

Annual Report

**2018**

Your success is : our benchmark

# DEUTSCHE HYPO AT A GLANCE

in € millions	01.01.- 31.12.2018	01.01.- 31.12.2017	Change (in %)
<b>New business figures</b>			
Commercial real estate finance business	2,869.8	3,798.3	- 24.4
Domestic finance	1,698.4	2,180.9	- 22.1
Foreign Finance	1,171.5	1,617.4	- 27.6
Funding volume	2,327.1	3,526.3	- 34.0
Mortgage Pfandbriefe	1,722.8	1,328.0	29.7
Unsecured	604.3	2,198.3	- 72.5

in € millions	31.12.2018	31.12.2017	Change (in %)
<b>Portfolio figures</b>			
Commercial real estate finance business	12,264.0	12,077.1	1.5
Domestic finance	6,878.0	7,079.6	- 2.8
Foreign finance	5,386.0	4,997.5	7.8
Loans to local authorities	2,844.4	3,892.5	- 26.9
Securities	4,716.6	5,489.9	- 14.1
Funding capital	19,616.7	22,254.0	- 11.9
Mortgage Pfandbriefe	8,128.1	8,414.1	- 3.4
Public Pfandbriefe	3,806.9	4,490.4	- 15.2
Unsecured	1,784.3	2,677.4	- 33.4
Other liabilities	5,897.4	6,672.1	- 11.6
Equity *)	1,232.1	1,252.1	- 1.6
Balance sheet total	21,072.8	23,698.3	- 11.1

in € millions	01.01.- 31.12.2018	01.01.- 31.12.2017	Change (in %)
<b>Income figures</b>			
Net interest income	177.4	193.4	- 8.3
Net commission income	- 0.1	0.3	<- 100.0
Administrative expenses **)	84.0	83.8	0.2
Risk result	- 20.3	- 41.3	50.8
Income from securities and participatory interest	9.1	- 10.2	>100.0
Result from normal operations	74.7	62.7	19.1
Extraordinary result	- 16.5	0.7	<- 100.0
Interest on investments by silent partners	0.0	3.5	- 100.0
Profit before taxes and profit and loss transfer	58.2	59.9	- 2.8

in %	31.12.2018	31.12.2017
<b>Other information</b>		
Cost-income ratio	49.5	42.3

\*) 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 2018**





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# FOREWORD BY THE CHAIRMAN OF THE SUPERVISORY BOARD

Dear Customers  
and Business Partners of Deutsche Hypo,

The commercial real estate business has been in upswing for many years. In fact, the transaction volume in excess of € 60 billion is a new record in Germany. Both national and international investors are highly active in this segment, which continues to afford good investment opportunities despite the fall in availability of premium properties.

The strong market performance goes hand-in-hand with an intensification of competition between the financiers of commercial real estate. Deutsche Hypo continues to meet this challenge head on. With its quality-oriented approach to business and its employees' extensive expertise, the Bank more than holds its own on the market and has cultivated many close and longstanding customer relationships – both as a financier and also a Pfandbrief issuer. Year by year, Deutsche Hypo proves itself to be a consistent profit driver in the NORD/LB Group.

Deutsche Hypo's financial year 2018 closed with a result from normal operations of just under € 75 million, actually exceeding the previous year's good result. The Bank used this positive business performance to bolster its contingency reserves yet further.





Foreword by the Chairman of the Supervisory Board | Interview with the Board of Managing Directors | 2018 at a glance | Sustainability | REECOX | References



Dear Customers and Business Partners, Deutsche Hypo is perfectly positioned to continue to support you in your transactions and projects and to generate added value for you.

Best regards,

A handwritten signature in blue ink, consisting of stylized initials and a long horizontal stroke.

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

# INTERVIEW WITH THE BOARD OF MANAGING DIRECTORS

In an interview, the Members of the Board of Managing Directors Sabine Barthauer and Andreas Rehfus cast an eye over the successful financial year 2018 and tell us how optimistic they are for the current year.

## How satisfied are you with the performance of the business in 2018?

**Rehfus:** We successfully increased the result from normal operations by almost 20 %. This is remarkable in view of the highly challenging prevailing conditions and is testament to how hard our colleagues have worked over the entire year. We have benefited in particular from the development of our risk provisions, which saw net releases in our core business area. We also benefited from special effects such as the sale of the debtor warrant of Heta Asset Resolution AG.

**Barthauer:** On the bottom line we can be happy with how things went in financial year 2018. Even if new business levels remained below expectations due to the intensification of competition in commercial real estate financing, we did see small increases in the portfolio. What matters for us is primarily portfolio quality, which we maintained at a very high level. We took advantage of the opportunities for new business that presented themselves in our target markets and again acquired high-quality finance, primarily in our core market of Germany, of course.

## The current real estate cycle is lasting an unusually long time. How do you assess the development?

**Barthauer:** The transaction volume in Germany has never been higher than it was last year. Yet I think would be bold to conclude that the upturn on the commercial real estate market will persist much longer because the growth trajectory has already lost some momentum. It's been the case for a while that not everything is being bought, let alone financed. Price limits seem to have been reached in a lot of places. Although the continuing low-interest phase and the robust economy mean that the prevailing conditions for our sector remain good or very good – the job market is booming, employment is increasing and real salaries are also on the rise – the geopolitical uncertainties still pose a risk that should not be underestimated.

**Rehfus:** Of course, we know that a cycle will come to an end at some point. All properties financed by us therefore need to meet our strict quality requirements. The good risk result and the historically low NPL rate underline the fact that our quality-oriented issue of loans proves its worth. Risk costs that do not materialise are certainly an important component of the result for us.

## How optimistic are you that you will be able to continue the positive business performance of the previous years in 2019?

**Barthauer:** We certainly started the new year with a tailwind. Although we know that there will always be a lot of competition on the market as long as the prevailing conditions for our sector are so positive, our structuring expertise will continue to set us apart. Our customers know that they can rely on us at least 100 % – not only in Germany, but also in our other core markets of the UK, France, Benelux, Poland and Spain. For us and other market actors alike, further development of the business will depend on external factors, be that the how Brexit pans out, possible trade tariffs or geopolitical crises.



## “Our focus on quality continues to prove its worth”



From left: Sabine Barthauer, Andreas Rehfus

**Rehfus:** The long upturn has resulted in a situation where some risk positions are at a historical low. We can assume that these will revert to their longstanding average values, at least in the medium to long term. However, for the current year we expect a largely stable earnings performance overall. We will use the year to continue investing in the Bank's infrastructure and increasing the digitalisation of our processes. Additionally, we will be implementing a cost-saving programme for a more efficient structure of our business operations. I am convinced that our strict quality focus will continue to prove its worth in future.

# The year 2018 at a glance

## 31 January 2018

Deutsche Hypo successfully taps a benchmark mortgage Pfandbrief set up in 2015 by € 250 million. The Pfandbrief now has a volume of € 750 million and a coupon of 0.125 %. The residual term is around four years. After the order book was opened, over 20 orders with a volume of more than € 300 million are quickly received.

## 15 March 2018

Deutsche Hypo places a benchmark mortgage in pounds sterling (GBP) for the first time. The issue with a volume of GBP 325 million has a term of three years. The coupon on the GBP floater is + 27 basis points above the 3-month GBP LIBOR. The issue price was 99.85 %. The order book consisted mainly of large-volume orders from Germany, the UK and Norway.

## 27 April 2018

Deutsche Hypo and bulwiengesa AG jointly launch a new economic index: The Deutsche Hypo Real Estate Economy Index (REECOX) aims to give a regular overview of trends on the real estate markets in Germany, the UK, France, Poland, Spain and the Netherlands. It provides a profound and quick overview of the respective development on Europe's key real estate markets.

## 23 May 2018

Deutsche Hypo publishes a new study about the French real estate market. The study says that the French real estate market overall is benefiting from the economic upturn and can considerably increase its attractiveness. The dynamic upturn can be seen in the high demand for first-rate commercial properties, above all in the Île-de-France region, and also in regional real estate markets such as Lyon, Lille or Marseilles.

## 30 May 2018

Deutsche Hypo finances the construction of the contemporary office building "The Oval" for GERCH-GROUP at Düsseldorf's established office location Kennedydamm. The mid-double-digit million loan is provided for a total term of two years. Deutsche Hypo is the sole lender. A contemporary, ring-shaped, nine-storey office building is being built on a gross floor space of some 15,300 square metres.

**21 June 2018**

Deutsche Hypo successfully issues a benchmark mortgage Pfandbrief. The loan with a volume of € 500 million has an eight-year term and a coupon of 0.50 %. With an issue price of 99.02 %, the yield is 0.626 %, corresponding to a return discount of five basis points at mid-swap. Transaction support for Deutsche Hypo comes from joint leads Commerzbank, Crédit Agricole CIB, Helaba, NORD/LB and UniCredit.

**30 August 2018**

Deutsche Hypo achieved results from normal operations of € 33.9 million in the first half of 2018 (first half of 2017: € 35.2 million), continuing the Bank's positive earnings performance in 2018. The Bank has again been able to boost its contingency reserves and further increase its portfolio quality – both in the real estate finance and also in the capital market business.

**3 September 2018**

On this date Deutsche Hypo issues its second Green Pfandbrief. The issue totalling € 500 million has a term of 6¼ years. The coupon is 0.25 %. When issuing its first Green Pfandbrief in 2017, the Bank added a green sub-portfolio to its mortgage cover pool. Since that time, comprehensive reports on this portfolio have been published, which are consistently updated.

**14 September 2018**

Deutsche Hypo publishes a new real estate special study about the Spanish real estate market. This study concludes that the markets for office, retail, hotel and logistics properties are each on a growth trajectory and that this looks set to continue. The attractiveness of Spain, in particular the major cities of Madrid and Barcelona, is apparent in the high demand for first-class commercial real estate. The supply of space is becoming increasingly scarce.

**20 September 2018**

Deutsche Hypo and Stadtsparkasse Düsseldorf finance the purchase of the land for the “Ulmenstraße project development” in Düsseldorf for a property company of the INTERBODEN Group. The plot is located centrally in the Derendorf district, on part of what was Düsseldorf's “Ulmer Höh” prison. The intention is to build primarily residential and commercial property on the land. The mid-double-digit million financing volume will be provided for a total term of two years.

# SUSTAINABILITY

As one of Germany's oldest Pfandbrief banks, Deutsche Hypo combines decades of tradition and experience in real estate financing with responsible corporate governance and a forward-looking strategy. Sustainability is thus one of the Bank's principal fields of action. It is therefore our mission to ensure the sustained profitability of Deutsche Hypo and thus to secure future income and jobs in the long term. In real estate financing, the Bank plays a role in the spatial design of many cities as a funding partner. Quality, professionalism and sustainability of the financing project are major factors in selecting the projects.

The Bank's sustainability strategy, which is updated annually, addresses the central aspects of global change for Deutsche Hypo and its customers and investors and shows how opportunities that arise are realised efficiently and risks managed responsibly. The Bank has identified five fields of action and has made them strategic priorities: governance, customers and investors, employees, society, and environment.

In 2018, Deutsche Hypo again expanded its sustainability activities as planned. The Bank conducted its first external stakeholder survey in order to better understand the needs of its stakeholder groups and manage them accordingly. As regards of its core business, the Bank set up its extensive green bond reports following the issue of its first Green Pfandbrief in September 2017. The reports provide investors with information about important details of the green buildings and are regularly made available on the website. The first health day for the Bank's employees, at which information about a wide range of topics to do with staying healthy was distributed, was held in 2018. There were also numerous internal personnel development measures. Further information is provided in the 2018 Sustainability Report. This will be available on the website <http://www.deutsche-hypo.de> by no later than 30 June 2019. The Bank will also submit a Declaration of Conformity with the German Sustainability Code. This will be provided over the course of the year at <http://www.deutscher-nachhaltigkeitskodex.de>.

## Honours for outstanding personalities in cancer research



Prize award 2019 (from left): Prof. Dr. Michael Manns, Chairman of the Board of Trustees of the Johann Georg Zimmermann prize and MHH President, PD Dr. Sebastian Kobold, winner of the Johann-Georg-Zimmermann prize and Andreas Rehfus, Member of the Board of Managing Directors of Deutsche Hypo. Prof. Christa Fonatsch, winner of the Johann Georg Zimmermann medal was absent due to illness.

The Johann Georg Zimmermann research prize and the Johann Georg Zimmermann medal are among the highest awards for accomplishments in cancer research in Germany. Deutsche Hypo endows both prizes annually, and this year they were handed out at Hanover Medical School (MHH) on 11 February 2019.

The Johann Georg Zimmermann research prize 2018/2019, endowed with € 10,000 and aimed at young doctors in cancer research for their current scientific work, was awarded to PD Dr. Sebastian Kobold, senior physician in the department of clinical pharmacology at the university hospital of the Ludwig-Maximilians-Universität München. His research focus

is tumour immunology and the development of immune therapies for treating tumour diseases. An important approach here was the deployment of genetically modified T cells and receptors developed in house to enable more effective deployment of immune cells against tumour cells.

The Johann Georg Zimmermann medal 2018/2019, endowed with € 2,500, was awarded to Professor Christa Fonatsch, emeritus professor and former director of the Institute for Human Genetics at the University of Vienna. Professor Fonatsch is a pioneer in tumour cytogenetics and her groundbreaking work has cast light on many chromosomal anomalies in leukaemias and solid human tumours. Professor Fonatsch has long-standing connections to the MHH. From 1973 she worked at the Institute for Human Genetics, where she also laid the foundation for the successes of her future tumour-cytogenetic working groups over the next ten years.

### Christmas wishing tree keeps growing

The employees of Deutsche Hypo organised a “Christmas Wishing Tree” for the ninth year running. This year the wish lists of 103 children hung from the large Christmas tree in the Deutsche Hypo foyer. The colleagues were able to select a wish of their choice and make it come true. Around € 20 was to be invested per wish, including for toys, cuddly animals, CDs, books or bed linen.

The presents went to the children of the “Guldene Sonne” organisation. The Guldene Sonne works closely with the children's and young people's psychiatric unit at Hanover Children's Hospital. The children and young people who live at the centre have often had to leave their homes after experiencing domestic violence, problem relationships or even alcohol and drug abuse.



Works Council member Christina Kanning (l.) and communication manager Bettina Thiedtke (r.) hand over the presents on behalf of the employees of Deutsche Hypo.

### From person to person

Deutsche Hypo took part in the Hanover Social Day for the first time in 2018. Twice a year the Hanover Volunteer Centre urges companies to volunteer for the public good. For one day people can exchange their everyday workplace for work in a community project. On 14 September 2018 eight committed employees of Deutsche Hypo set off to spend the day with the residents of the Sophienresidenz old people's home in the Hanover district of Döhren. On a glorious autumn day, the participants started by visiting the weekly market on Fiedeler Platz. Back at the home, the day ended with a communal lunch and a tour of the building.





**REECOX** –  
a real estate index for  
Europe



Foreword by the Chairman of the Supervisory Board | Interview with the Board of Managing Directors | 2018 at a glance | Sustainability | REECOX | References



In April 2018 Deutsche Hypo published the Deutsche Hypo Real Estate Economy Index (REECOX) for the first time – in six countries in the respective local languages. Data was previously only collected about the German real estate economy. However, a comparison of various markets such as the UK, France, the Netherlands, Spain and Poland is important for many market participants. After all, pan-European portfolio strategies also require pan-European benchmarking tools. The REECOX fills this gap, creating important transparency.

2012 ushered in a highly successful innovation for the Deutsche Hypo's external image. Launched in 2008, the real estate economic index – produced by research company bulwiengesa – was renamed the Deutsche Hypo-Index on 31 January 2012 and then published monthly by the Bank. Thereafter the index firmly established itself in the real estate business and was generally respected as an early indicator. The Deutsche Hypo-Index consisted of two components: the real estate economy and the real estate climate. The economy represented the result of macro-economic data, whilst the climate portrayed the results of a survey of around 1,200 professional actors in the real estate economy. Their responses produced a reflection of sentiment in the German real estate industry. The current business situation and the expectations of the real estate experts were surveyed.

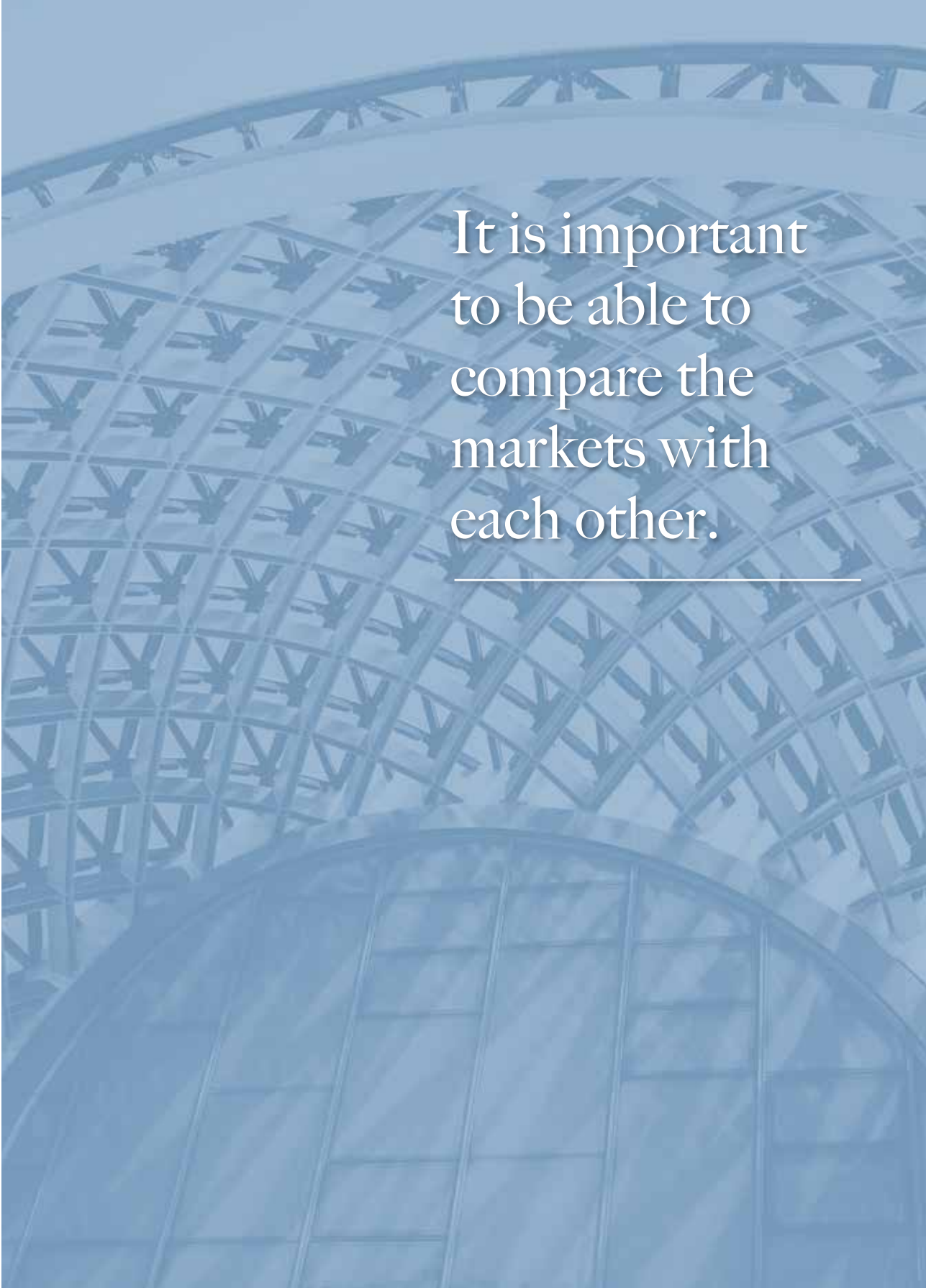
Around one-and-a-half years ago, it was time for something new: The Bank decided to restructure the Deutsche Hypo-Index in order to offer customers and market participants added value. After extensive research it quickly became apparent that there was something missing on the market: to date there was no index that enabled the individual European real estate target markets to be compared with one another. Real estate investors are also increasingly operating across borders and pursuing pan-European investment strategies, so it is important to be able to compare the markets with each other. The idea for the REECOX was born.



These two components of the Deutsche Hypo-Index were separated out. Whilst the sentiment has been published separately as the Deutsche Hypo Real Estate Climate since that time, the real estate economy was transformed into the Deutsche Hypo REECOX. The real estate economy has been transformed into the Deutsche Hypo REECOX. The challenge was to find comparable values for six different countries – Germany, France, Spain, UK, the Netherlands and Poland – in order to depict the respective real estate markets. Here the expertise of bulwiengesa was a key factor. The methodology for determining the REECOX is essentially based on the calculation of the German real estate economy.

