

THOMAS S. BÜRKLE

Hanover

Member – since 1 January 2017 Chairman – of the Board of Managing Directors of Norddeutsche Landesbank Girozentrale

– Vice chairman from 1 November 2016 – 31 December 2016 –

– Chairman since 1 January 2017 –

GÜNTER TALLNER

Hanover

Member of the Board of Managing Directors of Norddeutsche Landesbank Girozentrale

since 1 January 2017

– Vice chairman –

CHRISTOPH DIENG

Hanover

Member of the Board of Managing Directors of Norddeutsche Landesbank Girozentrale

since 1 January 2017

THOMAS KRÜGER

Hanover

Member of the Board of Managing Directors of VGH Versicherungen (retired)

DIRK METZNER

Hanover

Bank employee

ANDREA BEHRE

Hanover

Bank employee

Committees of the Supervisory Board until 31.10.2016

Lending and risk committee

THOMAS S. BÜRKLE

– Chairman –

ECKHARD FORST

DR. GUNTER DUNKEL

THOMAS KRÜGER

– Substitute Member –

Audit committee

ECKHARD FORST

– Chairman –

DR. GUNTER DUNKEL

THOMAS KRÜGER

THOMAS S. BÜRKLE

– Substitute Member –

Appointments committee

DR. GUNTER DUNKEL

– Chairman –

ECKHARD FORST

THOMAS S. BÜRKLE

Remuneration committee

DR. GUNTER DUNKEL

– Chairman –

ECKHARD FORST

THOMAS S. BÜRKLE

DIRK METZNER

Committees of the Supervisory Board 01.11. – 31.12.2016

Lending and risk committee

THOMAS S. BÜRKLE

– Chairman –

DR. GUNTER DUNKEL

THOMAS KRÜGER

Audit committee

THOMAS S. BÜRKLE

– Chairman –

DR. GUNTER DUNKEL

THOMAS KRÜGER

Appointments committee

DR. GUNTER DUNKEL

– Chairman –

THOMAS S. BÜRKLE

Remuneration committee

DR. GUNTER DUNKEL

– Chairman –