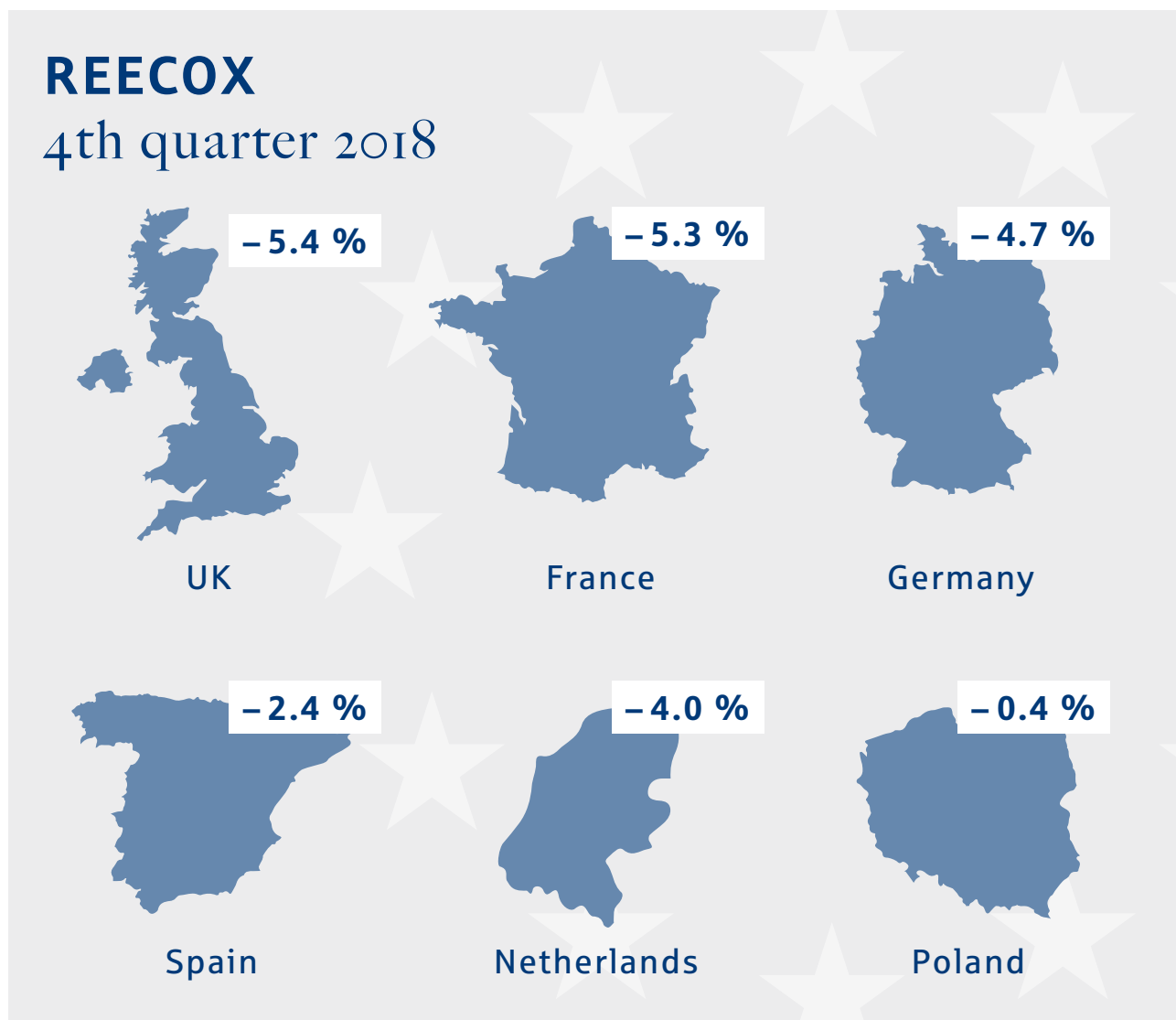
A total of five input variables that exhibit a high correlation across the real estate markets and can be easily combined to serve as a leading indicator were used. In Germany these are the DAX, the DIMAX (leading index for real estate shares), the European Commission's ESI sentiment indicator, the base interest rate pursuant to section 247 BGB and the interest rate for ten-year German federal bonds. The corresponding equivalents are used in the other countries, meaning that the individual markets can be compared with one another.





It is important  
to be able to  
compare the  
markets with  
each other.

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After the methodology for determining the REECOX had been settled, the next steps were initiated: the name REECOX was created, the corresponding logo developed and protected, the reporting layout decided, and a new website created. Additionally, the REECOX report is published not only in German, but also in the national languages English, Spanish, French, Polish and Dutch. This is crucial for marketing in Deutsche Hypo's target markets.

The real estate climate is still published monthly for the German market, whilst the REECOX reports are produced quarterly. The economic values are updated monthly on the website <http://www.deutsche-hypo-reecox.de>. The REECOX has been well received by the press: the resonance at press conferences has been very positive.

#### **Development of the REECOX at the end of the fourth quarter 2018**

Whilst no clear trend was apparent in recent quarterly reports and the European real estate economy (Euro-Score) was subject to fluctuations, the tendency at the end of 2018 is clear: Currently the REECOX Euro-Score stands at 233.9 points and is thus at its lowest point for two years. No clear driver for the current development can be identified. Instead, the majority of the countries considered by the REECOX exhibit downward trends – albeit to different intensities. The clearest negative fluctuations were apparent in the UK (– 5.4 %) and France (– 5.3 %), whilst the Polish real estate



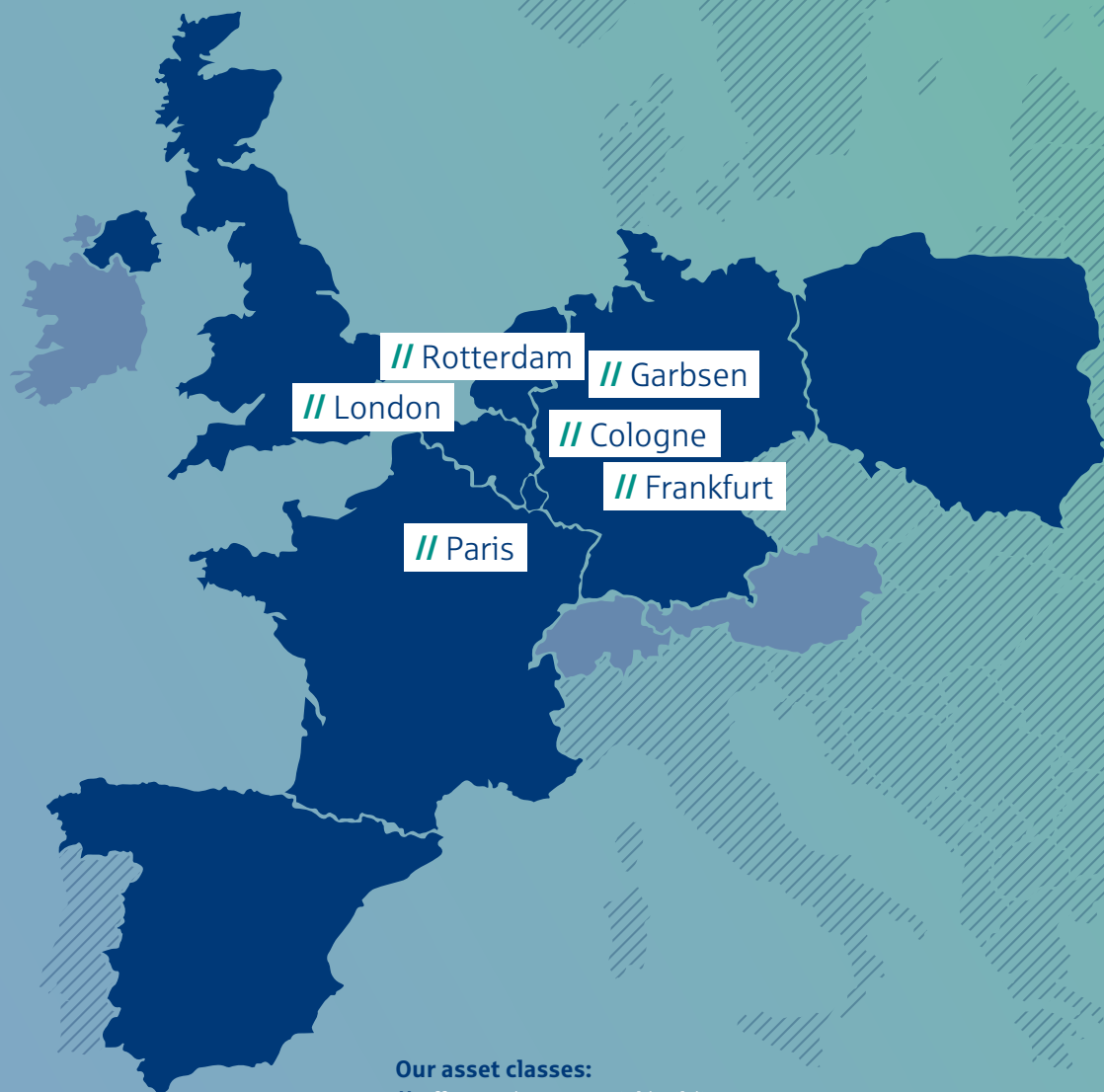
economy practically stagnated (– 0.4 %). In terms of the whole of 2018, Poland (– 0.9 %) also stands out as a positive example, whilst the annual review in all other countries is consistently negative. The largest losses were apparent in France (8.6 %), whilst the fall in Germany (– 4.7 %) was the least severe.

#### **Development of the real estate climate in February 2019**

Following the positive start to the year in January, the 134th monthly survey of the Deutsche Hypo real estate climate also showed an upward trend in February. Compared with the previous month, the count rose by 1.6 % and now stands at 125.0 points. Although the level is still significantly below the previous year's values, the general sentiment seems to have recovered from the significant decline at the end of 2018. Whilst the investment climate is stagnating, the income climate contributed to the positive development with a growth of 3.2 %.

# Our references

Deutsche Hypo's portfolio offers a wide range of interesting financing options across all of the bank's target markets and asset classes. Below is an exemplary list of six references



**Our asset classes:**

- // Office and commercial buildings
- // Retail
- // Hotels
- // Multi-storey residential
- // Logistics



Source „HG Esch“

## Gerling Quartier

**Type of property:** Office building and hotel

**Location:** Cologne

**Customer:** King Holding GmbH, a Joint Venture of Quantum Immobilien AG  
and PROXIMUS Real Estate AG



## Logistics Centre Garbsen

**Type of property:** Logistics property

**Location:** Garbsen

**Customer:**

BAUM Logistik Immobilien GmbH

## Theodor-Heuss-Allee 100

**Type of property:** Office building

**Location:** Frankfurt am Main

**Financing volume:** € 105 million

**Customer:** Object Frankfurt THA 100 GmbH & Co. KG, a company of the RFR Group



## Woodwork

**Type of property:** Office building

**Location:** Paris

**Customer:** Joint Venture of L'Etoile Properties and an US investor







## Central Post

**Type of property:** Office building

**Location:** Rotterdam

**Financing volume:** € 56.0 million

**Customer:** Central Post I B.V

## Oxford Street

**Type of property:** Retail and residential building

**Location:** London

**Financing volume:** GBP 34.5 million

**Customer:** HEVF Oxford Street Sarl





# MANAGEMENT REPORT

The figures in the tables and charts in the management report are expressed in thousand euros (€ thousands), or million euros (€ millions). 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.

## 1 Fundamentals of the Bank

### 1.1 Deutsche Hypo's business model

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

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 will be achieved through the quality of the cover pools and the associated rating of the Pfandbriefe, and through the credit rating and standing of Deutsche Hypo in the area of unsecured bonds.

Commercial real estate finance is Deutsche Hypo's core business and produces over 90 % of the Bank's total net interest and net commission income. It bundles all the financing of customers that primarily generate their cash flow from real estate or regularly make significant real estate investments. The capital market business includes the securities, financial investment and derivatives business with banks as well as funding. Strategically Deutsche Hypo has been pursuing a reduction of the public sector finance portfolio for years, which is why the importance of this business area has considerably decreased for the Bank in the meantime. Selective new business with liquid securities is conducted solely for the purpose of liquidity and cover pool management.

Deutsche Hypo's business is affected by numerous external influential factors. This is mainly due to the economic and sector-specific framework conditions that impact business development and thus affect 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, influence the development of the Bank's portfolios. Regulatory framework conditions constitute an external influential factor for the development of Deutsche Hypo's business and income. The various funding options are also influenced, among other things, by developments on the international financial markets and Deutsche Hypo's ratings depending on the rating development and capital resource of the parent company NORD/LB. These also have an influence on the management of liquidity.

Deutsche Hypo's main corporate goals are to secure and increase corporate value, profitability and returns over the long term. The Bank thereby plans to further expand the significance of commercial real estate finance as the core business area in the future. Here the Bank aims to continue to be perceived as an attractive competitor with interesting finance offerings. It is also engaged in the selective and risk-appropriate strengthening of its market position in Germany and abroad. The strategic target markets are characterised by high target-customer concentration, a large portfolio of real estate and long-term positive development. Financing in its home market of Germany continues to account for the largest share of the commercial real estate finance portfolio.

In addition to the intensive support of customers on the financing side, the Bank is pursuing close collaboration with institutional investors such 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.

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 on its website. The current declaration of conformity according to the German Sustainability Code is also available at <http://www.deutscher-nachhaltigkeitskodex.de>. The sustainability report and the declaration of conformity pursuant to the German Sustainability Code are not part of this management report.

## 1.2 Group affiliation

Deutsche Hypo is a subsidiary of NORD/LB, which holds 100 % of its shares, and is included in its consolidated financial statements. The consolidated financial statements as at 31 December 2017 were published on 25 June 2018 in the German Federal Gazette. There is a control and 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. NORD/LB is, in turn, required to compensate for any loss that may arise at Deutsche Hypo. The control and 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 the control and profit and loss transfer agreement as well as the use of a waiver rule according to Art. 7(1) CRR, formerly Section 2a(1) of the German Banking Act (KWG), Deutsche Hypo is dependent on the Group's parent company NORD/LB. Additional significant dependencies exist regarding compliance with the Group's capital requirements, the development of the rating, liquidity and funding as well as controlling and organisation within the Group. There are also service relationships between Deutsche Hypo and NORD/LB as well as intra-group receivables and liabilities.

NORD/LB most recently published an ad-hoc announcement on 2 February 2019. Accordingly a considerable net loss is expected for financial year 2018 and the common equity tier 1 capital ratio will at times fall below the required regulatory threshold. The ad-hoc announcement states that the owners of NORD/LB have decided to focus on a joint solution with the current owners and the DSGV (Deutscher Sparkassen- und Giroverband e. V.) in the public sector. According to the ad-hoc announcement, this solution is to be defined in concrete terms during further discussions with the DSGV and needs to be coordinated with the relevant regulatory authorities under state aid law aspects. Regarding the resulting risks for Deutsche Hypo, please refer to section 4.1.2.4 "Dependencies of Deutsche Hypo on NORD/LB".



### 1.3 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 a medium-term plan 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. 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. RoRaC is also used as a supplementary performance indicator for business area management. Compliance with external requirements for regulatory performance indicators 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. Among other things, the supplementary performance indicators include the development of employee capacities and the sustainability rating, which underlines the importance of sustainable corporate governance.

### 1.4 Non-financial statement

Due to its number of employees, Deutsche Hypo is not required to issue a non-financial statement in accordance with Section 289b of the German Commercial Code (HGB). However, the Bank's sustainability report includes significant non-financial information. The report for financial year 2018 will be published on the Bank's website, <http://www.deutsche-hypo.de>, by 30 June 2019 at the latest. As a group company, Deutsche Hypo is also included in NORD/LB's non-financial statement. Deutsche Hypo's sustainability report and NORD/LB's non-financial statement are not part of this management report.

## 1.5 Corporate governance statement

Deutsche Hypo regularly publishes a voluntary declaration of conformity with respect to the Corporate Governance Code on the Bank's website under <http://www.deutsche-hypo.de>. A current overview of the legally required information about the proportion of women on the Supervisory Board, Board of Managing Directors and the two levels of management below the Board of Managing Directors is also provided on the Bank's website at the above address. Further information about the management of the company is included in the corporate governance report in the Bank's annual report. The publications on the Bank's website listed above (declaration of conformity, disclosures on the percentage of women in management, corporate governance report) are not part of this management report.

# 2 Economic report

## 2.1 Macroeconomic and sector environment

### 2.1.1 Economic performance in Germany and Europe

The previously very dynamic development in the eurozone did not continue in 2018. In fact, the upturn slowed more and more in the course of the year. With a 1.8 % increase in the real gross domestic product compared to the previous year, stable growth was however still achieved in the single currency area. This development was supported by the sustained decrease in unemployment and accompanying increase in employment. The unemployment rate decreased to 8.2 % on average for the year. However the expansion of real available income was slowed by the increase in the inflation rate compared to the previous year, which at times exceeded 2.0 %.

The slowdown of economic growth in Germany was somewhat more pronounced. Nevertheless the real gross domestic product still increased by 1.5 % for the year overall. The German economy suffered in particular from the increasingly worse global economic climate in 2018 caused by global risk factors. Especially the strain of international trade conflicts and the imminent Brexit had a negative impact on Germany's export-oriented economy. Domestic demand was the main pillar of growth even though consumption turned out weaker than expected. The positive development of the job market also continued, with the unemployment rate dropping to 5.2 % on the annual average.

### 2.1.2 Development of real estate target markets

The market environment was defined by growing political and economic uncertainties in reporting year 2018. Nevertheless the global transaction volume for commercial real estate exceeded expectations and reached a new record value of € 637.4 billion (2017: € 582.7 billion).



## German real estate market

In view of stable economic framework conditions, the positive development of Germany's investment market for commercial real estate continued in reporting year 2018. Investor interest in real estate remained high thanks to ongoing low interest rates. A new record value was reached in 2018 with a transaction volume of around € 60.3 billion (2017: € 56.8 billion). Prices continued to increase while the available supply decreased.

The development of the German office real estate market remained dynamic in 2018. With a transaction volume of around € 29.0 billion (2017: € 24.9 billion) and a share of about 48.1 % (2017: 43.8 %) out of the total commercial transaction volume in Germany, office properties remained the most popular asset class. Demand for office space among companies also remained high due to the ongoing increase in employment. Space turnover in the big 7 – Berlin, Hamburg, Munich, Cologne, Frankfurt am Main, Stuttgart and Dusseldorf – at nearly 4 million m<sup>2</sup> was lower compared to the previous year (– 6.5 %). This is solely due to the lack of available space. The completion of office space increased in 2018 (+ 7.8 %). Project developments were also delayed due to the high level of capacity utilisation in the construction sector. Consequently the vacancy rate in the big 7 fell as well, to 3.6 % (2017: 4.7 %). Rental prices in the leading office locations increased by 6.4 % on average year on year due to excess demand.

The retail property transaction volume at around € 10.5 billion (2017: € 11.4 billion) declined again in 2018, only accounting for a 17.4 % share (2017: 20.1 %) of the total transaction volume for commercial real estate in Germany. Investor interest shifted from shopping centres to specialist retailers and retail parks. The tense mood among stationary retailers notwithstanding, the space turnover in 2018 increased by 7.0 % year on year with a total of 480,000 m<sup>2</sup>. International retailers primarily focused on the big 10 (big 7 plus Leipzig, Nuremberg and Hanover), further increasing their share of the total rental volume (42 % compared to 28 % in 2017). Peak rents decreased slightly across Germany (– 3.3 %).

Logistics real estate were once again very popular in the reporting year. The second-best ever result was achieved with a transaction volume of around € 7.5 billion (2017: € 8.7 billion). Therefore this asset class is meanwhile moving at a high level. A new turnover record was set with regard to space demand in 2018 at around 7.2 million m<sup>2</sup> (2017: 6.5 million m<sup>2</sup>).

The investment volume in Germany's hotel property market once again exceeded the € 4 billion mark. Even though the investment volume fell, this was not so much due to a decrease in demand but rather the limited supply in the core and core-plus segment. While sales in the portfolios were considerably below the previous-year values, a new turnover record was reached with certain hotel sales.

Residential properties also constituted a popular asset class in 2018, notwithstanding regulatory and bureaucratic changes. An above-average result was achieved at € 18.7 billion (2017: € 15.7 billion) and 131,200 residential units. The increase in the transaction volume was largely due to a further rise in prices for residential investments (+ 20 %).

### European target real estate markets

In the past financial year, the European real estate markets continued to be supported by largely stable economic framework conditions and ongoing low interest rates. At € 254.8 billion however, the commercial transaction volume fell slightly short of the previous-year level. Developments in the European markets varied considerably.

The UK generated a commercial transaction volume of € 72.7 billion in 2018. Ongoing uncertainties regarding Brexit had a visible impact on the real estate market. Nevertheless, the British office rental market proved comparatively resilient. Even though the development of retail sales was slightly positive, consumer confidence dropped considerably towards the end of the year. The development of the retail rental market continues to be volatile. Demand is largely focusing on premium properties with high foot traffic volumes. The development of the residential property market was once again ambivalent. Central London suffered price corrections while the national house price growth remained nearly stable.

In 2018 the French real estate market once again achieved third place in terms of commercial transaction volumes in Europe, after Germany and the UK, with growth to € 31.1 billion. Rising employment numbers in the Île-de-France region are boosting the demand for office space. However the space turnover in the Paris office market was below the previous-year level due to the short supply. Excess demand resulted in rising office rents in Paris and Lyon. The development of retail sales was stable notwithstanding the weak economy. Only peak rents for smaller premium properties in the main shopping streets of Paris increased. Peak rents for other retail formats on the other hand remained stable. Another slight increase in peak rents was seen in the logistics real estate market in Paris. Peak rents sustained their previous level in the remaining logistics regions.

The positive general economic conditions in the Benelux states also made themselves felt in the investment markets. The Netherlands generated a new record value in 2018 with a commercial transaction volume of € 22.0 billion. A shift of investor interest in favour of secondary locations and cities was observed here, indicated by the increase of investments outside the “Randstad”. High demand for office space caused an increase in peak rents, especially in Utrecht. Office rents in Amsterdam most recently remained stable after a number of increases over the past two years.

In Spain the transaction volume grew to about € 11.6 billion, reaching the highest value since 2007. The investment market benefited from favourable economic framework conditions, high demand in the rental markets and stable to rising rents in nearly all sub-markets. Especially the office markets in Madrid and Barcelona, recovering late in the cycle, saw a noticeable rent increase starting from a low level. Rents in the retail rental market continued to increase in Madrid while most recently remaining stable in Barcelona.

A new record was set in Poland with a commercial transaction volume of € 7.2 billion. Dynamic economic development led to a noticeable increase of space turnover in Warsaw's office market. The Polish capital saw the largest decrease in vacancy rates among all European office locations. The economic upturn was noticeable in Poland's retail property market as well, leading to a positive development of space turnover. While peak rents for shopping centres remained stable due to the large supply of new space on the market, a slight decrease was observed in the main shopping streets. The high level of construction activity is gradually counteracting the upwards pressure on peak rents in the logistics real estate market.





### 2.1.3 Development of international financial markets

Growing global uncertainty was reflected in the capital markets as well. The German share index DAX lost more than 18 % in the course of the year, with trading closing at 10,559 points at year-end. On the one hand the US Federal Reserve implemented four further interest rate increases in 2018, respectively by 25 basis points, and continued to reduce its balance sheet total. In the eurozone on the other hand, the European Central Bank (ECB) stood by its highly expansive monetary policy, even though it stopped net bond purchases within the framework of the Expanded Asset Purchase Programme (EAPP) by the end of the year. Maturities from the programme however continue to be fully reinvested. The prime rate remained at the historic low and the forward guidance was only adjusted slightly in the past year. In the US, the treasuries were unable to hold the 3.0 % mark that was temporarily exceeded. European capital market interest rates trended downwards in 2018 overall, after initially continuing to exhibit strong growth in the first half of the year. The yield on ten-year federal bonds reached a high of more than 0.80 % for the year in February. In May and at the end of the year however, uncertainty drove investors to safe havens so the federal yield was driven down to the range of 0.20 %.

Euro money market interest rates remained nearly unchanged in the negative range. The US dollar benefited from increased tightening of the US monetary policy and the increased growth difference in the past year. After considerably losing in value, the single European currency traded below USD 1.15 per EUR at the end of the year. The EUR/USD basis swap spreads narrowed considerably for all maturities in the course the year, to a range of – 10 to – 15 basis points.

### 2.1.4 Development of the banking sector

The market environment in commercial real estate finance was considerably influenced by the developments in the real estate and capital markets described above, and by macroeconomic developments. Commercial property financing remained highly competitive in the past year, as it has been in previous years. A large number of real estate financiers continues to be represented in the real estate markets that are relevant for Deutsche Hypo. These developments continued to exert strong pressure on margins and on the structures being financed.

The implementation of various general regulatory requirements was once again in focus for Deutsche Hypo in reporting year 2018. The European Markets in Financial Instruments Directive (MiFID II) and the new International Financial Reporting Standards (IFRS 9) came into force in January 2018. An EU-wide stress test of the banking sector was also conducted again at the beginning of 2018, involving Deutsche Hypo as a subsidiary of NORD/LB. The implementation of all required regulatory measures led to an increased expenditure of resources by Deutsche Hypo.

## 2.2 Course of business at a glance

### 2.2.1 Significant influencing factors and developments in financial year 2018

Deutsche Hypo's business development in the past financial year was once again defined by the fundamentally positive external framework conditions. Largely stable economic development in the economies relevant for the Bank, ongoing positive development of the real estate markets and the supportive environment of the money and capital markets resulted in stable risk indicators in the Bank's core business area. Accordingly the average rating in the real estate finance portfolio remained constant at a favourable level. A historic low of financing defaults led to a very good risk result, considerably boosting the development of Deutsche Hypo's results in financial year 2018.

Simultaneously however the high intensity of competition observed for years in commercial real estate finance continued. This affected Deutsche Hypo's new business volume in the past financial year, which was below the previous-year value and the forecast, also against the background of strict internal requirements for risk parameters in lending. The high intensity of competition also caused additional margin pressure for new business. This is considered one reason for the decline in the Bank's interest result compared to the previous year.

Uncertainties remained in the past financial year for the important UK real estate target market. How the impending withdrawal of the UK from the EU would be handled legally was not foreseeable on the reporting date. The Bank is prepared for future developments with various options for action. Thanks to good risk parameters of the financing portfolio, Deutsche Hypo considers itself well positioned in the UK both currently and for the future, especially since the Bank does not expect any general negative developments for the UK real estate market even after Brexit. Accordingly attractive new business opportunities were realised in the UK even in the past financial year, selectively and in line with the Bank's conservative risk policy, and especially subject to observing market developments.

Within the capital market business, the Bank continued with the strategic portfolio reduction in the public sector finance business. Here the Bank as in the previous year utilised stable market conditions to selectively sell off exposures to especially high-risk counterparties and less liquid loans. The Bank also sold a debtor warrant in the past financial year in the context of accepting a swap offer from Heta Asset Resolution AG, resulting in a positive one-time effect. The quality of the capital market portfolio remained at the favourable level of the previous year on the reporting date.

On the funding side, the Bank was able to gain new groups of investors with the first-time issue of a benchmark format Pfandbrief in British pounds and an additional green Pfandbrief. Since the other issues were also met with continuous demand, the required liquidity could be obtained at competitive conditions at all times.



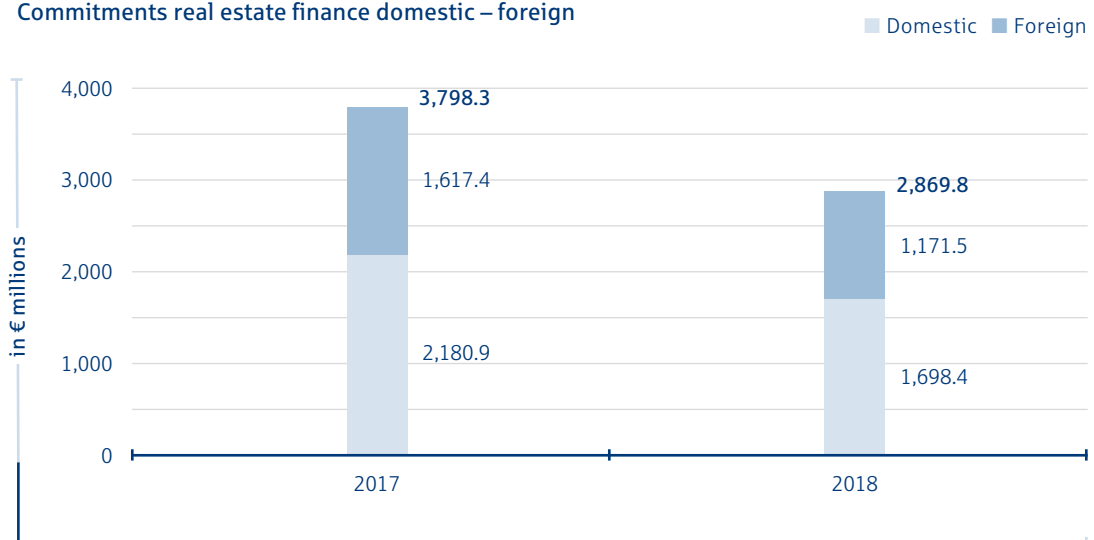
Ongoing high implementation costs for regulatory matters and investments in the Bank's organisational and technical infrastructure caused other administrative expenses to increase as expected in 2018. To ensure future competitiveness, the Bank commenced a cost-reduction programme in the past financial year and developed various measures. These call for investments in the digitalisation of internal processes in the coming years, in addition to reducing personnel expenses. The goal is to ensure the Bank's continued future viability and competitiveness by establishing even more streamlined and efficient processes. Restructuring costs of € 16.8 million have already been included in the Bank's extraordinary result for these measures in the annual financial statements.

In the opinion of the Board of Managing Directors, the business developments described above led to a good result from normal operations in the past financial year, coming in at € 74.7 million after the addition to the precautionary reserve (2017: € 62.7 million). Even under consideration of the extraordinary expenses for restructuring to ensure future competitiveness, a nearly stable profit – to be transferred to NORD/LB – of € 55.2 million remained (2017: € 56.3 million).

### 2.2.2 Development of new business in commercial real estate finance

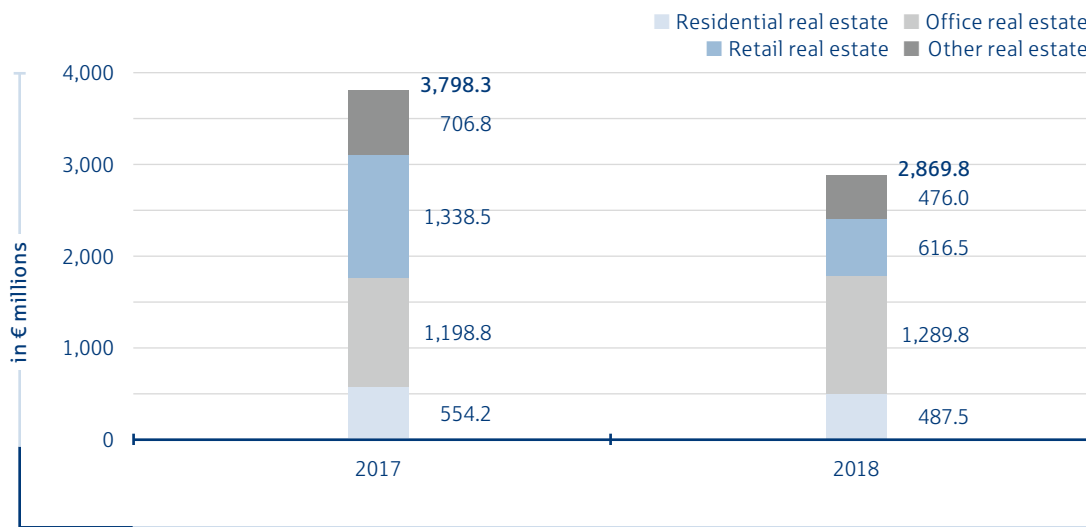
Strong competition in commercial real estate finance was reflected by a considerable decrease in Deutsche Hypo's new business volume. Last year's forecast of a slight increase could not be reached with € 2,869.8 million (2017: € 3,798.3 million). This development is due in part to Deutsche Hypo's quality focus, which requires a good risk profile for new business. The average new business rating therefore remained at a good level. A slight decrease in the new business margin was observed because of the highly competitive market situation.

#### Commitments real estate finance domestic – foreign



The regional distribution of the new business volume among the various target markets remained largely stable compared to the previous year. Once again the domestic market accounted for considerably more than half the commitment volume at € 1,698.4 million (2017: € 2,180.9 million). A large proportion of new business abroad was once again generated in the largest target markets – Benelux, the UK and France. Decreases of a similar magnitude were seen in all three target markets at € 368.9 million (2017: € 488.6 million) in Benelux, € 347.4 million (2017: € 466.1 million) in the UK and € 274.6 million (2017: € 399.7 million) in France. These new business figures also reflect the challenging competitive conditions and the Bank’s quality-oriented business policy. In the UK, the uncertainties surrounding Brexit that were previously described also led to cautious lending by Deutsche Hypo in this important foreign market. The commitment volume in Poland declined as well, to € 85.0 million (2017: € 193.7 million).

**Real estate finance by property types**



Clear shifts were seen in the types of property financed by Deutsche Hypo. The new business volume for office properties increased slightly to € 1,289.8 million compared to the previous year (€ 1,198.8 million). This considerably increased the share of the total new business. More than half the new business in the office property segment was domestic. On the other hand, the commitment volume for retail properties decreased considerably in the past financial year, to € 616.5 million (2017: € 1,338.5 million). The new business volume in residential property financing fell slightly to € 487.5 million (2017: € 554.2 million), and the volume of other real estate dropped considerably to € 476.0 million (2017: € 706.8 million). Other real estate continues to consist mainly of hotel and logistics centre financing.

Project developments also continue to represent an important proportion of the new business. Close to 80 % of these transactions were concluded domestically.



### 2.2.3 Funding activity

Deutsche Hypo issued own securities in the amount of € 2,327.1 million in 2018 (2017: € 3,526.3 million). € 1,722.8 million (2017: 1,328.0 million) of this consisted of mortgage Pfandbriefe and € 604.3 million (2017: € 2,198.3 million) of unsecured bonds. 100 % of the unsecured bonds were issued as private placements, usually in the form of registered bonds and only to a lesser proportion as bearer bonds.

Deutsche Hypo issued mortgage Pfandbriefe almost exclusively as benchmark transactions. Chronologically these were a Pfandbrief tap of € 250.0 million in January, a Pfandbrief in British pounds totalling £ 355.0 million – also after a tap – in March and April, a new Pfandbrief issue in June with a volume of € 500.0 million and a green Pfandbrief of more than € 500.0 million in September. In total, Deutsche Hypo successfully placed mortgage Pfandbriefe in the benchmark format with a volume of € 1,643.8 million in the market. All issues were met by extensive domestic and foreign demand. New investors were once again secured for the Bank. This was realised mainly through the green Pfandbrief but also the GBP transaction, which was the benchmark premiere in this currency for Deutsche Hypo. The green Pfandbrief impressively confirmed the decision to consistently develop the green value chain in the granting of energy-efficient commercial real estate finance.

The contracted business in commercial real estate finance was consistently funded at competitive conditions. Deutsche Hypo's liquidity was therefore ensured at market conditions at all times. As usual, Deutsche Hypo was engaged in secondary market servicing for its own securities. The portfolio of own securities totalled € 47.3 million at the end of the year (2017: € 26.5 million).

## 2.3 Net assets, financial and income position

### 2.3.1 Income position

in € millions	Total result		Commercial real estate finance		Capital market & other business	
	2018	2017	2018	2017	2018	2017
Net interest income	177.4	193.4	162.4	173.6	15.0	19.8
Net commission income	-0.1	0.3	0.4	1.0	-0.5	-0.7
Administrative expenses	84.0	83.8	41.0	42.4	43.0	41.4
Other operating income	-7.4	4.2	0.5	0.2	-7.9	4.0
Risk result	-20.3	-41.3	16.3	-5.7	-36.6	-35.6
Income from securities and participatory interest	9.1	-10.2	0.0	0.0	9.1	-10.2
<b>Result from normal operations</b>	<b>74.7</b>	<b>62.7</b>	<b>138.6</b>	<b>126.7</b>	<b>-63.9</b>	<b>-64.0</b>
Extraordinary result	-16.5	0.7	0.0	0.0	-16.5	0.7
Interest on investment by silent partners	0.0	3.5	0.0	0.0	0.0	3.5
<b>Profit before taxes and profit and loss transfer</b>	<b>58.2</b>	<b>59.9</b>	<b>138.6</b>	<b>126.7</b>	<b>-80.5</b>	<b>-66.8</b>

Deutsche Hypo generated a result from normal operations of € 74.7 million in financial year 2018, exceeding the previous-year result of € 62.7 million and the forecast result. Under consideration of the restructuring expenses reported under the extraordinary result, the generated result led to a RoE of 6.8 %. This corresponds to last year's forecast and is close to the previous-year level of 7.0 %. The core business area generated a result of € 138.6 million, exceeding the previous-year value of € 126.7 million. In particular, the risk result in the commercial real estate finance business area defined by net releases contributed to the Bank's overall result above expectations. One-time proceeds were also generated from the sale of a debtor warrant related to the acceptance of a swap offer from Heta Asset Resolution AG (Heta) in the

amount of € 12.1 million. Following the original assignment of the underlying receivables and securities, these were included in the Bank's risk result and in the income from securities and participatory interest. The Bank used the positive result to strengthen the precautionary reserves. Restructuring expenses of € 16.8 million were also incurred for the defined measures to decrease personnel and improve efficiency. After taking the restructuring expenses into account, the result before taxes and profit and loss transfer was € 58.2 million, approximately equal to the previous-year level.

The net interest income for the Bank as a whole at € 177.4 million was below the previous-year value of € 193.4 million. Here the commercial real estate finance business area continued to make the biggest contribution with a net interest income of € 162.4 million. Contrary to the forecast, the previous-year level of € 173.6 million could not be reached because of the reduced new business volume and the margin pressure, caused among other things by the competitive situation. As predicted the contribution of the remaining active, reduced capital market portfolio to the result fell compared to the previous year. Low interest rates also caused the income from investments of the Bank's equity to drop slightly from the previous year as expected.

Investments in further boosting the market presence and in the organisational and technical infrastructure continued to be a focus for Deutsche Hypo. The operating expenditure slightly exceeded the previous-year level as expected. Lower personnel expenses were mainly due to variable compensation components. Administrative expenses totalled € 84.0 million (2017: € 83.8 million). Once again the bank levy accounted for a large share at € 11.1 million. The resulting CIR of around 49.5 % exceeded the previous-year value (2017: 42.3 %) as expected. Nevertheless the continued low level of this performance indicator underscores Deutsche Hypo's existing cost discipline.

In a stable market environment, the continued risk-aware lending policies in the commercial real estate finance business area led to the net release of loan loss provisions. The positive development of specific provisions in the core business area was used to further strengthen the precautionary reserve. The risk result improved to € – 20.3 million for the Bank as a whole (2017: € – 41.3 million). In the course of reducing the balance sheet total, which included the repurchase of own Pfandbriefe in the course of market servicing, positive effects in the course of decreasing the capital market business portfolio and unplanned redemptions, the result for the Bank as a whole was reduced by about € 15 million net. Future funding costs are reduced accordingly. This negative impact was partly compensated by income from the sale of the Heta debtor warrant.

Other operating income of € – 7.4 million was below the previous-year level of € 4.2 million, which had been significantly influenced by positive one-time effects, and was defined by expenditures for the compounding of long-term provisions and increases in provisions due to legal uncertainties in existing credit contracts.

The positive income from securities and participatory interest was also defined by income from the sale of the Heta debtor warrant, and was therefore considerably above the previous-year result that was driven down by the active reduction of the Italian exposure.



## 2.3.2 Net assets

### 2.3.2.1 Development of the balance sheet

in € millions	31.12.2018	31.12.2017
Receivables		
Mortgage loans	12,264.0	12,077.1
Loans to local authorities	2,844.4	3,892.5
Other receivables	1,014.2	1,392.2
Securities	4,716.6	5,489.9
Other assets	233.6	846.6
<b>Total assets</b>	<b>21,072.8</b>	<b>23,698.3</b>

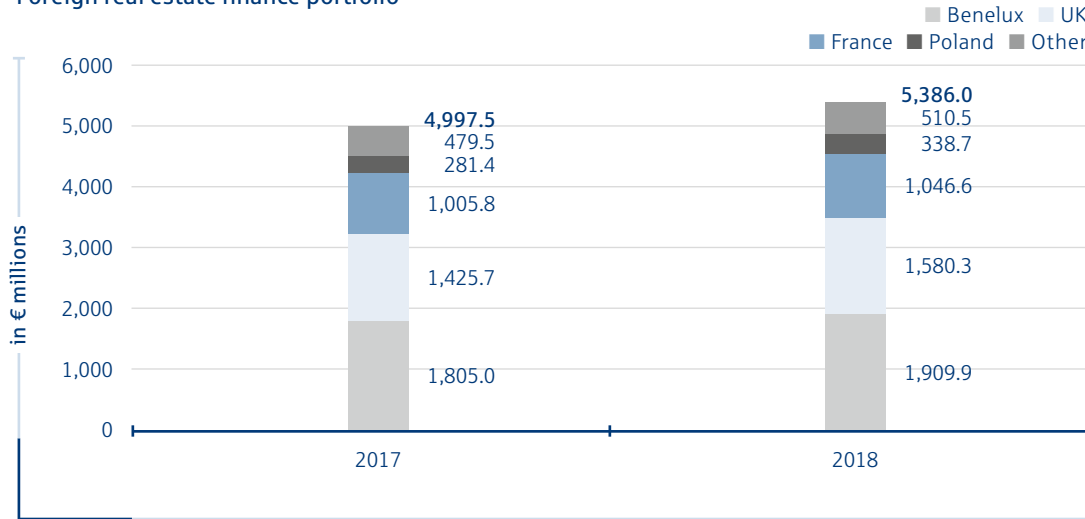
Deutsche Hypo's balance sheet total dropped considerably to € 21,072.8 million compared to the previous year (€ 23,698.3 million). This decrease was among other things due to the strategy of reducing the public sector finance business, which has been pursued for years, and the associated focus on the commercial real estate finance business area. While the portfolio in the core business area remained approximately constant, the loans to local authorities and securities once again dropped considerably by a total of more than € 1,821.4 million in the past financial year. This decrease was due both to planned maturities and selective disposals. As in the previous year, the Bank thereby made use of market opportunities, particularly to reduce exposure to individual high-risk counterparties. New business for the purpose of liquidity and cover pool management was conducted in the past financial year with a nominal volume of just € 10.0 million (2017: € 102.8 million). The quality of the capital market portfolio remained at the favourable level of the previous year on the reporting date.

### 2.3.2.2 Commercial real estate finance portfolio development

Even though new business fell short of expectations, Deutsche Hypo was able to keep its portfolios constant in the core business area during the past financial year at € 12,264.0 million (2017: € 12,077.1 million) since early repayments were somewhat lower. The slight portfolio increase predicted in the previous year was therefore not achieved. Maintaining the good risk parameters of the loan portfolio remained a key objective for Deutsche Hypo in the past financial year. Against the background of quality-oriented lending policies and supported by continued favourable external framework conditions, the average rating in the real estate finance portfolio was maintained at the good level of the previous year. Financing in default as a proportion of the overall portfolio was at a historic low and therefore significantly below the expected long-term average. Detailed information on the distribution of the portfolio by rating categories and regions is provided in the presentation of the analysis of credit risk in the expanded risk report.