THOMAS S. BÜRKLE

DIRK METZNER

Committees of the Supervisory Board since 01.01.2017

Lending and risk committee

CHRISTOPH DIENG

– Chairman –

GÜNTER TALLNER

THOMAS S. BÜRKLE

THOMAS KRÜGER

– Substitute Member –

Audit committee

GÜNTER TALLNER

– Chairman –

THOMAS S. BÜRKLE

THOMAS KRÜGER

CHRISTOPH DIENG

– Substitute Member –

Appointments committee

THOMAS S. BÜRKLE

CHRISTOPH DIENG

GÜNTER TALLNER

Remuneration committee

THOMAS S. BÜRKLE

– Chairman –

CHRISTOPH DIENG

GÜNTER TALLNER

DIRK METZNER

Board of Managing Directors

ANDREAS POHL

Hanover

– Chairman of the Board of Managing Directors –

SABINE BARTHAUER

Hanover

ANDREAS REHFUS

Hanover

Public trustees

WOLFDIETRICH KÜHNE

Hanover

Degree in business, auditor, tax advisor

– Trustee –

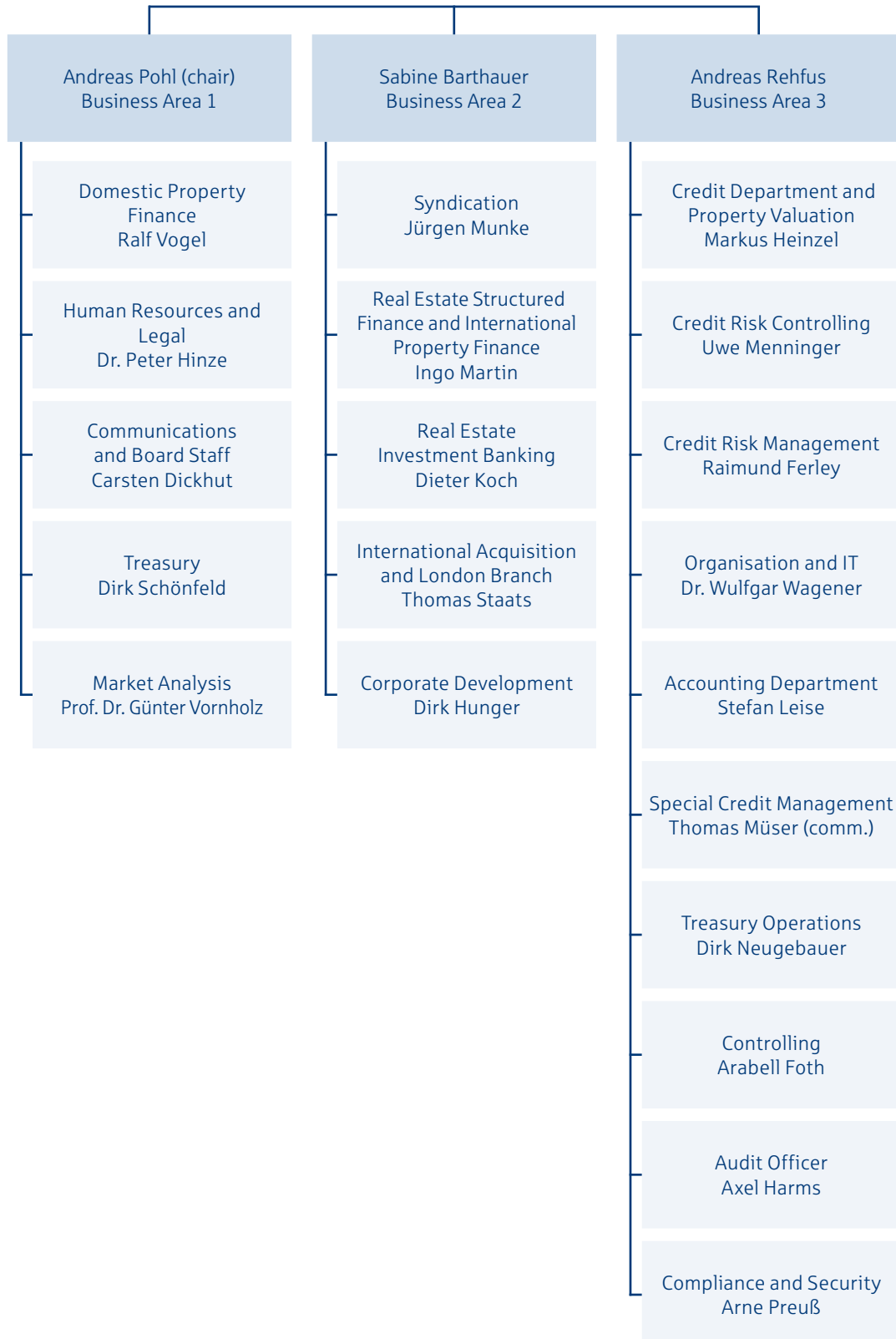
DORIS VOGEL

Hanover

Tax advisor

– Deputy trustee –

ORGANISATIONAL STRUCTURE



ADDRESSES IN GERMANY AND ABROAD

Management

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The Netherlands: 1077 XX Amsterdam

Zuidplein 108 · WTC Tower H / 13 · Tel.: +31 20 6914551 · Fax: +31 20 6919811

Poland: 00-021 Warszawa

ul. Chmielna 25 · Tel.: +48 22 8280253 · Fax: +48 22 6924428

Supervisory body

Europäische Zentralbank (EZB) · Kaiserstraße 29 · 60311 Frankfurt/Main

Bundesanstalt für Finanzdienstleistungsaufsicht · Graurheindorfer Straße 108 · 53117 Bonn

GLOSSARY

Backtesting

Process to monitor the quality of value-at-risk models, which retrospectively compares losses calculated using the value-at-risk approach with the losses actually recorded.