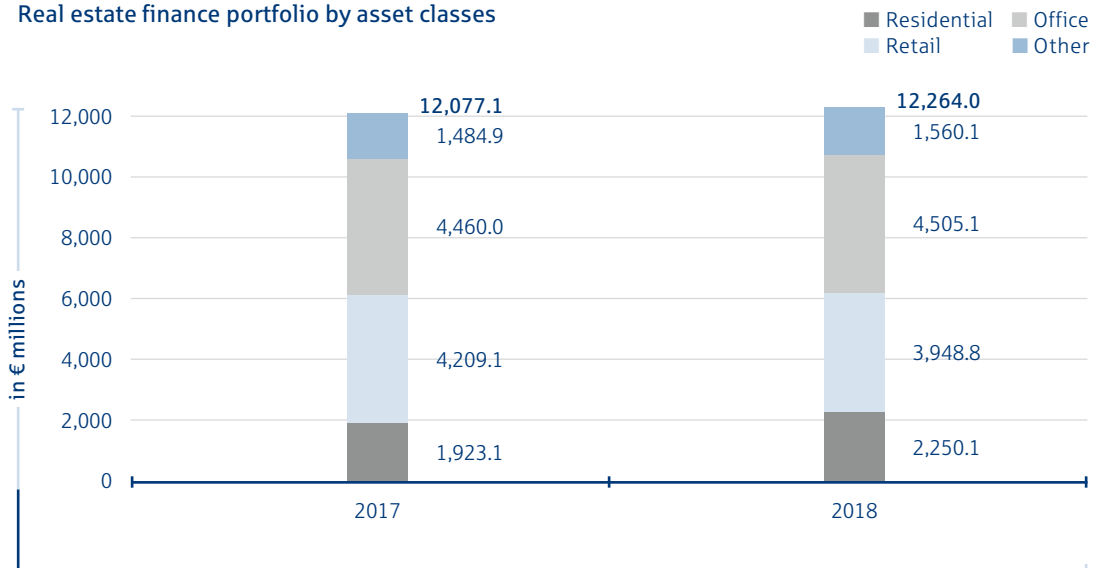
Notwithstanding a slight decrease to € 6,878.0 million (2017: € 7,079.6 million), domestic financing continues to account for the bulk of the portfolio. There was however a slight shift in favour of the foreign markets again in the past financial year, with total portfolios increasing significantly to € 5,386.0 million (2017: € 4,997.5 million). This increase was mainly due to an expansion of the financing portfolios in the key target markets of Benelux to € 1,909.9 million (2017: € 1,805.0 million) and the UK to € 1,580.3 million (2017: € 1,425.7 million). Smaller portfolio increases were also seen in the target markets of France and Poland. Portfolios in regions that are not among the direct target markets on the other hand decreased slightly.

Foreign real estate finance portfolio



Following the development of new business figures, the breakdown of the portfolios by property type changed compared to the previous year. The proportion of retail properties with portfolios falling to € 3,948.8 million (2017: € 4,209.1 million) shifted in favour of the other property types. Office properties at € 4,505.1 million (2017: € 4,460.0 million) remained the leading type of property. The residential development financing portfolio once again increased considerably to € 2,250.1 million (2017: € 1,923.1 million). Portfolio changes with regard to other real estate were only minor. This largely consists of hotel and logistics buildings, mostly financed in Germany. With regard to residential financing, the majority of the properties financed were located in the Netherlands and Germany.

Real estate finance portfolio by asset classes





In addition to the commercial real estate finance portfolios, a comparatively large portfolio of irrevocable loan commitments also remained on the reporting date of 31 December 2018 in the amount of € 1,061.6 million (2017: € 1,378.7 million). Guarantee facility agreements with a volume of € 327.9 million (2017: € 346.8 million) were also reported.

Project developments continued to account for a noteworthy proportion of the portfolio, irrevocable loan commitments and guarantee facility agreements in the core business area. Based on the current key risk figures, they continue to be of high quality in the Bank's view.

### 2.3.3 Financial position

in € millions	31.12.2018	31.12.2017
<b>Liabilities</b>		
Mortgage Pfandbriefe	8,128.1	8,414.1
Public Pfandbriefe	3,806.9	4,490.4
Unsecured bonds	1,784.3	2,677.4
Other liabilities	5,897.4	6,672.1
Subordinated liabilities	379.5	379.5
Jouissance right capital	0.0	20.0
Funds for general banking risks	14.4	14.4
Equity	838.2	838.2
Other liabilities	224.0	192.2
<b>Total liabilities</b>	<b>21,072.8</b>	<b>23,698.3</b>
Contingent liabilities	462.2	502.2
Other obligations	1,061.6	1,378.7

The considerable decrease in the balance sheet total during the past financial year was accompanied by a reduction of both secured and unsecured liabilities. In line with the strategic aims of the Bank to reduce the public sector finance business, there was a further considerable decrease in public Pfandbriefe currently in circulation on the reporting date to € 3,806.9 million (2017: € 4,490.4 million). This decrease was largely due to maturities. As in the past, the Bank selectively repurchased own public Pfandbriefe before they matured in the course of regular secondary market servicing. Simultaneously the portfolios of mortgage Pfandbriefe decreased slightly to € 8,128.1 million (2017: € 8,414.1 million), and the portfolio of unsecured bonds fell to € 1,784.3 million (2017: € 2,677.4 million) corresponding to the development of funding needs in the core business area.

Please see the cash flow statement for further information on the development of the Bank's financial position. Regarding the terms and maturities of the liabilities, please refer to the maturity breakdown for liabilities in sections 14 to 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 constant at € 838.2 million compared to the previous year because of the profit and loss transfer agreement. Jouissance right capital on the other hand decreased to zero since they were fully repaid by the reporting date as announced (2017: € 20.0 million). Please see the explanations in the expanded risk report of this management report regarding the Bank's regulatory equity resources.

There was a year-on-year decrease in off-balance-sheet obligations in the form of irrevocable loan commitments to € 1,061.6 million (2017: € 1,378.7 million) due to disbursements. That resulted in a continued high level of agreed loans not yet included in the portfolio. Contingent liabilities decreased slightly to € 462.2 million (2017: € 502.2 million). This was mainly due to a further reduction in commitments from credit derivatives to € 134.3 million (2017: € 155.5 million) and a decrease in contingent liabilities from sureties in the real estate finance business to € 327.9 million (2017: € 346.8 million).

### 2.3.4 Rating

	Mortgage Pfandbriefe	Public Pfandbriefe	Short-term liabilities	Senior unsecured preferred	Junior/Senior unsecured non-preferred	Baseline Credit Assessment (BCA)
Moody's	Aa1 Outlook: on review for upgrade	Aa2 Outlook: on review for upgrade	Prime-2	Baa2 Outlook: on review for upgrade	Ba1 Outlook: on review for upgrade	b2 Outlook: on review for upgrade
	until 14 February 2019	until 14 February 2019	until 14 February 2019	until 14 February 2019	until 14 February 2019	until 14 February 2019
	Aa1 Outlook: on review direction uncertain	Aa2 Outlook: on review direction uncertain	Prime-2 Outlook: on review for downgrade	Baa2 Outlook: on review direction uncertain	Ba1 Outlook: on review direction uncertain	b2 Outlook: on review direction uncertain
	until 19 December 2018	until 19 December 2018	until 19 December 2018	until 19 December 2018	until 19 December 2018	until 19 December 2018
	Aa1	Aa2	Prime-2	Baa2 Outlook: negative	Ba1	b2
				until 3 August 2018: -	until 3 August 2018: Baa3 Outlook: negative	

The rating agency Moody's published its new methodology for rating banks on 3 August 2018 in response to the EU Bank Recovery and Resolution Directive and its implementation in German law. Here the liability cascade was reorganised. In this context the Senior Unsecured rating class was divided into two new rating classes, Senior Unsecured (preferred) and Junior/Senior Unsecured (non-preferred). All Deutsche Hypo bonds issued before the law took effect have been assigned to the Junior/Senior Unsecured non-preferred asset class since 21 July 2018 and received a non-investment grade rating of Ba1 from Moody's. The Senior Unsecured Preferred rating was set at Baa2.

After Moody's set almost all of the Bank's capital market instruments to the outlook "on review direction uncertain" on 19 December 2018 based on the situation and the measures required to replenish the capital of the parent company NORD/LB, the rating agency published a more optimistic assessment on 14 February 2019. Moody's set all of the Bank's ratings to "on review for upgrade" following Deutsche Hypo's ad-hoc announcement on 2 February 2019. The only exception was the short-term rating, which was confirmed with a stable P2 rating. Moody's positively acknowledged the pending measures to replenish the NORD/LB Group's capital with the changed assessment. According to Moody's, the solution preferred by NORD/LB's owners also underscores the long-term direct responsibility of the public banking sector.

For the current rating process, Moody's assumes that the review of NORD/LB and its subsidiaries will be concluded during the second or third quarter of 2019, depending on when the measures are realised and the required approvals of the regulatory authorities are obtained.

### Sustainability ratings

	imug	oekom research
Sustainability rating	positive BB	Overall Score C+
Mortgage Pfandbriefe	positive BB	Investment Status „Prime“
Public Pfandbriefe	positive BBB	„Industry Leader“

In March of 2019 the sustainability rating agency imug Beratungsgesellschaft für sozial-ökologische Innovationen mbH reassessed the Bank in its annual cycle. Deutsche Hypo takes 2nd place among the assessed mortgage banks (28 in total) with the assigned ratings, and 4th place among all European banks (171 in total).

The rating agency oekom research AG, which issues ratings at intervals of two to three years, gave Deutsche Hypo a prime rating in April 2016. Such ratings are given to the companies that meet the sector-specific requirements regarding sustainability management in a particular industry. Deutsche Hypo was one of the top three companies in its industry at that time with its “C+” rating.

#### 2.4 Overall statement on the course of business and the Bank’s situation

In the view of the Board of Managing Directors, Deutsche Hypo can look back on a good financial year 2018. A positive annual result was achieved notwithstanding the strengthening of the precautionary reserves in view of the highly positive development of specific risk provisioning. Investments were also made in the organisational and technical infrastructure as well as the launch of a cost-reduction programme, for which restructuring expenses were incurred, to lay the foundation for the Bank’s future cost-effective positioning. These considerable expenditures notwithstanding, the profit transfer to NORD/LB remained nearly constant compared to the previous year.

Portfolio development was differentiated. While the quality of the portfolios in the business areas was consistently maintained at the good levels of the previous years and defaults on financing in the core business area reached a historic low, the planned portfolio growth was not achieved in the core business area because new business fell short of expectations. On the other hand, the considerable decrease of the public sector loan portfolio beyond regular maturities is considered positive against the background of the strategic focus on the commercial real estate finance business area. The Bank gained new investors on the funding side by issuing another green Pfandbrief and its first GBP benchmark issue, consistently obtaining the required liquidity from the market at competitive rates.

Overall the Bank’s business development in the past financial year 2018 can therefore be assessed as positive due to its good profitability, maintaining positive risk indicators in the portfolios and the investments made in cost-effective positioning.

### 3 Report on subsequent events

Significant developments at NORD/LB that occurred after the reporting date and are relevant for Deutsche Hypo due to its dependency are discussed in the sections “Group affiliation” and “Dependencies of Deutsche Hypo on NORD/LB” in the forecast report of this management report.

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

### 4 Forecast, opportunity and risk report

#### 4.1 Forecast report

The following section should be read in the context of the other 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 and risks related to the occurrence of future events, including many factors that 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 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.

#### 4.1.1 Development of business and framework conditions

##### 4.1.1.1 Forecast for economic development

The German economy will only recover slowly from the economic downturn. After GDP growth ground to a halt in the second half of 2018, an ongoing flat basic economic trend is expected for the first half of the year based on the most important early indicators. Most recently the mood among financial market experts and German companies worsened considerably. Even though economic expectations improved again slightly at the start of the year, the situation was assessed as considerably worse. Domestic demand however should be robust enough to keep growth in the forecast year slightly above 1.0 %.

Early indicators offer little reason to hope for a fast economic recovery in the eurozone this year either. Unemployment is expected to continue falling in 2019, albeit less dynamically. Real economic growth of 1.2 % compared to the previous year is expected for the year overall. Initially the monetary policy is going to remain highly expansive. The main downside risks for the forecast are geopolitical conflicts, US trade policies, the withdrawal of the UK from the European Union, European elections coming up in the spring and possible political instability in some member states of the euro currency union.



#### 4.1.1.2 Forecast for the development of the target real estate markets

The global transaction volume in commercial real estate is expected to be somewhat more moderate in the current year after the record value for 2018. While the fundamental framework conditions for the global real estate market remain robust, investors are becoming more selective in view of the advanced real estate cycle. Against this background, a transaction volume of around \$ 680 billion is expected for the year as a whole.

The German real estate market should initially continue to benefit from an at least stable economic situation in 2019. An interest increase that is not expected before the end of the year and the lack of investment alternatives are going to keep the demand for real estate investments high. The commercial real estate transaction volume is expected to be around € 55 billion for the year overall. Prime yields are going to stabilise at a low level in the office sector. Opposing developments are expected in the retail sector: while the demand for specialist retail products with discounters or food product markets as anchor tenants remains high, and can be expected to cause a further drop in prime yields, an increase of prime yields is once again being observed in the shopping centre segment since the fourth quarter of 2018. The demand for hotel investments is going to remain high. Residential properties will also continue to be among the most popular real estate investments in 2019.

Overall the rising trend in the German real estate market should continue in 2019, although not as dynamically. Germany remains a safe investment haven with rent increase prospects, especially in the leading office and residential markets.

An above-average transaction volume in the historic context is once again expected in the European real estate markets for 2019. The investment volume however should be somewhat lower here than in the previous year as well. This is not only due to the growing economic and geopolitical uncertainties. A gradual interest rate turnaround expected starting at the end of 2019 should dampen real estate performance as well. After years of high transaction volumes, an increasingly short supply can also be observed in some countries. Continued rent increase expectations over the short term support the demand for real estate.

#### 4.1.1.3 Forecast for developments on international financial markets

The US Federal Reserve is expected to act more cautiously this year and only increase the prime rate twice according to current assessments. The ECB on the other hand is continuing its highly expansive monetary policy. An initial prime rate increase should be postponed until 2020 by the ECB. Thus the monetary environment remains favourable. The development of capital market interest rates should be very restrained in this environment. Yields on federal bonds with a remaining term of ten years should only increase slightly to 0.50 % by the end of 2019. The expected exchange rate between the USD and euro over twelve months is 1.20 USD/EUR. EUR/USD basis swap spreads are expected to remain at levels in the vicinity of – 10 basis points over the short to medium term. Econometric forecast models indicate that the maturity curve should remain flat.

#### 4.1.2 Forecast for the development of business with significant opportunities and risks

##### 4.1.2.1 Significant assumptions in the forecast

Deutsche Hypo's medium-term plan, which is compiled annually, provides the basis for the statements on the income forecast. Its foundation consists of economic assumptions, expectations with regard to developments on real estate markets, forecasts on capital market developments and regulatory requirements. New business, the development of the portfolios and the margins, among other factors, are planned on this basis.

In terms of macroeconomic framework data, planning for the coming years 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 but with strong competition on the lender side. 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 of the acquisition capacities and expansion of further sales initiatives (development of business relationships with new partners and segments)
- Pursuit and development of sustainability measures, for example by issuing more green bonds
- Depletion of the public sector finance portfolio with an accompanying reduction of credit spread risks
- Further 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 processes and structures, in particular through a cost programme initiated in 2018 to boost efficiency and reduce costs over the long term

Regarding the bank rating, which has a significant influence on the development of new business and portfolio margins, Deutsche Hypo expects a rating improvement in the further course of planning.

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

Deutsche Hypo expects the new business volume in the commercial real estate finance business area to increase slightly in 2019 compared to the previous year. A slight increase is also expected for the portfolios. Deutsche Hypo will continue to apply high quality standards and prioritise yield criteria in lending. Pressure on margin development is expected against the background of ongoing intense competition. To counteract this competition, Deutsche Hypo continues to rely on the diversification of the earnings base and the further development of its structuring expertise.



### 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 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 the 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. 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. Other uncertainties resulting from political developments, e.g. the Brexit negotiations, are not to be excluded as they could influence the real estate markets and hence also the new business activities of Deutsche Hypo. 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.

Against the background of close integration into the NORD/LB Group, complying with the regulatory capital requirements is ensured at the Group level and not at the level of Deutsche Hypo. There is thus the risk that the Bank's new business opportunities could be limited by the CET1 capital adequacy of the parent institution, discretionary decisions by the banking authority regarding additional individual and increased industry-wide capital requirements (capital buffer for systemic and counter-cyclical risks) as well as decisions by the parent institution on the allocation of capital. Significant uncertainty regarding the further development and structuring of NORD/LB could have a negative impact on new business as well. Furthermore, stricter legal and regulatory requirements (in particular regarding the equity backing) or a higher RWA commitment due to a worsening of the real estate economy could lead to fewer new business opportunities.

Customer behaviour also harbours opportunities and risks for portfolio development, particularly with regard to loan extensions and unscheduled repayments.

#### 4.1.2.3 Income forecast

Deutsche Hypo expects the development of earnings to remain stable in the core business area and for the Bank overall. Quality-oriented lending by Deutsche Hypo and the ongoing positive real estate market environment are expected to continue leading to a good risk result in the credit business. In the forecast for financial year 2019, the Bank takes a slight increase in risk costs into account and therefore a need for net additions in the real estate finance area.

Investments to strengthen Deutsche Hypo's market presence and the organisational and technical infrastructure as well as the Bank's further development and digitalisation will continue. The start of implementing the cost reduction programme is intended to initiate improvements in the interest of efficient and streamlined business operations while maintaining the proven cost discipline. Against the background of implementing regulatory requirements, another slight increase in administrative expenses is expected for 2019. This will lead to a slight increase in the CIR at the same time. However the CIR will remain low compared to the rest of the industry.

The result from normal operations was defined by unexpectedly positive extraordinary items in the past financial year. These are not expected for 2019, leading to a considerably lower result forecast. The good RoE that will be nearly at the level of the current year in the coming year reflects the ongoing positive business development.

### **Opportunities and risks**

Limited predictability of developments in the capital market portfolio constitutes a 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, both in the commercial real estate finance business and in the capital market portfolio. Despite careful planning of the risk result, a trend reversal of the external framework conditions, for example a considerable drop in real estate prices following an interest rate increase, could lead to the deterioration of borrower creditworthiness and to an impairment of the value of the collateral provided, and could also result in a need for additional loan loss provisions.

Weaker than planned portfolio and margin developments, resulting for instance from increased competition or a reduction in credit demand, also bear risks regarding the result. Furthermore, it is conceivable that the terms for funding may become more costly and that these costs cannot be passed on within the framework of conditions, or the demand for unsecured funding may increase. Generally speaking, an early improvement in the Bank's or the parent company's rating compared to the planning assumptions could have positive effects on funding conditions. A deterioration of the Bank's or parent company's rating as well as longer-term uncertainty about the Group's situation could have corresponding negative effects on the Bank's funding opportunities and costs. Potential tensions in the financial markets could make funding measures more difficult. A more restrictive than expected monetary policy of the relevant central banks could increase funding costs or reduce funding opportunities as well. Risks could arise if the expected new business volume cannot be generated in the markets at the planned margins. Increased funding costs for Deutsche Hypo, for example due to changes to the Bank's or parent company's rating with constant margin requirements, could restrict the volume of the planned new business and therefore reduce the earnings base. Furthermore, legal uncertainty over existing contracts in the credit business could influence the income results.

The possibility of a considerable decrease in real estate prices in the UK after Brexit cannot be excluded, which could lead to higher risk provisioning costs. Under consideration of the portfolio's good risk parameters and the conservative portfolio orientation, the risks regarding the result are considered low in view of Deutsche Hypo's real estate financing portfolio in the UK with a volume of € 1,580.3 million (2017: € 1,425.7 million). No significant one-time costs and higher administrative expenses that could be incurred in the course of the UK's withdrawal from the EU are expected according to current assessments. The German Accompanying Tax Legislation on Brexit (Brexit-Steuerbegleitgesetz) shores up the coverability of British cover assets both through grandfathering rules and also for new business by seamlessly integrating the United Kingdom and Northern Ireland into the German Pfandbrief Act (PfandBG) as third countries.





Furthermore, new regulatory changes may be associated with restrictions and therefore with earnings risks as well as the implementation of new regulatory requirements with 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 the core business area, for instance in the context of reduced competition. Higher fees also constitute earnings and therefore income opportunities. Opportunities for more favourable funding could result from the further diversification of the investor base, for example by issuing more green bonds.

It is also conceivable that, given constant or improving economic framework conditions, the loan loss provisions in the real estate finance business area will be lower and therefore 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 the fact that investments may lead to lower than planned expenses, thereby increasing the result. If investments cannot be made to the planned extent, there would be an opportunity of a higher result in the forecast year. The reduction in costs could, however, be associated with higher expenses in the subsequent year. It is also possible that the cost reduction programme may be implemented more quickly than expected, making the administrative expenses lower than predicted. Income opportunities arising from regulatory changes, for example in the form of a lower bank levy, 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 relating to the performance indicator RoE. Regarding the CIR, opportunities mainly result from a positive forecast deviation in reference to costs and income. Negative deviations in these result components constitute a risk leading to a less favourable Cost-Income-Ratio.

#### 4.1.2.4 Dependencies of Deutsche Hypo on NORD/LB

Due to a control and profit and loss transfer agreement as well as the use of the waiver rule in accordance with Art. 7 (1) CRR, formerly Section 2a(1) of the German Banking Act (KWG), Deutsche Hypo is dependent on the Group's parent company NORD/LB. Additional significant dependencies exist regarding compliance with the Group's capital requirements, the development of the rating, liquidity and funding as well as controlling and organisation within the Group. There are also service relationships between Deutsche Hypo and NORD/LB as well as intra-group receivables and liabilities.

Over the previous year, the ongoing crisis on the shipping markets has led to a gradual increase in non-performing credit portfolios as well as a strong need for risk provisions with a corresponding adverse impact on the regulatory capital ratios of NORD/LB and the NORD/LB Group. Similar trends again contributed to significant annual losses at NORD/LB level in 2018.

With the aim of reducing non-performing ship finance portfolios and creating a foundation for measures to strengthen the capital ratios, NORD/LB and its owners initiated an extensive concept to strengthen capital and realignment of NORD/LB in financial year 2018. This also includes measures to sell non-performing credit portfolios. This is intended to equip NORD/LB for further increasing regulatory requirements and shore up its crisis resilience and competitiveness in the long term. A realignment of the business model will be pursued as before.

In terms of strengthening the capital ratios, a bidding process was carried out to attract external investors to NORD/LB. During this process bids were received from a range of investors with a potential interest in investing in NORD/LB.

NORD/LB's ad hoc announcement dated 3 December 2018 on the status of the bidding process and the reduction of the NPL shipping portfolio by NORD/LB states that the status of the reduction of NORD/LB's NPL ship financing portfolio prior to the implementation of the capital strengthening measures at NORD/LB could result in a decrease in capital ratios and an annual loss at NORD/LB level.

Among other things, NORD/LB published a further ad hoc announcement on 2 February 2019. According to this announcement, significant annual losses are expected and the common equity tier 1 capital ratio will periodically fall below the regulatory threshold for financial year 2018 at Group level as a result of for example additional risk provisioning for NORD/LB's NPL portfolio and associated portfolio transactions. The ad hoc announcement stated that the owners of NORD/LB have decided to focus on a joint solution with the Deutscher Sparkassen- und Giroverband e. V. (DSGV) for capital strengthening in the public sector. According to the ad hoc announcement, this solution will be concretised in further discussions with the DSGV. It will need to be agreed with the relevant regulatory authorities and issues around state aid clarified.

NORD/LB assumes that the capital ratios will bounce back in future and will satisfy all regulatory requirements when the planned measures for capital strengthening and realignment of the business model are implemented. The measures for realigning the NORD/LB business model envisage an extensive transformation of individual business areas and subsidiaries of the Bank and Group over the coming years.

Due to the dependencies of NORD/LB set out above, there is significant uncertainty surrounding the continuation of the business activity of Deutsche Hypo. The assumption of a continuation of business activity (going concern) for accounting and valuation purposes and the survival of Deutsche Hypo is dependent on the survival of NORD/LB. The survival of NORD/LB in turn faces significant uncertainty and is premised in particular on

- the intended capital strengthening measures at NORD/LB level being implemented, executed and approved by all relevant stakeholders, in particular the regional parliaments of Lower Saxony and Saxony-Anhalt as well as the Deutscher Sparkassen- und Giroverband e. V., enabling renewed compliance with the capital ratios and buffers and thresholds required under regulatory law,



- banking regulation authorities, in particular the European Central Bank, the German Federal Institute for the Supervision of Financial Services and the Deutsche Bundesbank, tolerating a shortfall of the regulatory minimum capital quotas up to the point of the completion of the intended measures for capital strengthening at NORD/LB level,
- all official approvals required for implementation, in particular from the EU Commission and the relevant banking regulation authority, being granted and
- the realignment of the business model and the intended restructuring measures being implemented as planned.

If the intended capital strengthening measures at NORD/LB level are not performed as planned, the outcome may be the winding up of NORD/LB. This eventuality or a rating downgrade or other adverse developments may trigger significant outflows of short-term funds, fundamentally limiting the funding options for NORD/LB.

A successful implementation of the realignment of the NORD/LB business model also presupposes the requisite acceptance by the market participants and other relevant stakeholders.

A winding up of NORD/LB could result in a winding up or a sale of Deutsche Hypo. Such a situation or a rating downgrade of NORD/LB or other adverse developments may fundamentally limit the funding options for Deutsche Hypo.

## 4.2 Expanded risk report

### 4.2.1 Risk management

#### 4.2.1.1 Fundamentals of risk management

Deutsche Hypo has made use of the waiver rule in accordance with Art. 7(1) CRR, formerly Section 2a(1) of the German Banking Act (KWG), since 2013. For this reason, the bank regulatory provisions concerning the requirements for equity at the institution 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 at the level of the cover pools.

Deutsche Hypo has implemented an inter-divisional risk management process and is closely integrated 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.

The risk organisation of Deutsche Hypo corresponds to the risk strategy principles both at the individual institution level and at the Group level. Deutsche Hypo attaches great importance to an appropriate risk management system from a business perspective, and such a system is deeply anchored in its corporate culture. Deutsche Hypo promotes an appropriate risk culture and continuously develops it further.

#### 4.2.1.2 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. Deutsche Hypo's risk strategy is integrated into the Group risk strategy. On the one hand, the Group risk strategy describes the risk policy principles of the NORD/LB Group; on the other hand, the institution-specific risk strategy of Deutsche Hypo is included as a significant company from the Group's perspective. Counterparty, market price, liquidity and operational risks were qualified as significant in the course of a risk inventory conducted at Group level. Accordingly, risk management focuses on these risk types in the narrower sense. Compliance with the existing risk strategy requirements was checked at the same time. In this context it was determined that the risk strategy goals were met.

#### 4.2.1.3 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. There is an established organisational separation between the market and risk management function up to and including the management level.

The Board of Managing Directors establishes framework conditions, responsibilities and risk tolerances for the main types of risk and is responsible for the implementation of the risk strategy at the Bank level and for effective control. 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 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 and distinctly defined down to the level of individual employees.

At the level of NORD/LB as the Group institution, additional boards have been established for handling the risk management process and exercising the consulting, monitoring, control and coordination functions. These include the Group Risk Committee, the Methodenboard Risikomanagement (Method Board Risk Management) and various working groups. Due to the integration in the risk management process at Group level, the results of the previously mentioned boards have an impact on Deutsche Hypo, which is included by sending representatives to these boards.

Deutsche Hypo has an independent risk controlling function. Its primary function is to continuously monitor the Bank's risk situation and to prepare the risk report for management and the Supervisory Board.



The risk-oriented and process-independent review of the effectiveness and appropriateness of risk management is carried out by Deutsche Hypo's Internal Audit department. Its audit approach also extends to the Bank's outsourced functions and divisions. The former outsourcing of key internal audit tasks to NORD/LB ended as of 1 September 2018. Since then this function has been realised by an organisation unit internal to the Bank.

In addition, Deutsche Hypo has an established compliance management system, which monitors developments regarding legal and regulatory framework conditions and initiates implementation measures if applicable. It serves to protect the Bank and its customers and thereby boosts customer confidence in Deutsche Hypo. The Bank has set up a central compliance function to ensure the compliance of legal and regulatory undertakings and to assist other divisions with compliance-related aspects of performing their tasks. The compliance management function is rounded out by cross-divisional boards. The compliance function also carries out regular preventive measures and suitability and effectiveness surveys in the divisions, and prepares risk analyses. The former outsourcing of key compliance tasks to NORD/LB ended as of 31 October 2018. Since then this function has been realised by an organisation unit internal to the Bank.

In addition to existing contact methods, Deutsche Hypo has implemented a whistle-blower system, which can be used by employees as well as customers, business partners and other stakeholders. This includes the function of an external ombudsman, to whom whistle-blowers can turn in confidence if the case involves suspicions of criminal acts or inappropriate transactions.

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 day-to-day 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 in day-to-day business operation.

#### 4.2.1.4 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 with major types of risk 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 case of material events.

#### 4.2.1.5 Management of risks in the cover pool

The goal of the risk management system is to control the counterparty, market price and liquidity risks at 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-effective 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, ensuring sufficient cash coverage at all times (Section 4 (1) of the German Pfandbrief Act) and ensuring 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 pool. This includes internal rating processes, analysis of external ratings and regular monitoring of the performance of 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. The information on the Bank's website is not part of this management report.

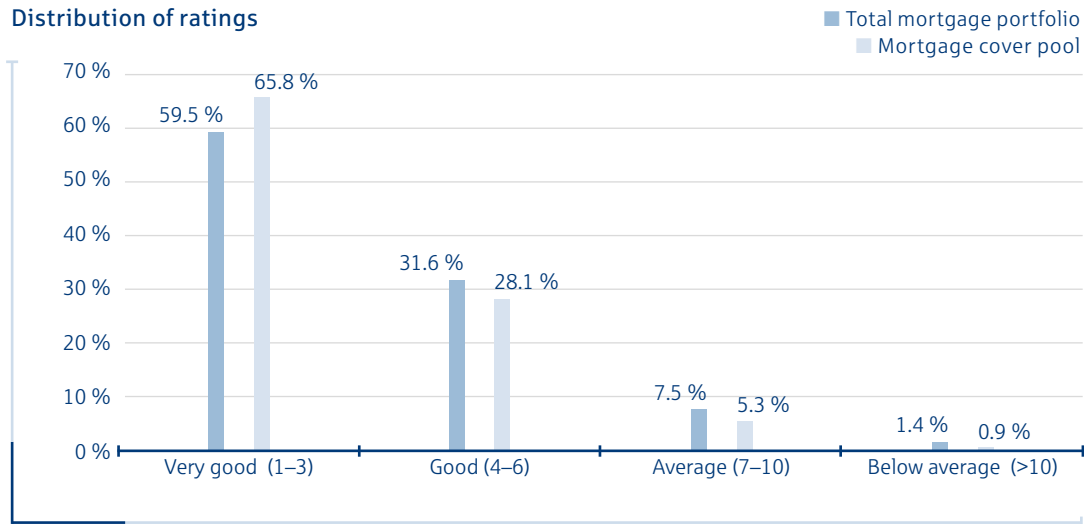
The coverability of the cover assets in the United Kingdom will also be assured after Brexit. First, grandfathering rules apply to cover assets entered into the cover register by the end 29 March 2019. And second, the United Kingdom has been included in the group of third countries with coverage approval under the PfandBG. The passing of the German Accompanying Tax Legislation for Brexit in March 2019 thus safeguards the coverability of both portfolio finance and new business in the long term.



### Cover pool of mortgage Pfandbriefe

The proportion of good and very good credit ratings (rating scores 1 to 6 in line with the DSGV rating master scale) in the mortgage cover pool amounted to 93.9 % as of 31 December 2018 (2017: 94.7 %). In reference to the real estate finance portfolio, this proportion was 91.1 % (2017: 92.1 %). The rating distribution in the mortgage cover pool is an indicator for the good quality of the Pfandbriefe.

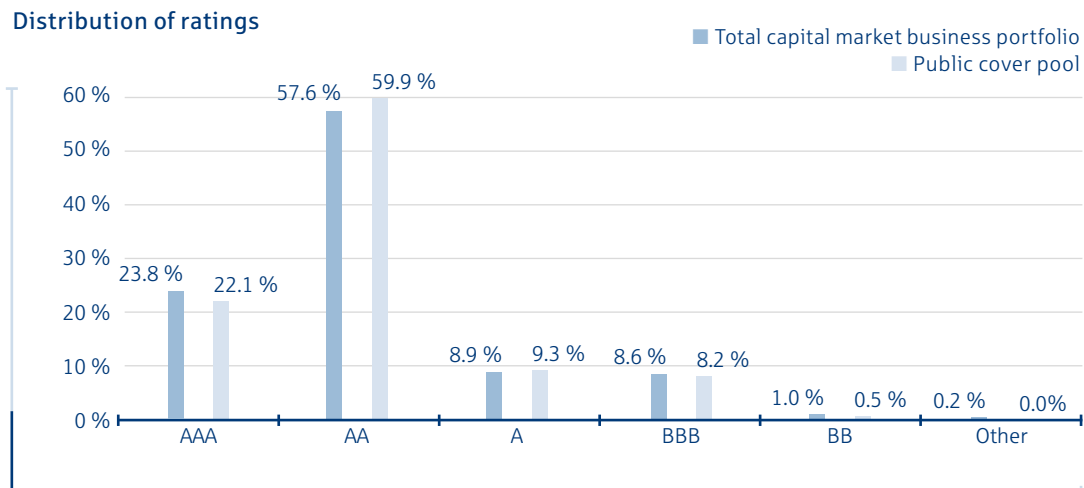
#### Distribution of ratings



### Cover pool for public Pfandbriefe

The share of loans with a rating of A to AAA in the cover pool of public Pfandbriefe was 91.3 % as of 31 December 2018 (2017: 91.2 %). This contributes to the high quality of the cover pool for the issued Pfandbriefe.

#### Distribution of ratings



#### 4.2.1.6 Risk management – risk bearing capacity

The risk bearing capacity (RBC) of Deutsche Hypo is monitored at 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. Various factors are examined under the NORD/LB Group's RBC model. Based on the ECB's ICAAP guideline, the risk bearing capacity is examined from both a normative and an economic perspective. The interplay of the two perspectives is explicitly taken into account. Concrete limits are derived for Deutsche Hypo in regards to credit risk, market price risk and liquidity risk. To check compliance with these limits, which constitute a central aspect of risk management at Deutsche Hypo, the risk contributions of the relevant risk types are calculated regularly. In the course of a value-at-risk approach, the risk contributions are standardised to a uniform confidence level of 99.9 % and generally a holding period of one year. Escalation mechanisms have been established for when limits are exceeded.

Managing the risk bearing capacity at Group level was further refined by NORD/LB in the course of 2018. Especially the market price risk is now more highly differentiated with regard to the influences of market fluctuations on the NORD/LB Group's capital ratios. New, additional risk limits are also derived from this for Deutsche Hypo. Another change is the elimination of a concrete limit for operational risk. Note that the relevant limits were adhered to at the Deutsche Hypo level.

#### 4.2.1.7 Current developments

The real estate markets remained stable in 2018. The positive environment and Deutsche Hypo's continued quality-oriented lending policies contributed to an ongoing low risk level in the real estate finance portfolio. Due to the strategic focus on the core business area of commercial real estate finance, risk management focuses on counterparty risks. The money and capital markets continued to be defined by ongoing low interest rates and a flat yield curve, which however had no material impact on the Bank's earnings and risk situation due to the tight management of market price risks. All of the Bank's funding needs could be met at adequate prices in 2018, even though the ECB's gradual withdrawal from the purchase programme in the fourth quarter led to slightly higher liquidity costs across the market. Counterparty and credit spread risks arising from the capital market business were further lowered through the selective reduction of positions and regular maturities. The significance of operational risks continues to be minor.

#### 4.2.2 Counterparty risk

Deutsche Hypo's counterparty risk consists of the credit risk including country risk. The financial investment risk has no strategic importance and is not relevant since there are no investments as of 31 December 2018. 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.

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





#### 4.2.2.1 Counterparty risk – goals and strategies

Credit risks are handled on the basis of the Bank's risk strategy for credit risks which, in turn, is part of the Group risk strategy. Deutsche Hypo's aim is to achieve a competitive level of profitability under risk and reward aspects and to take into account effectiveness and flexibility in terms of active management of the credit risk items in order to minimise unanticipated losses. The credit business and therefore the management of credit risks are a core competency in the portfolio and new business 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 property financing. 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 a comparable internal rating. Deutsche Hypo only pursues business with customers and counterparties that lie outside of the aforesaid credit rating focus after careful consideration of the opportunities and risks.

Active portfolio management and limitations are intended to ensure that the granularity of the credit portfolio is retained and concentration risks are avoided. 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 within the Bank for the new credit business for each market segment 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, methods and credit processes).

#### 4.2.2.2 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 and distinctly 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 credit risk controlling, credit risk management and special credits management.

Credit decisions as defined in MaRisk include all decisions on new loans, loan increases, loan takeovers, loan extensions and significant changes to risk-relevant properties of loans. Credit decisions are always made by two authorised employees or, for certain 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 credit decision is made by the responsible employee, two additional consenting votes – one vote from the market division and one from the back office division – are first required. The responsibility of the authorised employees is generally 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.

#### 4.2.2.3 Counterparty risk – management and monitoring

Deutsche Hypo's counterparty credit risk is controlled and monitored primarily through the stipulation of financial principles, the limit system and the rating system. The Bank also operates portfolio management for the optimisation of the income and risk structure. As portfolio-improving measures, not only 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 risk exist in the underlying portfolio. The Bank topped up one of the existing transactions in the reporting year. Future new business may also be included in the hedging transactions within the scope of a replenishment period. The total value of the guarantees included as of the balance sheet date is € 77.0 million (2017: € 85.0 million).

#### Financing principles

The financing principles as a risk management instrument must be applied by all the institutions affiliated with the Group. With financing principles, the back office division and the market division establish ex ante what requirements potential business should meet as a minimum. The financing principles serve as an effective pre-selection mechanism for business initiation and do not anticipate definitive decisions in individual cases. Here the focus is on the financing structure in connection with general property-related financing requirements:

- 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.

Furthermore, the following strict criteria apply as minimum risk standards in the commercial real estate finance business:

- 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 or most of the portfolio in the case of apartment portfolios is inspected by a Bank employee (IBC, market, KRM) or an expert hired by the Bank prior to the credit decision.
- The financing must run out within the market values upon the initial decision with due regard for the mitigants and/or additional securities.



**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 limits are binding across the Group. 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. Various limits for each business area at Deutsche Hypo exist within this framework. 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 segments 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 twelve-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 Sparkassen-Finanzgruppe and the Landesbanks. Deutsche Hypo uses the rating results as part of the basic internal ratings based approach to estimate the regulatory equity backing required and for the determination of expected economic losses. 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 from the portfolio perspective.

**Treatment of conspicuous exposures**

The use of sophisticated credit rating assessment processes cannot prevent the credit ratings of individual borrowers from deteriorating beyond expectations 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 division (drawing right). Proactive avoidance or reduction of potential capital losses is the goal. This division is responsible for exerting influence early on and introducing a restructuring process if necessary 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 or merit therein, an effort is made to optimise the income from the collateral in case of unwinding. Special Credit Management is also the sole centre of competence for appropriate risk provisioning and has to ensure an appropriate level of risk provisions at all times in this process.

The early identification of potential 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 effective limiting.

#### 4.2.2.4 Counterparty risk – collateral

Deutsche Hypo accepts collateral in order to reduce its credit risk. With regard to the commercial real estate finance business area, loans are generally secured by means of a mortgage in the amount of the loan. Mortgage collateral can be omitted in exceptional cases. A requirement for this is a good credit rating and observing 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 changes to the influencing 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 security 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 cover eligibility of the loan receivables and thus influences the volume of the cover pool available as security for Pfandbriefe issued by Deutsche Hypo, in accordance with the terms of the German 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 institutions and assigned 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.

#### 4.2.2.5 Counterparty risk – measurement

The direct quantification of the credit risk takes place for the Bank on the one hand at the level of the NORD/LB Group and on the other at the level of the individual institution of Deutsche Hypo. Credit risk is measured using the risk key figures of expected loss and unexpected loss. These are calculated on the basis of the determined probability of default and the anticipated loss amount per loan, taking into account any collateral. The expected loss corresponds to 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 volume of receivables after adjustments for the loan conversion factor, the rating or one-year probability of default and on the expected loss ratio. The unexpected loss for the credit risk is quantified using an economic credit risk model 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. It determines the unexpected loss at the level of the portfolio as a whole. The credit risk model can be used to study sub-portfolios and their share of the unexpected loss. The results of such analyses have 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. Deutsche Hypo uses the internal ratings based approach (basic IRBA) to calculate the regulatory equity backing required for credit risks pursuant to the CRR.



In addition, scenario calculations for the individual institution's portfolio in the form of stress test analyses are performed. The design of the Group-wide stress scenarios and their ongoing monitoring take place with the inclusion of Deutsche Hypo. Major 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. That applies correspondingly for the stress analysis of a real estate crisis, which is generally performed every two years. This makes it possible to carry out a risk-causing assignment of the credit risk potential to the business areas. The scenario analyses can be used as early warning instruments. Additional scenarios, for example focused on real estate financing, are calculated on a case-by-case basis.

#### 4.2.2.6 Counterparty risk – reporting

The quarterly risk report includes the credit risk sub-report. It contains a summary and analysis of 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 reports on conspicuous exposures as part of the early warning system and on the development of risk provisioning.

#### 4.2.2.7 Counterparty risk – analysis of the credit exposure

The credit exposure, a key reference indicator in credit risk controlling, represents the quantification of all 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 %. Revocable 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 2018 was € 23,475.6 million, down € 1,677.8 million as compared to the end of the previous year. In the commercial real estate finance business area, the volume of € 13,535.9 million was only slightly below the previous-year level. In contrast, the credit exposure for loans to local authorities fell significantly by € 1,047.5 million to € 2,852.8 million. There was also a significant decline of € 821.7 million in the portfolio of securities and derivatives. There is an increase of € 237.7 million in other financing products, which mainly arises from bank balances. These developments reflect 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 rating classes. This classification corresponds to the standard IFD rating 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 82.4 %, up from the previous-year level. This was due to the high proportion of exposures to governments, public authorities and financial institutions that have a good credit rating and the good ratings in the real estate finance portfolio.

The share of non-performing loans (NPL) in the overall exposure at 0.5 % was below the level of the previous year (0.8 %). The absolute volume fell by € 68.2 million to € 120.9 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 management in recent years for loan portfolios consisting of commercial real estate financing by means of cash guarantees are not included in the representation due to their effect on the pure mezzanine risk of the underlying portfolios.