Cost-income ratio (CIR)

Ratio that puts administrative expenses in relation to net interest and commission income. The cost-income ratio provides quantitative information regarding the efficiency in the operative banking business. In principle, the lower the value of the cost-income ratio, the more efficient the Bank's economic management.

Credit Default Swap (CDS)

CDSs belong to the group of credit derivatives. In this case, the secured party transfers only the isolated credit default risk to the party granting security.

Credit spread risk

The risk of potential changes in value that arises if the individual credit spread of the issuer, borrower or debtor, which is used in the context of a market assessment of the position, changes.

Derivative or derivative financial instrument

Derivatives or derivative financial instruments are financial assets and liabilities the value of which changes depending on a defined underlying asset (interest, currency, share, etc.). Derivatives require no or very little initial investment and will be discharged in the future.

Expected Loss (EL)

Calculated loss of a financing or a customer within one year. The EL is an expected value that results from exposure at default (EAD), probability of default (PD) and loss given default (LGD) calculated, and specifies the standard risk costs of a loan.

IFD risk class default (Non performing loans – NPL)

This refers to loans for which the debtors have already fallen into arrears in fulfilling their contractual obligations.

Confidence level

Within the context of the value-at-risk model, the confidence level describes the likelihood that a potential loss will not exceed the loss threshold defined by the value-at-risk.

Deferred taxes

If the amounts stated in the tax balance sheet differ from the book values for the assets and liabilities in the balance sheet pursuant to the Code of Commercial Law and these differences are not permanent from a fiscal perspective, income taxes to be paid or obtained in future will be applied as deferred taxes.

PfandBarwertV

Pfandbrief Net Present Value Regulation: Regulation on the safeguarding at all times of the cover for Mortgage Pfandbriefe, Public Pfandbriefe and Ship Pfandbriefe according to the net present value and the calculation of the same in the case of Pfandbrief Banks.

Rating

Standardised assessment of the credit-worthiness of a security or debtor by means of a detailed internal risk assessment (internal rating) or by independent rating agencies (external rating).

Risk-bearing capacity

To safeguard the risk-bearing capacity within a credit institution, all significant risks must be covered at all times by the risk coverage potential (capital that is actually available).

Scoring procedure

Deutsche Hypo's internal rating procedure to determine the credit-worthiness of a debtor in the capital market business.

Hedging instrument

Derivative or non-derivative financial instruments where it is expected that their fair value or cash flows will offset changes to the fair value or cash flow of a designated basic transaction in an effective hedging relationship.

“Using Synergies in the Group” (SIGN)

An efficiency improvement programme launched at Deutsche Hypo in 2012. As well as cost optimisations, closer ties to NORD/LB are envisaged through procedural and methodological adjustments.

Spread

In exchange and off-exchange trading, a spread (also known as bid-ask spread) is defined as the margin between the bid price (market demand) and the offer price (market supply).

Stress testing

Future analysis that institutions apply in addition to the regular risk control mechanisms and with which they simulate the impact of unusual but potentially possible events.

Swap

In economics, a swap is an agreement between two contracting parties that provides for the future exchange of payment flows.

Total Return Swap (TRS)

In a Total (Rate of) Return Swap (TRORS or TRS), the return from the underlying financial instrument is exchanged for a different return. This is a credit derivative.

Unexpected Loss

Quantification of the credit risk as the potential difference between the actual and expected loss.

Value-at-risk (VaR)

The value-at-risk designates the potential future loss that will not be exceeded within a certain period and with a certain probability.

Waiver provision

Exceptional provision pursuant to section 2a German Banking Act (KWG), old version, that enables banks affiliated to the group to be exempted from the minimum capital requirements, the requirements relating to large exposure reports as well as the requirements for proper business organisation pursuant to section 25a (1) KWG, provided the requirements set out in the law are satisfied. The responsibility for these requirements then passes to the upstream institute.

DEUTSCHE HYPO

Member of NORD/LB

Deutsche Hypothekenbank

(Actien-Gesellschaft)

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