#### Breakdown of total credit exposure by rating category according to IFD:

31.12.2018 in € millions	Real estate finance	Loans to local authorities	Securities	Deriva- tives	Other	Total exposure	Share in total exposure
Very good to good	9,804.1	2,852.8	4,352.6	603.5	1,739.6	19,352.6	82.4 %
Good / satisfactory	2,554.2	0.0	332.5	0.0	0.0	2,886.7	12.3 %
Still good / sufficient	868.7	0.0	16.2	0.0	0.0	884.9	3.8 %
Elevated risk	128.8	0.0	14.1	0.0	11.3	154.3	0.7 %
High risk	65.8	0.0	0.0	0.0	0.0	65.8	0.3 %
Very high risk	10.4	0.0	0.0	0.0	0.0	10.4	0.0 %
Default (=NPL)	103.9	0.0	0.0	17.0	0.0	120.9	0.5 %
<b>Total</b>	<b>13,535.9</b>	<b>2,852.8</b>	<b>4,715.5</b>	<b>620.6</b>	<b>1,750.9</b>	<b>23,475.6</b>	<b>100.0 %</b>

31.12.2017 in € millions	Real estate finance	Loans to local authorities	Securities	Deriva- tives	Other	Total exposure	Share in total exposure
Very good to good	10,083.0	3,849.0	5,128.9	640.0	791.7	20,492.6	81.5 %
Good / satisfactory	2,321.6	0.1	233.9	0.0	35.1	2,590.7	10.3 %
Still good / sufficient	765.4	51.2	123.0	0.0	669.1	1,608.7	6.4 %
Elevated risk	204.9	0.0	7.8	0.0	15.0	227.8	0.9 %
High risk	30.8	0.0	0.0	0.0	2.3	33.1	0.1 %
Very high risk	11.4	0.0	0.0	0.0	0.0	11.4	0.0 %
Default (=NPL)	164.9	0.0	0.0	24.2	0.0	189.1	0.8 %
<b>Total</b>	<b>13,582.2</b>	<b>3,900.3</b>	<b>5,493.6</b>	<b>664.2</b>	<b>1,513.2</b>	<b>25,153.4</b>	<b>100.0 %</b>

The Bank's credit exposure in the real estate finance business amounted to € 13,535.9 million at year end (2017: € 13,582.2 million) and 97.7 % of it (2017: 97.0 %) consisted of financing for customers that have a rating of at least satisfactory. In the past quarter, the volume-weighted average probability of default in the commercial real estate business (excluding defaults) only changed slightly and remains at a very low level of currently 0.31 % (2017: 0.30 %). The NPL volume sank further in comparison to the previous year to € 103.9 million (2017: € 164.9 million). The share of NPL in the overall portfolio was 0.8 %, down from 1.2 % in the previous year. Most of the NPL portfolio consisted of foreign financing, largely in the Netherlands and the UK. Overall the proportion of the NPL credit exposure also falls below the level of the long-term average values.

**Breakdown of the total credit exposure by segments and region:**

31.12.2018 in € millions	Real estate finance	Loans to local authorities	Securities	Deriva- tives	Other	Total expo- sure	Share in total exposure
Eurozone	11,355.2	2,683.5	3,472.7	366.3	1,743.0	19,620.6	83.6 %
<i>of which, Germany</i>	7,715.2	2,057.8	1,971.1	333.1	1,727.7	13,804.8	58.8 %
Other EU	2,031.4	8.2	175.5	39.6	4.5	2,259.2	9.6 %
<i>of which, UK</i>	1,641.8	0.0	83.5	25.2	4.5	1,754.9	7.5 %
Other Europe	0.0	67.6	50.4	56.0	0.0	174.0	0.7 %
North America	149.4	0.0	440.1	158.7	3.4	751.6	3.2 %
Central America	0.0	0.0	5.6	0.0	0.0	5.6	0.0 %
Middle East / Africa	0.0	0.0	0.0	0.0	0.0	0.0	0.0 %
Asia	0.0	0.0	238.2	0.0	0.0	238.2	1.0 %
Other	0.0	93.4	333.0	0.0	0.0	426.5	1.8 %
<b>Total</b>	<b>13,535.9</b>	<b>2,852.8</b>	<b>4,715.5</b>	<b>620.6</b>	<b>1,750.9</b>	<b>23,475.6</b>	<b>100.0 %</b>

31.12.2017 in € millions	Real estate finance	Loans to local authorities	Securities	Deriva- tives	Other	Total expo- sure	Share in total exposure
Eurozone	11,579.8	3,730.8	3,706.3	399.9	1,497.5	20,914.2	83.1 %
<i>of which, Germany</i>	7,993.5	2,716.8	2,011.3	350.3	1,392.6	14,464.4	57.5 %
Other EU	1,858.9	8.2	262.5	28.4	3.8	2,161.8	8.6 %
<i>of which, UK</i>	1,526.9	0.0	85.9	21.3	3.8	1,638.0	6.5 %
Other Europe	0.0	64.8	50.5	54.1	0.0	169.4	0.7 %
North America	143.5	0.0	490.1	181.8	11.9	827.4	3.3 %
Central America	0.0	0.0	5.7	0.0	0.0	5.7	0.0 %
Middle East / Africa	0.0	0.0	0.0	0.0	0.0	0.0	0.0 %
Asia	0.0	0.0	260.6	0.0	0.0	260.6	1.0 %
Other	0.0	96.4	718.0	0.0	0.0	814.4	3.2 %
<b>Total</b>	<b>13,582.2</b>	<b>3,900.3</b>	<b>5,493.6</b>	<b>664.2</b>	<b>1,513.2</b>	<b>25,153.4</b>	<b>100.0 %</b>

The breakdown of the credit exposure by segments and regions shows that 93.9 % (2017: 92.4 %) of the entire exposure is in Europe. The credit exposure in Germany as a percentage of the total exposure increased slightly to 58.8 % (2017: 57.5 %) during the reporting period.

The exposure in what are known as the PIIGS countries decreased significantly in recent years. Balances were further reduced beyond planned maturities in the past financial year, especially in Italy.

Real estate financing in the UK was analysed in particular against the background of a Brexit scenario. Even in case of considerable market changes, the results confirm the overall conservative portfolio structure. No significant negative effects are expected aside from individual special cases.

**Non-performing loans and credit exposures in arrears**

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 provisions 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 towards written-down claims are recorded in the income statement.

The specific loan loss provisions and provisions fell in the past financial year compared to the previous year, to € 27.7 million (2017: € 66.5 million). This amount was attributable to the countries of the euro-zone and North America. Of the overall NPL portfolio credit exposure of € 120.9 million (2017: € 189.1 million), € 24.1 million (2017: € 109.2 million) related to impaired loans in the core area of real estate finance, while € 17.0 million (2017: € 24.2 million) related to impaired transactions in the capital market business with derivatives, and € 79.8 million (2017: € 55.7 million) to overdue, non-impaired loans. The amount of specific loan loss provisions and provisions as a percentage of the total credit exposure as of 31 December 2018 was 0.12 % (2017: 0.26 %).

The period of default for the overdue, not impaired loans was less than 90 days. The overall amount of NPL exposures is secured by standard collateral, which is valued using the applicable lending principles.

#### 4.2.2.8 Counterparty risk – outlook

The Bank assumes that the current, consistent development in the real estate markets will generally persist in 2019. However, it cannot be assumed that the low level of risk provisioning will be maintained in the long term. This normalisation would also be associated with a moderate increase in the ratings. Deutsche Hypo therefore expects that the necessary risk provisioning and the risk-weighted assets in the core business area will once again approach the long-term average value. Even though the capital market environment was largely consistent in 2018, it cannot be ruled out entirely that individual capital market counterparties could face payment difficulties in the future. Depending on the specific framework conditions of the individual countries and their public authorities, this can also lead to different developments with regard to credit risks posed by such difficulties. Deutsche Hypo will monitor the performance of real estate and capital markets attentively and take suitable measures, if need be.

#### 4.2.3 Market price risk

Market price risk refers to the potential losses that could be incurred following changes in the market parameters. The focus of risk management and monitoring is on economic and earnings-oriented interest rate risks in the banking book, on credit spread risks and on currency risks.

##### 4.2.3.1 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. 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. Further opportunistic positioning – particularly with the goal of achieving the short-term realisation of speculative profits – is not pursued and also not planned.

The economic interest rate risks arise mainly from the investment of perpetually available equity. Earnings-oriented interest rate risks arise in the course of operational business activities and are largely caused by mismatches in the maturity structure of short-term fixed interest rates as well as different reference interest rates on the assets and liabilities side along with corresponding hedging transactions. They are of minor importance compared to economic interest rate risks. Interest rate risks in foreign currencies are not assumed.





To reduce credit spread risks, Deutsche Hypo has been pursuing the strategy of successively reducing the existing capital market portfolio while protecting the income statement for some years now. The capital market portfolio also comprises liquid securities that are retained to fulfil internal, legal and regulatory requirements for a liquidity reserve.

#### 4.2.3.2 Market price risk – structure and organisation

Against the background of the risk-related organisational structure, a range of divisions and committees 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 the 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. Ensuring the correctness of the transaction data in the data processing systems and the proper processing of the financial market business is handled by Treasury Operations in the market price risk management process. Controlling is responsible for various risk controlling tasks, for example related to risk assessment, controlling and monitoring processes, and reporting. It provides methods for managing, assessing and monitoring market price risks internally. Controlling and Treasury Operations are functionally and organisationally independent of Treasury.

#### 4.2.3.3 Market price risk – management and monitoring

Material market price risks are mainly managed using limits that take the risk strategy requirements into account. Factors including interest sensitivities, interest shocks and probability-based figures such as value-at-risk (VaR) and earnings-at-risk (EaR) are used for the economic and earnings-oriented management of interest rate risks in the banking book. VaR figures are also used to manage credit spread risks, together with the monitoring of hidden charges and the analysis of adverse scenarios. The management of currency risks is primarily handled by limiting currency results on the income statement in accordance with the German Commercial Code. To achieve these goals, the open nominal overhangs per currency are controlled within narrow early warning limits.

A major component of risk monitoring 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 limit violations. Compliance with the limits is monitored at various intervals from daily to quarterly.

To control or reduce market price 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. Derivatives such as interest and currency swaps as well as forwards are primarily used as hedging instruments. Additional information regarding hedging and the reporting of hedging relationships on the balance sheet is provided in the notes to the financial statements.

**4.2.3.4 Market price risk – reporting**

The quarterly risk report encompassing all risk types includes a sub-report on market price risk, which includes all the important information on strategic management of the market price risks.

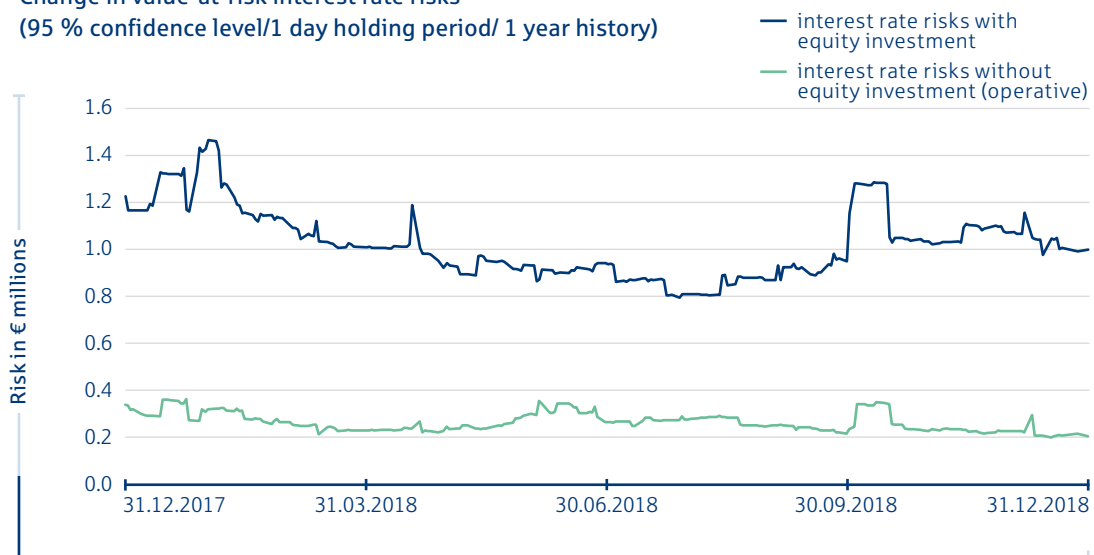
The Board of Managing Directors and Treasury receive a daily report to keep them informed of the economic interest rate risks and the income from the Bank’s interest maturity transformation. Weekly reporting is in place for the ALCO and also includes VaR indicators for interest rate and credit spread risks. The banking book’s hidden charges and reserves as well as the earnings-oriented risk figures are reported to the ALCO monthly or quarterly. Daily reports on foreign currency risks are also sent to Treasury.

**4.2.3.5 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 reporting year as expected. Also as expected, the very low, in part negative interest rates observed in the markets had a negligible impact on the Bank’s earnings and risk position.

The economic interest rate risk was mainly caused by the investment of perpetually available equity. Other interest rate risk caused by the Bank’s operational business activities, measured as a 100 basis point interest rate shock, was around € 3.0 million at the end of the year. The daily calculated VaR for the interest rate risk fluctuated between € 0.80 million and € 1.47 million in the reporting period, with an average of € 1.02 million. At the end of 2018, the effect of the BaFin interest rate shock at + 200 and – 200 basis points on the interest book cash value was 7 % of the regulatory equity. Both confirm Deutsche Hypo’s low risk appetite. The following chart shows the development of the VaR for interest rate risk (95 % confidence level, 1 day holding period) in the past reporting year, including the equity investment, along with the operative portfolio VaR (excluding the equity investment). Credit spread risks of the banking book are not included in the VaR. The chart clearly shows the minor importance of the operational portfolio for the economic interest rate risk.

**Change in value-at-risk interest rate risks  
(95 % confidence level/1 day holding period/ 1 year history)**



The nominal volume that involves credit spread risks totalled € 7,458.1 million as of 31 December 2018 (2017: € 9,250.3 million), a considerable decrease of € 1,792.2 million over the course of the year. The hidden charges in the capital market portfolio have been continuously and considerably reduced since 2014, following which they increased slightly again in 2018.

The systematic pursuit of the conservative risk-strategic goals and the attentive monitoring of the market developments in 2019 are also the focal points of controlling for the market price risk at Deutsche Hypo. In this context, this includes the continued strategy for a reduction in the positions that have credit spread risks in a way that protects the income statement, among other elements. For 2019, Deutsche Hypo expects the interest rate risk to remain low. The focus of the further development of the risk management process at Deutsche Hypo in 2019 will, among other things, be on fulfilling the requirements of the European regulatory authorities with regard to the interest rate risk in the banking book.

#### 4.2.4 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. Internally the liquidity risk is divided into classic liquidity risk including intra-day liquidity risk and liquidity spread risk.

##### 4.2.4.1 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. This is ensured by holding highly liquid, diversified and unencumbered assets and by stable funding sources. In funding the business activities in the market divisions, Deutsche Hypo fundamentally pursues the strategy of term-congruent funding. Involvement in structural liquidity-term transformation positions is of minor strategic significance for the Bank. The intraday liquidity risk has no appreciable impact. Complying with the regulatory LCR (liquidity coverage ratio) requirements at all times is anchored in the liquidity risk goals and strategies. Meeting the legal requirements of the German Pfandbrief Act (PfandBG) for ensuring sufficient liquidity in the cover pool complements the strategic requirements.

The Bank's Liquidity Policy (LP) constitutes the strategic framework directive for ensuring adequate liquidity. In the case of a liquidity crisis, the management of the liquidity risk in accordance with the LP concept is assumed by an independent committee 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 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 Funds Transfer Pricing Policy.

#### 4.2.4.2 Liquidity risk – structure and organisation

The process of liquidity risk management must include the ALCO first and foremost, and also 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 operational liquidity risk management. It is also responsible for the management of the intraday liquidity positions. As an independent monitoring unit, Controlling defines the internal processes for the measurement, limiting and monitoring of liquidity risks and carries out the operative model validation, monitoring and reporting functions. Controlling handles liquidity reporting in accordance with CRR.

#### 4.2.4.3 Liquidity risk – management and monitoring

Present value limits derived from the risk bearing capacity of the NORD/LB Group and volume structure limits are used to control and monitor the liquidity spread risks. Monitoring 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 liquidity spread 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. This 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. A standardised process is used to assess the materiality of individual foreign currencies. Insofar as individual foreign currencies are classified as significant, the classic liquidity risk is also monitored in these foreign currencies.

Additional scenarios and stress tests are also examined. Both institution-specific and market-wide crisis scenarios are modelled in this context. The goal is to avoid liquidity shortages both normally and in cases of crises. Additional liquidity in the case of stress is secured in accordance with the MaRisk requirements by maintaining a liquidity buffer consisting of unencumbered, diversified and highly liquid securities. The costs associated with a liquidity buffer are taken into account in the liquidity transfer price system.

Compliance at all times with minimum regulatory requirements for the liquidity coverage ratio (LCR) is ensured by the daily management and monitoring of the ratio. Management includes internal target ratios, which are set intentionally higher than the minimum regulatory requirements. The net stable funding ratio (NSFR) is increasingly coming into the focus of liquidity management as well. It is managed through internal planning specifications.



#### 4.2.4.4 Liquidity risk – reporting

The quarterly risk report provides the Board of Managing Directors and the Supervisory Board with comprehensive information about the current situation regarding the classic liquidity risk and liquidity spread risk as well as the regulatory liquidity indicators, LCR and NSFR. 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 cash limit for the liquidity spread risk as well as the LCR positions and ratios are also provided to Treasury daily.

#### 4.2.4.5 Liquidity risk – developments and outlook

In 2018 Deutsche Hypo had sufficient access at all times to the money market and capital market at conditions in line with the market. It was able to expand its product range and further diversify its investor base, in particular through the placement of a pound sterling debut issue in the amount of £ 355 million. The total issue volume presented in the economic report and measured in terms of the Bank's need made it possible to place sufficient secured and unsecured issues on the market. The changes to Section 46f of the German Banking Act (KWG) made in 2018 in regards to differentiating between preferred and non-preferred debt instruments had no material impact on the Bank's liquidity situation. Reduced net purchases of the ECB within the scope of the Expanded Asset Purchase Programme (EAPP) led to a market-wide increase in liquidity spreads for secured issues at the end of 2018. This had no negative impact on the Bank's liquidity risk situation in 2018.

All the volume structure limits were complied with in the past financial year with the help of forward-looking liquidity management. The present value liquidity spread risk dropped slightly compared to the previous year, and was met at all times. The Dtl metric from the dynamic liquidity stress test used for internal controlling and limiting was within the existing required range in 2018. The green phase in the traffic light system was maintained throughout the year. As of 31 December 2018, the Dtl was 293 days (2017: 265 days). Likewise, the Bank met the requirements for the maintained liquidity buffer in accordance with MaRisk throughout the course of 2018.

The applicable minimum regulatory LCR requirements of 100.0 % were met continuously in 2018. As of 31 December 2018 the ratio was at 264.1 % (2017: 345.7 %, 2018 average: 302.9 %). Internal planning specifications for the NSFR ratios were considerably over-fulfilled as of 31 December 2018.

More enduring uncertainties resulting from the Group situation and an associated downgrade of the rating of the Bank or parent company could have adverse impacts on the funding terms, significantly impair access to the capital market, or fundamentally restrict the funding options especially in the unsecured sector. The ECB's SREP process may impose additional liquidity requirements by way of discretionary decisions. For that reason very close management and monitoring of the liquidity situation will be performed in 2019.

Furthermore, the minimum regulatory requirements for the NSFR ratio will become more concrete and increasingly move into the focus of management. What the requirements will be in regards to an individual MREL ratio (minimum requirement for own funds and eligible liabilities) for Deutsche Hypo based on the policy of the Single Resolution Board (SRB) of 16 January 2019 remains to be seen.

#### 4.2.5 Operational risk

Operational risks are possible events, unintended from the Bank's perspective, that occur due to the inadequacy or failure of internal processes, employees or technologies or due to external influences and lead to damage or significant negative consequences for the Bank. 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, information security risks and vulnerability risks in emergency and crisis management as well as HR risks.

##### 4.2.5.1 Operational risk – goals and strategies

The guidelines for dealing with operational risks are formulated in the Group risk strategy. These encompass the timely identification of operational risks and the initiation of meaningful countermeasures regarding economic and risk strategy aspects. Operational risks should generally be avoided, transferred or alleviated. The guidelines also include the goal of avoiding future damage through a solid risk culture, which encompasses dealing with operational risks openly. Operational risks must be taken into account in all company decisions. There are framework conditions in the form of technical and organisational measures, contractual provisions and work 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 understanding of risks play a key role in this context.

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 method. 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.

##### 4.2.5.2 Operational risk – structure and organisation

The Board of Managing Directors and all other Bank divisions are included in the process of managing operational risks. Within the set framework conditions, responsibility for the controlling of operational risks is decentralised and lies with the individual divisions. An integrated, Group-wide approach is used for controlling operational risks and continuously optimised. The Risk Round Table committee is a platform for discussing important matters of relevance to operational risk, the evaluation of such matters by the Bank, and the assessment of possible future risks within Deutsche Hypo at the level of division heads and experts. A uniform risk matrix is used for the assessment of risks. Controlling handles the central tracking of operational risks and their independent reporting.



#### 4.2.5.3 Operational risk – management 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 adapted to an appropriate extent in view of the type and scope, structure and operational risk situation of the Bank.

The management of operational risks is supported in this context by a methodological framework for risk assessment. Against the background of a constantly updated assessment of the risk situation, ongoing extensive information such as cases of loss, risk indicators and the results of scenario analyses is evaluated. Suitable countermeasures are taken by the responsible divisions if the occasion requires it. For example, in the past financial year, investments in the IT systems continued with the aim of strengthening the level of IT and information security over the long term, 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 established to ensure the prompt introduction of countermeasures.

#### 4.2.5.4 Operational risk – reporting

In the course of the ongoing risk management process, the results from the Risk Round Table committee are processed as part of the risk report. Current risk is assessed using a traffic light system overview on the basis of different risk categories. This examination includes the recorded risk indicators, information from the loss event database, the results of the scenario analyses and the risk assessment of the ongoing legal disputes and externally outsourced significant activities. Special events in the reporting period are reported as well, such as damage or ad hoc reports, as well as the OpVaR determined for Deutsche Hypo by NORD/LB AöR. The Board of Managing Directors and the Supervisory Board are informed of the current status in the quarterly risk report.

#### 4.2.5.5 Operational risk – development

Significant cases of damage were not noted in 2018. Existing risks were adequately taken into account with the existing provisions for legal uncertainties arising from existing contracts in the credit business at € 7.8 million.

#### 4.2.6 Accounting-related internal control system and risk management system

The accounting-related internal control system (ICS) is 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 as warranted on occasion, their results must be documented and their appropriateness has to be checked at regular intervals. They include ongoing manual control tasks within the work process and programmed controls within the IT systems. In particular, controls have been implemented at the interfaces between the participating divisions and 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 accounting transactions from supplying divisions is their responsibility, and is subject to directed controls. The functions of the Bank's divisions involved in the accounting process are separated and areas of responsibility are clearly assigned.
- 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 access restrictions.
- The continuous monitoring of the IT systems by appropriately trained employees of the Bank and external system partners reduces the risk of downtime and ensures high availability.
- The Bank has implemented a system of guidelines and instructions in an organisation manual that takes the form of an organisational structure and workflows.
- All accounting processes are subject to consistent manual and automated controls according to the principle of dual control.
- Bookkeeping files that are received or forwarded are continuously checked for completeness and accuracy, for example by means of random sampling. Programmed plausibility tests are conducted by the software that is used.
- The plausibility of the data determined in the accounting process is regularly checked.
- Internal Audit checks compliance with 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 legal and internal company specifications form the basis for a proper accounting process. Report recipients are therefore provided with accurate and reliable information.

#### 4.2.7 Regulatory equity resources

Due to the exercising of the waiver rule, the obligations to provide individual bank reports, compliance with the equity and capital requirements and the regulatory equity resource requirements in accordance with CRR, part 2 and 3, do not apply to Deutsche Hypo at the level of the individual institution. For the reports on the equity resources at Group level according to IFRS and for internal controlling in line with HGB, Deutsche Hypo calculates, after exercising the waiver rule, the equity capital and risk-weighted assets (RWA) that are consolidated in the IFRS reports prepared by NORD/LB for the Group. The Bank also follows the HGB to calculate an equity ratio, which compares all eligible equity in accordance with Art. 4 (1) no. 71 CRR with the risk-weighted assets.

In accordance with the regulatory requirements, a total of € 1,054.8 million (2017: € 1,123.0 million) was eligible for recognition under regulatory capital requirements in the Group as of the balance sheet date. This means a decline of € 68.3 million relative to the end of 2017 due to the planned maturity of supplementary capital components and a slightly lower excess of loan loss provision. Simultaneously the RWA increased slightly by 2.9 %. Therefore the equity ratio was 18.5 % (2017: 20.3 %).





#### 4.2.8 Summary of the risk position

From the perspective of the Board of Managing Directors, Deutsche Hypo has systematically continued its conservative risk policy in 2018. The Bank's risk position remains favourable at the individual institution level (without considering the risks due to dependency on NORD/LB). In particular, significant further reductions were realised in the capital market portfolio in line with the business strategy in 2018, thereby reducing the accompanying credit spread risks. The Bank's interest rate risk also remained very low as a result of Deutsche Hypo's low risk appetite.

Due to the ongoing positive development of the commercial real estate markets and the constant focus on quality when acquiring new business, the risk indicators for the credit portfolio continue to confirm its high level. This is indicated among other things by the historically low proportion of financing in default out of the overall portfolio.

Deutsche Hypo was able to adequately cover its funding requirements at all times at conditions in line with the market during the past financial year. Internal and regulatory minimum liquidity requirements were met at all times. All regulatory requirements and those derived from the German Pfandbrief Act (PfandBVG) as well as the Group's strategic rules were also met.

Due to the dependency on NORD/LB, the developments at NORD/LB affect the risk position of Deutsche Hypo as well. Detailed discussions are found in sections 4.1.2.4 "Dependencies of Deutsche Hypo on NORD/LB" and 4.2.4.5 "Liquidity risk – developments and outlook". Please refer to those sections.

Deutsche Hypo will continue to systematically pursue its conservative risk policy. This includes the continuation of the reduction of its public sector finance portfolio while protecting the income statement and the adherence to high risk standards in the commercial real estate finance business. Deutsche Hypo will push ahead with the continuous improvement of its risk expertise and the consistent optimisation of the risk structure in the future.

Hanover, 2 April 2019

The Board of Managing Directors



Barthauer



Rehfus



# ANNUAL FINANCIAL STATEMENTS

**Balance sheet as of 31 December 2018**

**Income statement for the period  
from 1 January to 31 December 2018**

**Statement of changes in equity**

**Cash flow statement**

**Notes**

# BALANCE SHEET AS OF 31 DECEMBER 2018

## ASSETS

	€	€	€	31 December 2017 (in € thousands)
<b>1. Cash reserve</b>				
b) Credit with central banks		13,661,609.18		648,151
of which:				
with the "Deutsche Bundesbank"				
€ 13,661,609.18 (PY € 648,151 thousand)				
			<b>13,661,609.18</b>	<b>648,151</b>
<b>2. Receivables from financial institutions</b>				
a) Mortgage loans		7,853,506.09		10,582
b) Loans to local authorities		298,008,686.93		487,081
c) Other receivables		997,234,263.56		1,375,328
of which: due daily				
€ 679,161,858.23 (PY € 773,251 thousand)				
			<b>1,303,096,456.58</b>	<b>1,872,991</b>
<b>3. Receivables from customers</b>				
a) Mortgage loans		12,256,143,856.00		12,066,514
b) Loans to local authorities		2,546,400,983.47		3,405,403
c) Other receivables		17,005,836.05		16,868
			<b>14,819,550,675.52</b>	<b>15,488,785</b>
<b>4. Bonds and other fixed interest securities</b>				
b) Bonds and debentures				
ba) from public issuers	2,282,180,123.44			2,847,185
of which:				
lendable to the "Deutsche Bundesbank"				
€ 1,489,320,955.19 (PY € 1,533,444 thousand)				
bb) from other issuers	2,434,434,406.73			2,642,680
of which:				
lendable to the "Deutsche Bundesbank"				
€ 2,299,337,314.30 (PY € 2,365,299 thousand)				
c) Own bonds		4,716,614,530.17		26,650
Nominal amount:		46,868,711.97		
€ 47,297,000.00 (PY € 26,479 thousand)				
			<b>4,763,483,242.14</b>	<b>5,516,515</b>
<b>5. Intangible assets</b>				
b) Purchased licenses, industrial property rights, as well as licenses to such rights and assets				
d) Payments made on account		1,382,126.00		595
		119,348.67		1,056
			<b>1,501,474.67</b>	<b>1,651</b>
<b>6. Tangible assets</b>			<b>1,770,062.03</b>	<b>2,146</b>
<b>7. Other assets</b>			<b>121,789,784.37</b>	<b>118,968</b>
<b>8. Accrued and deferred items</b>				
a) from the issue and loan transaction		42,903,588.13		40,530
b) others		5,081,413.81		8,532
			<b>47,985,001.94</b>	<b>49,062</b>
<b>Total assets</b>			<b>21,072,838,306.43</b>	<b>23,698,269</b>

Balance sheet as of 31 December 2018 | Income statement for the period from 1 January to 31 December 2018 |  
Statement of changes in equity | Cash flow statement | Notes

## LIABILITIES

	€	€	€	31 December 2017 (in € thousands)
<b>1. Liabilities to financial institutions</b>				
a) Issued registered mortgage Pfandbriefe		191,895,000.88		276,014
b) Issued registered public Pfandbriefe		278,093,880.59		283,487
c) Other liabilities		2,643,359,029.73		3,117,686
of which: due daily				
€ 324,473,489.24 (PY € 339,357 thousand)				
			<b>3,113,347,911.20</b>	<b>3,677,187</b>
<b>2. Liabilities to customers</b>				
a) Issued registered mortgage Pfandbriefe		680,490,146.20		684,296
b) Issued registered public Pfandbriefe		3,385,837,927.76		3,825,684
d) Other liabilities		3,253,996,928.61		3,554,438
with which: due daily				
€ 8,747,370.70 (PY € 1,448 thousand)				
			<b>7,320,325,002.57</b>	<b>8,064,418</b>
<b>3. Securitised liabilities</b>				
a) Assigned bonds				
aa) mortgage Pfandbriefe	7,255,699,076.51			7,453,756
ab) public Pfandbriefe	142,989,875.19			381,203
ac) other bonds	1,784,279,413.32			2,677,420
		9,182,968,365.02		
			<b>9,182,968,365.02</b>	<b>10,512,379</b>
<b>4. Other liabilities</b>				
			<b>83,446,996.03</b>	<b>62,564</b>
<b>5. Accrued and deferred items</b>				
a) from the issue and loan transaction		28,559,334.94		31,125
b) other		11,307,373.33		13,605
			<b>39,866,708.27</b>	<b>44,730</b>
<b>6. Provisions</b>				
a) Provisions from pensions and similar obligations		54,162,976.72		48,373
b) Tax provisions		2,273,926.51		2,796
c) Other provisions		44,374,796.92		33,750
			<b>100,811,700.15</b>	<b>84,919</b>
<b>7. Subordinated liabilities</b>			<b>379,500,000.00</b>	<b>379,500</b>
<b>8. Jouissance right capital</b>			<b>0.00</b>	<b>20,000</b>
<b>9. Funds for general banking risks</b>			<b>14,400,000.00</b>	<b>14,400</b>
<b>10. Equity</b>				
a) Subscribed capital		80,640,000.00		80,640
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		
			<b>838,171,623.19</b>	<b>838,172</b>
<b>Total liabilities</b>			<b>21,072,838,306.43</b>	<b>23,698,269</b>
<b>1. Contingent liabilities</b>				
b) Liabilities arising from sureties and guarantee agreements		462,220,285.65		502,232
			<b>462,220,285.65</b>	<b>502,232</b>
<b>2. Other obligations</b>				
c) Irrevocable credit commitments		1,061,605,702.61		1,378,660
			<b>1,061,605,702.61</b>	<b>1,378,660</b>

# INCOME STATEMENT

FOR THE PERIOD FROM 1 JANUARY TO 31 DECEMBER 2018

	€	€	€	1 January 2017 – 31 December 2017 (in € thousands)
<b>1. Interest earnings from</b>				
a) Credit and money market transactions	428,519,477.94			493,617
less negative interest from money market transactions	<u>- 2,965,345.00</u>	425,554,132.94		- 3,303
b) Fixed interest bearing securities and book-entry securities		<u>119,445,697.70</u>		156,267
			544,999,830.64	
<b>2. Interest expenses</b>				
Interest expenses from the banking business	372,728,701.70			462,633
less positive interest from the banking business	<u>- 5,136,592.38</u>			- 9,405
			<u>367,592,109.32</u>	
			<b>177,407,721.32</b>	<b>193,353</b>
<b>3. Commission income</b>			10,736,688.88	11,983
<b>4. Commission expenses</b>			<u>10,844,031.54</u>	11,635
				<u>348</u>
			<b>- 107,342.66</b>	<b>348</b>
<b>5. Other operating income</b>				<b>16,455</b>
<b>6. General administrative expenses</b>				
a) Personnel expenses				
aa) wages and salaries		32,942,721.66		39,065
ab) social security and expenses for pension plans and for support of which:		10,189,752.25		6,763
for pension plans				
4,293,431.58 € (PY € 1,105 thousand)			43,132,473.91	
b) Other administrative expenses			<u>39,925,367.78</u>	37,202
			<b>83,057,841.69</b>	<b>83,030</b>
<b>7. Write-downs and value adjustments of intangible assets and tangible fixed assets</b>				<b>744</b>
			<b>959,468.65</b>	
<b>8. Other operating expenses</b>				<b>12,217</b>
			<b>9,769,774.06</b>	
<b>9. Write-downs and value adjustments on receivables and specific securities as well as allocations to provisions in credit business</b>				
			20,271,742.25	41,268
			<b>20,271,742.25</b>	<b>41,268</b>
<b>10. Write-downs and value adjustments on participatory interest, shares in affiliated companies and on securities treated as fixed assets</b>				
			0.00	10,190
			<b>0.00</b>	<b>10,190</b>
<b>11. Income from write-ups of participatory interest, shares in affiliated companies and securities treated as fixed assets</b>				
			9,091,808.84	0
			<b>9,091,808.84</b>	<b>0</b>
<b>12. Result from normal operations</b>			<b>74,701,306.11</b>	<b>62,707</b>
<b>13. Extraordinary income</b>			294,811.00	689
<b>14. Extraordinary expenses</b>			<u>16,831,569.74</u>	14
<b>15. Extraordinary result</b>				<b>675</b>
			<b>- 16,536,758.74</b>	
<b>16. Taxes on income</b>			2,920,481.65	3,724
<b>17. Other taxes not included under item 8</b>			<u>48,439.34</u>	- 87
			<b>2,968,920.99</b>	<b>3,637</b>
<b>18. Profits surrendered under partial surrender agreements or a profit and loss transfer agreement</b>				
			<b>55,195,626.38</b>	<b>59,745</b>
<b>19. Profit for the period</b>			<b>0.00</b>	<b>0</b>
<b>20. Transfer to profit reserves</b>			<b>0.00</b>	<b>0</b>
<b>21. Balance sheet profit</b>			<b>0.00</b>	<b>0</b>

Balance sheet as of 31 December 2018 | Income statement for the period from 1 January to 31 December 2018 |  
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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 2018	80,640	0	481,314	276,218	0	0	0	838,172
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 2018	80,640	0	481,314	276,218	0	0	0	838,172

in Tsd. €	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 2017	80,640	75,000	481,314	276,218	0	0	0	913,172
Capital increase / reduction	0	- 75,000	0	0	0	0	0	- 75,000
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 2017	80,640	0	481,314	276,218	0	0	0	838,172

# CASH FLOW STATEMENT

in € thousands	1 January – 31 December 2018	1 Januar – 31 December 2017
1. Net result	0	0
2. Write-downs, value adjustments and write-ups to receivables and tangible fixed assets	12,313	42,639
3. Increase/decrease in reserves	856	8,886
4. Other non-cash expenses/income	0	0
5. Profit/loss from the disposal of tangible fixed assets	– 42,497	– 45,952
6. Profit to be surrendered under a profit and loss transfer agreement	55,196	56,280
7. Other adjustments (balance)	– 2,352	1,902
8. Increase/decrease of receivables from financial institutions	536,827	118,127
9. Increase/decrease of receivables from customers	635,327	702,632
10. Increase/decrease of securities (if not financial assets)	– 20,410	12,557
11. Increase/decrease of other assets from current operations	– 14,526	– 46,582
12. Increase/decrease of liabilities to financial institutions	– 532,270	– 1,588,036
13. Increase/decrease of liabilities to customers	– 730,543	954,805
14. Increase/decrease of securitised liabilities	– 1,317,243	– 520,012
15. Increase/decrease of other liabilities from current operations	37,896	– 105,249
16. Interest expenses/income	– 177,408	– 193,353
17. Expenses/income from extraordinary items	16,537	– 675
18. Income tax expenses/income	2,920	3,724
19. Interest and dividend payments received	587,968	660,171
20. Interest paid	– 389,552	– 453,192
21. Extraordinary deposits	0	0
22. Extraordinary disbursements	– 978	0
23. Income tax payments	– 3,303	– 2,303
<b>24. Cash flow from current operations (total of items 1 to 23)</b>	<b>– 1,345,242</b>	<b>– 393,631</b>
25. Deposits from disposals of financial assets	854,170	1,346,594
26. Disbursements for investments in financial assets	– 43,958	– 87,866
27. Deposits from disposals of tangible fixed assets	3	0
28. Disbursements for investments in tangible fixed assets	– 246	– 518
29. Deposits from disposals of intangible fixed assets	0	0
30. Disbursements for investments in intangible fixed assets	0	0
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)	– 192	– 760
34. Deposits from extraordinary items	0	0
35. Disbursements for extraordinary items	0	0
<b>36. Cash flow from investment activities (total of items 25 to 35)</b>	<b>809,777</b>	<b>1,257,450</b>
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	– 22,744	– 34,100
46. Profit and loss transfer	– 56,280	– 101,609
47. Changes in funds from other capital (balance)	– 20,000	– 130,500
<b>48. Cash flow from financing activities (total of items 37 to 47)</b>	<b>– 99,024</b>	<b>– 266,209</b>
49. Cash changes in finance funds (total from 24, 36, 48)	– 634,489	597,610
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	648,151	50,541
<b>53. Finance funds at the end of period (total of items 49 to 52)</b>	<b>13,662</b>	<b>648,151</b>

The cash flow statement was prepared in accordance with the recommendations of the German Accounting Standard (DRS) 21. The finance funds results from the bank's cash reserve shown in the balance sheet, which exclusively contains credit with the Deutsche Bundesbank. The credit balance is not subject to any restrictions on disposal. Existing bank balances at other banks were not included in the finance funds. Deutsche Hypo does not have any securities that meet the definition of DRS 21 for an addition to cash equivalents and thus for an addition to finance funds.



## 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 2017 were published on 8 May 2018 in the federal gazette.

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

#### 2. Accounting regulations

The annual financial statements of Deutsche Hypo for financial year 2018 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 foreign locations. These are calculated on the basis of the taxable result at the applicable income tax rate.

### 3. Events after the reporting date

After the balance sheet date NORD/LB published an ad hoc announcement on 2 February 2019 among other things. According to this announcement, significant annual losses are expected and the common Equity tier 1 capital ratio will periodically fall below the regulatory threshold for financial year 2018 at Group level as a result of for example additional risk provisioning for NORD/LB's NPL portfolio and associated portfolio transactions. The ad hoc announcement stated that the owners of NORD/LB have decided to focus on a joint solution with the Deutscher Sparkassen- und Giroverband e. V. (DSGV) for capital strengthening in the public sector. According to the ad hoc announcement, this solution will be concretised in further discussions with the DSGV. It will need to be agreed with the relevant regulatory authorities and issues around state aid clarified.

NORD/LB assumes that the capital ratios will bounce back in future and will satisfy all regulatory requirements when the planned measures for capital strengthening and realignment of the business model are implemented. The measures for realigning the NORD/LB business model envisage an extensive transformation of individual business areas and subsidiaries of the Bank and Group over the coming years.

### 4. Statements on the continuation of business activity

The assumption of a continuation of business activity (going concern) for accounting and valuation purposes and the survival of Deutsche Hypo is dependent on the survival of NORD/LB given the dependencies set out above. The survival of NORD/LB in turn faces significant uncertainty and is premised in particular on

- the intended capital strengthening measures at NORD/LB level being implemented, completed and approved by all relevant stakeholders, in particular the regional parliaments of Lower Saxony and Saxony-Anhalt as well as the Deutscher Sparkassen- und Giroverband e. V., enabling renewed compliance the capital ratios and buffers and thresholds required under regulatory law,
- banking regulation authorities, in particular the European Central Bank, the German Federal Institute for the Supervision of Financial Services and the Deutsche Bundesbank, tolerating a shortfall of the regulatory minimum capital quotas up to the point of the completion of the intended measures for capital strengthening at NORD/LB level,
- all official approvals required for implementation, in particular from the EU Commission and the relevant banking regulation authority, being granted and
- the realignment of the business model and the intended restructuring measures being implemented as planned.

If the intended capital strengthening measures at NORD/LB level are not conducted as planned, the outcome may be the winding up of NORD/LB. This eventuality or a rating downgrade or other adverse developments may trigger significant outflows of short-term funds, fundamentally limiting the funding options for NORD/LB.

A successful implementation of the realignment of the NORD/LB business model also presupposes the requisite acceptance by the market participants and other relevant stakeholders.



A winding up of NORD/LB could result in a winding up or a sale of Deutsche Hypo. Such a situation or a rating downgrade of NORD/LB or other adverse developments may fundamentally limit the funding options for Deutsche Hypo.

## 5. 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 recognised in accordance with the lower-of-cost-or-market-principle pursuant to Section 253 (4) of the HGB. Zero coupon bonds are measured at cost plus accrued interest. 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.

Applying Section 340c (2) clause 1 of the HGB, the expenses from write-downs on 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. If a permanent impairment is considered likely, unscheduled write-downs are performed. Assets with costs between € 250.01 and € 1,000.00 are capitalised as compound items in accordance with Section 6 (2a) of the German Income Tax Act (EStG) and written off on a flat-rate basis at 20 % respectively per year over a period of five years. Low-value assets with costs of less than € 250.00 are written off in full in the year of acquisition in accordance with the procedure under tax law.

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

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.

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 differing amount pursuant to Section 253 (6) clause 1 of the HGB totalled € 9,776 thousand as of 31 December 2018 (2017: € 8,250 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 new 2018 G mortality tables published by Heubeck AG as of the reporting date were used to calculate pension provisions. This resulted in an increase in pension provisions attributable to a separate period of € 326 thousand and further personnel-related provisions of € 21 thousand. The calculation was based on the following actuarial assumptions as of 31 December 2018:

	31.12.2018	31.12.2017
Actuarial interest	3.21 %	3.68 %
Mortality tables	Heubeck RT 2018 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 were fund assets from reinsurance contracts at a fair value of € 3,868 thousand (2017: € 3,048 thousand) as of the balance sheet date that is netted with the pension provision under application of Section 246 (2) clause 2 of the HGB. The fair value as defined in Section 255 (4) clause 4 of the HGB is equal to amortised cost calculated in accordance with the lower-of-cost-or-market-principle pursuant to Section 253 (4) of the HGB. The fund assets of the insurance contract were calculated in accordance with the calculation principles as defined in Section 169 (3) of the German Insurance Contracts Act. The settlement value of the covered obligations amounted to € 12,724 thousand as of the balance sheet date. The reinsurance contract resulted in an income contribution equal to the change in the asset value compared to the previous period, plus insurance benefits received in financial year 2018 and less insurance premiums paid in financial year 2018. Income from pledged reinsurance contracts amounted to € 104 thousand in the reporting year (2017: € 117 thousand).

The tax provisions and other provisions are set in accordance with the requirements of Section 249 (1) clause 1 of the HGB in conjunction with Section 253 (1) clause 2 and, 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 financial years. 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.

Restructuring provisions are recognised to the extent that the Bank incurs liabilities or surplus obligations under a restructuring programme from which it is unable to escape. Deutsche Hypo recognises provisions from announced personnel-related measures under other provisions. As soon as the obligation is quantifiable and can be defined with a suitable degree of certainty, for example due to signed contracts, amounts are reclassified to other liabilities or to provisions for pensions and similar obligations. Income and expenses from restructuring measures are recognised in the extraordinary result. Restructuring provisions amounted to € 15.8 million as of the balance sheet date.

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 transactions as well as day-to-day money and fixed-term deposits. The amount of negative interest in the items “interest income” and “interest expenses” is set out separately in the income statement.

## 6. 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 (ECB reference rate).

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 as net amounts under “other operating expenses” or under “other operating income”.

The amount of net assets denominated in foreign currency totalled € 2,534.4 million as of the reporting date (2017: € 2,798.7 million); the amount of the liabilities denominated in a foreign currency was € 559.7 million (2017: € 417.5 million).

## 7. 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.

Balance sheet valuation units did not exist as of the reporting date.

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.

## 8. 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 of the HGB 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.



Balance sheet as of 31 December 2018 | Income statement for the period from 1 January to 31 December 2018 | Statement of changes in equity | Cash flow statement | Notes

## Notes on the balance sheet

### 9. Receivables from financial institutions

in € thousands	31.12.2018	31.12.2017
<b>Breakdown of residual maturities</b>		
due daily	679,162	773,251
up to three months	105,530	484,803
between three months and one year	152,074	161,042
between one year and five years	10,218	64,716
more than five years	200,565	200,564
proportionate interest in total	155,547	188,614
<b>Balance sheet item</b>	<b>1,303,096</b>	<b>1,872,990</b>
of which from affiliated companies	174,294	357,325

### 10. Receivables from customers

in € thousands	31.12.2018	31.12.2017
<b>Breakdown of residual maturities</b>		
up to three months	337,861	352,719
between three months and one year	1,436,555	1,302,346
between one year and five years	6,188,673	6,352,012
more than five years	6,781,288	7,391,308
proportionate interest in total	75,174	90,400
<b>Balance sheet item</b>	<b>14,819,551</b>	<b>15,488,785</b>

### 11. Bonds and other fixed interest securities

in € thousands	31.12.2018	31.12.2017
<b>Balance sheet item</b>	<b>4,763,483</b>	<b>5,516,515</b>
of which to affiliated companies	1,009,319	1,030,595
of which due in the following year	1,024,112	400,136
of which exchange eligible	4,763,483	5,516,515
of which listed on exchanges	4,535,628	4,843,545
of which not listed on exchanges	227,855	672,970
of which not valued at the lower of cost or market value*)	308,702	234,539
fair value of securities not valued at lower of cost or market value	270,199	201,907

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

## 12. Fixed asset schedule

in € thousands	Intangible assets	Tangible assets*)
<b>Balance sheet date 31.12.2017</b>	1,651	2,146
<b>Historical costs 01.01.2018</b>	9,443	5,034
Change in additions	192	246
Change in disposals	0	- 15
<b>Historical costs 31.12.2018</b>	9,635	5,264
<b>Accumulated depreciation as of 01.01.2018</b>	7,791	2,888
Depreciation in current financial year	342	618
Change in disposals	0	- 11
<b>Accumulated depreciation as of 31.12.2018</b>	8,133	3,495
<b>Balance sheet date 31.12.2018</b>	1,501	1,770

\*) Tangible assets involve only business and office equipment.

in € thousands	Securities**)
<b>Balance sheet date 31.12.2017</b>	5,489,865
Change*)	- 773,250
<b>Balance sheet date 31.12.2018</b>	4,716,615

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

\*\*\*) Securities treated as fixed assets.

## 13. Other assets

in € thousands	31.12.2018	31.12.2017
<b>Balance sheet item</b>	121,790	118,968
of which adjustment items from foreign currencies	120,633	113,359

## 14. Accrued items

in € thousands	31.12.2018	31.12.2017
<b>Balance sheet item</b>	47,985	49,062
of which premium on claims	8,459	10,930
of which issuing discount from bonds	34,444	29,600





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## 15. Liabilities to financial institutions

in € thousands	31.12.2018	31.12.2017
<b>Breakdown of residual maturities</b>		
due daily	324,473	339,357
up to three months	971,519	1,204,862
between three months and one year	1,042,068	995,529
between one year and five years	194,653	518,671
more than five years	411,908	420,673
proportionate interest in total	168,727	198,095
<b>Balance sheet item</b>	<b>3,113,348</b>	<b>3,677,187</b>
of which not senior liabilities with preferential treatment*)	397,570	–
of which assets pledged	498,888	835,169
as collateral to affiliated companies	1,542,552	1,609,403
of which within the context of real pension transactions	1,542,552	1,609,403

\*) These are debt instruments as defined in Section 46f (6) clause 1 of the KWG as amended 10 July 2018.

## 16. Liabilities to customers

in € thousands	31.12.2018	31.12.2017
<b>Breakdown of residual maturities</b>		
due daily	8,747	1,448
up to three months	414,799	433,691
between three months and one year	1,123,150	1,111,989
between one year and five years	2,192,091	2,472,339
more than five years	3,470,219	3,919,854
proportionate interest in total	111,319	125,097
<b>Balance sheet item</b>	<b>7,320,325</b>	<b>8,064,418</b>
of which not senior liabilities with preferential treatment*)	1,955,658	–

\*) These are debt instruments as defined in Section 46f (6) clause 1 of the KWG as amended 10 July 2018.

## 17. Securitised liabilities

in € thousands	31.12.2018	31.12.2017
<b>Balance sheet item</b>	<b>9,182,968</b>	<b>10,512,379</b>
of which not senior liabilities with preferential treatment*)	1,591,000	–
of which due in the following year	1,548,162	2,967,523
of which from affiliated companies	247,392	759,230

\*) These are debt instruments as defined in Section 46f (6) clause 1 of the KWG as amended 10 July 2018

## 18. Other liabilities

in € thousands	31.12.2018	31.12.2017
<b>Balance sheet item</b>	<b>83,447</b>	<b>62,564</b>
of which adjustment items from foreign currencies	67,297	47,813
of which pro-rata interest on subordinated liabilities	10,986	10,986

## 19. Deferred items

in € thousands	31.12.2018	31.12.2017
<b>Balance sheet item</b>	<b>39,867</b>	<b>44,729</b>
of which discounts on claims	4,961	6,632

## 20. Subordinated liabilities

Subordinated liabilities stood at € 379.5 million (2017: € 379.5 million) as of the balance sheet date. 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 regulatory 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 € 21.0 million in the reporting period (2017: € 21.6 million). As of the balance sheet date, there were subordinated liabilities to affiliated companies in the amount of € 165.0 million (2017: € 165.0 million).

## 21. Jouissance right capital

Jouissance right capital no longer existed after the planned repayment of the final jouissance rights as of the reporting date (2017: € 20.0 million).

## 22. Notes on the development of equity

Deutsche Hypo held subscribed capital of € 80.6 million on 31 December 2018, which is divided into 13,440,000 individual shares and is the same as in 2017.



### 23. Contingent liabilities and other obligations

in € thousands	31.12.2018	31.12.2017
Liabilities arising from sureties and guarantee agreements	462,220	502,232
of which total return swaps	134,346	155,457
of which sureties in the mortgage business	327,874	346,775
of which assets pledged as collateral	3,096	3,861

The risk of drawdowns of contingent liabilities is considered to be low, as the liabilities are managed with regard to credit and monitored. Provisions are created for the event of an imminent drawdown (see 4. Accounting and valuation principles).

Other obligations 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 exclusively include 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 without accrued interest, calculated using a calculation model (in most cases the discounted cash flow model) on the basis of observable market parameters (yields curves, forex rates, etc.). The book values (without pro-rata interest) are comprised of upfronts. The figures determined in this way are summarised in the following tables by product category.

31.12.2018						
in € millions	Nominal amount	Market value		Book value		Balance sheet item
		positive	negative	positive	negative	
Currency-related transactions	688	7	2	0	0	
Interest rate-related transactions	34,095	1,193	1,528	4	9	Assets 8; Liabilities 5
Interest rate- and currency-related transactions	2,202	128	184	0	3	Assets 8; Liabilities 5
<b>Total</b>	<b>36,985</b>	<b>1,329</b>	<b>1,714</b>	<b>4</b>	<b>11</b>	

31.12.2017						
in € millions	Nominal amount	Market value		Book value		Balance sheet item
		positive	negative	positive	negative	
Currency-related transactions	581	4	3	0	0	
Interest rate-related transactions	41,201	1,346	1,714	6	10	Assets 2 and 8; Liabilities 5
Interest rate- and currency-related transactions	2,007	126	188	2	4	Assets 8; Liabilities 5
<b>Total</b>	<b>43,789</b>	<b>1,476</b>	<b>1,905</b>	<b>8</b>	<b>14</b>	



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## Notes on the income statement

### 26. Other operating income

in € thousands	31.12.2018	31.12.2017
Income statement item	2,368	16,455
of which significant items:		
income from the release of provisions	917	930
reimbursement of expenses	770	87
interest rebates from taxes	391	15,057

### 27. Other operating expenses

in € thousands	31.12.2018	31.12.2017
Income statement item	9,770	12,217
of which significant items:		
expenses from the discounting of provisions*)	6,710	4,975
additions to provisions**)	2,602	5,020
losses from currency transactions	12	563
adjustments of surrender values from reinsurance policies	0	1,161

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

\*\*\*) The addition was made to due to legal uncertainty over existing credit contracts.

### 28. Extraordinary income

in € thousands	31.12.2018	31.12.2017
Income statement item	295	689
of which release of provisions in connection with the efficiency improvement programme	295	689

### 29. Außerordentliche Aufwendungen

in € thousands	31.12.2018	31.12.2017
Income statement item	16,832	14
of which additions to provisions due to cost-reduction programme*)	15,776	0
of which restructuring expenses**)	978	0
of which additions to provisions due to efficiency improvement programme	78	14

\*) These are additions to restructuring provisions for resolved future measures in relation to a cost-reduction programme geared towards cutting personnel and other administrative expenses.

\*\*\*) These are expenses relating to a cost-reduction programme in relation to a cost-reduction programme geared towards cutting personnel and other administrative expenses that were already incurred in the previous year.

## 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 of the Pfandbriefe in circulation and the fixed-interest period of the cover pool (Section 28 (1) of the PfandBG):

#### Mortgage Pfandbriefe:

in € millions	Nominal		Net present value		Risk net present value *)	
	31.12.2018	31.12.2017	31.12.2018	31.12.2017	31.12.2018	31.12.2017
Mortgage Pfandbriefe	8,095	8,376	8,279	8,570	7,919	8,260
of which derivatives	–	–	1	2	–3	4
Cover pool	9,010	9,369	9,796	10,342	9,280	9,752
of which derivatives	–	–	15	22	18	25
Excess cover	915	993	1,517	1,772	1,362	1,492

\*) For the calculation of the risk net present value, the dynamic approach in accordance with Section 5 (1) clause 2 of the PfandBarwertV is used.

in € millions	31.12.2018		31.12.2017	
	Pfandbriefe in circulation	Cover pool	Pfandbriefe in circulation	Cover pool
up to 0.5 years	176	629	875	700
more than 0.5 years up to 1 year	1,415	646	1,108	550
more than 1 year up to 1.5 years	505	329	175	497
more than 1.5 years up to 2 years	25	636	1,415	518
more than 2 years up to 3 years	971	1,158	530	1,178
more than 3 years up to 4 years	880	1,074	578	1,079
more than 4 years up to 5 years	1,308	842	630	1,024
more than 5 years up to 10 years	2,481	3,169	2,710	3,192
more than 10 years	335	528	355	631
<b>Total</b>	<b>8,095</b>	<b>9,010</b>	<b>8,376</b>	<b>9,369</b>

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### Public Pfandbriefe:

in € millions	Nominal		Net present value		Risk net present value *)	
	31.12.2018	31.12.2017	31.12.2018	31.12.2017	31.12.2018	31.12.2017
Public Pfandbriefe	3,719	4,389	4,696	5,518	4,429	5,185
of which derivatives	–	–	–	2	–	0
Cover pool	3,958	5,075	5,112	6,214	4,663	5,711
of which derivatives	–	–	1	5	9	13
Excess cover	239	686	416	696	234	526

\*) For the calculation of the risk net present value, the dynamic approach in accordance with Section 5 (1) clause 2 of the PfandBarwertV is used.

in € millions	31.12.2018		31.12.2017	
	Pfandbriefe in circulation	Cover pool	Pfandbriefe in circulation	Cover pool
up to 0.5 years	214	510	412	794
more than 0.5 years up to 1 year	177	259	108	273
more than 1 year up to 1.5 years	111	259	214	383
more than 1.5 years up to 2 years	189	8	177	133
more than 2 years up to 3 years	256	53	329	312
more than 3 years up to 4 years	300	120	255	120
more than 4 years up to 5 years	292	314	300	322
more than 5 years up to 10 years	1,164	1,145	1,384	1,401
more than 10 years	1,016	1,290	1,210	1,337
<b>Total</b>	<b>3,719</b>	<b>3,958</b>	<b>4,389</b>	<b>5,075</b>

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 (each as of 31.12)	Germany		Belgium		EU		France	
	2018	2017	2018	2017	2018	2017	2018	2017
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	–	–	–	–	23	246	–	–
of which: uncovered debt securities in terms of Art. 129 of Regulation (EU) 575/2013	–	–	–	–	23	246	–	–
Claims in terms of Section 19 (1) clause 3 of the PfandBG	366	408	–	75	–	–	–	22
<b>Total</b>	<b>366</b>	<b>408</b>	<b>–</b>	<b>75</b>	<b>23</b>	<b>246</b>	<b>–</b>	<b>22</b>

in € millions (each as of 31.12)	Italy		Japan		Canada		Luxembourg	
	2018	2017	2018	2017	2018	2017	2018	2017
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	69	119	–	–	–	–	–	40
of which: uncovered debt securities in terms of Art. 129 of Regulation (EU) 575/2013	69	119	–	–	–	–	–	40
Claims in terms of Section 19 (1) clause 3 of the PfandBG	–	3	149	149	41	–	–	–
<b>Total</b>	<b>69</b>	<b>121</b>	<b>149</b>	<b>149</b>	<b>41</b>	<b>–</b>	<b>–</b>	<b>40</b>

in € millions (each as of 31.12)	Netherlands		Austria		Sweden		Spain		Total	
	2018	2017	2018	2017	2018	2017	2018	2017	2018	2017
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	–	–	–	25	–	–	–	–	91	429
of which: uncovered debt securities in terms of Art. 129 of Regulation (EU) 575/2013	–	–	–	25	–	–	–	–	91	429
Claims in terms of Section 19 (1) clause 3 of the PfandBG	–	25	–	–	25	–	–	8	581	689
<b>Total</b>	<b>–</b>	<b>25</b>	<b>–</b>	<b>25</b>	<b>25</b>	<b>–</b>	<b>–</b>	<b>8</b>	<b>672</b>	<b>1,119</b>

**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 2018.

**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	31.12.2018	31.12.2017
up to and including € 0.3 million	14	15
more than € 0.3 million up to and including € 1 million	43	48
more than € 1 million up to and including € 10 million	1,189	1,436
more than € 10 million	7,092	6,751
<b>Total</b>	<b>8,338</b>	<b>8,250</b>

#### Breakdown of receivables by areas and types of use:

in € millions (each as of 31.12)	Germany		Belgium		France	
	2018	2017	2018	2017	2018	2017
<b>Residential</b>						
Apartments	3	5	–	–	0	0
Detached family homes	4	6	–	–	–	–
Multi-family homes	466	432	–	–	105	133
New buildings, not yet completed or not yet a source of income	38	6	–	–	–	–
<b>Total residential</b>	<b>511</b>	<b>448</b>	<b>–</b>	<b>–</b>	<b>105</b>	<b>133</b>
<b>Commercial</b>						
Office buildings	1,382	1,458	–	8	236	290
Commercial buildings	1,783	1,752	26	–	322	364
Industrial buildings	19	19	–	–	–	–
Other commercially used buildings	415	473	–	–	–	–
New buildings, not yet completed or not yet a source of income	250	264	–	–	54	54
Building sizes	26	7	–	–	–	–
<b>Total commercial</b>	<b>3,875</b>	<b>3,973</b>	<b>26</b>	<b>8</b>	<b>612</b>	<b>707</b>
<b>Total value of cover</b>	<b>4,386</b>	<b>4,420</b>	<b>26</b>	<b>8</b>	<b>718</b>	<b>841</b>



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in € millions (each as of 31.12)	UK		Ireland		Luxembourg	
	2018	2017	2018	2017	2018	2017
<b>Residential</b>						
Apartments	–	–	–	–	–	–
Detached family homes	–	–	–	–	–	–
Multi-family homes	58	59	–	–	–	–
New buildings, not yet completed or not yet a source of income	26	–	–	–	–	–
<b>Total residential</b>	<b>83</b>	<b>59</b>	<b>–</b>	<b>–</b>	<b>–</b>	<b>–</b>
<b>Commercial</b>						
Office buildings	477	432	83	83	13	–
Commercial buildings	424	411	34	18	–	–
Industrial buildings	–	–	–	–	–	–
Other commercially used buildings	11	20	–	–	–	–
New buildings, not yet completed or not yet a source of income	16	48	–	–	–	–
Building sizes	–	–	–	–	–	–
<b>Total commercial</b>	<b>927</b>	<b>911</b>	<b>117</b>	<b>101</b>	<b>13</b>	<b>–</b>
<b>Total value of cover</b>	<b>1,010</b>	<b>969</b>	<b>117</b>	<b>101</b>	<b>13</b>	<b>0</b>

in € millions (each as of 31.12)	Netherlands		Austria		Poland	
	2018	2017	2018	2017	2018	2017
<b>Residential</b>						
Apartments	–	16	–	–	–	–
Detached family homes	79	58	–	–	–	–
Multi-family homes	888	724	–	–	–	–
New buildings, not yet completed or not yet a source of income	16	29	–	–	–	–
<b>Total residential</b>	<b>983</b>	<b>827</b>	<b>–</b>	<b>–</b>	<b>–</b>	<b>–</b>
<b>Commercial</b>						
Office buildings	130	172	85	86	189	152
Commercial buildings	208	274	10	10	100	39
Industrial buildings	–	–	–	–	–	–
Other commercially used buildings	157	159	–	–	23	23
New buildings, not yet completed or not yet a source of income	8	4	–	–	–	–
Building sizes	–	–	–	–	–	–
<b>Total commercial</b>	<b>501</b>	<b>608</b>	<b>95</b>	<b>95</b>	<b>311</b>	<b>213</b>
<b>Total value of cover</b>	<b>1,485</b>	<b>1,435</b>	<b>95</b>	<b>95</b>	<b>311</b>	<b>213</b>

in € millions (each as of 31.12)	Spain		USA		Total – all countries	
	2018	2017	2018	2017	2018	2017
<b>Residential</b>						
Apartments	–	–	–	–	4	21
Detached family homes	–	–	–	–	83	64
Multi-family homes	–	–	–	–	1,517	1,347
New buildings, not yet completed or not yet a source of income	–	–	–	–	79	35
<b>Total residential</b>	–	–	–	–	1,683	1,467
<b>Commercial</b>						
Office buildings	–	–	100	95	2,693	2,775
Commercial buildings	46	49	24	13	2,976	2,929
Industrial buildings	–	–	–	–	19	19
Other commercially used buildings	9	10	–	–	614	684
New buildings, not yet completed or not yet a source of income	–	–	–	–	327	369
Building sizes	–	–	–	–	26	7
<b>Total commercial</b>	55	59	124	109	6,655	6,783
<b>Total value of cover</b>	55	59	124	109	8,338	8,250

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

in € millions	31.12.2018		31.12.2017	
	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	–	–	0.5	0.3
<b>Total</b>	–	–	0.5	0.3

**Foreclosure / sequestration** (Section 28 (2) clause 4 of the PfandBG):

in € millions	As of 31 December					
	Foreclosures pending		Sequestration pending		Foreclosures executed	
	2018	2017	2018	2017	2018	2017
Properties used for residential purposes	–	1	–	1	1	–
Properties used for commercial purposes	–	–	–	–	–	1
<b>Total</b>	–	1	–	1	1	1

In financial year 2018, 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	31.12.2018	31.12.2017
Properties used for residential purposes	–	–
Properties used for commercial purposes	–	0.9
<b>Total</b>	<b>–</b>	<b>0.9</b>

#### Disclosures in connection with receivables used as cover for public Pfandbriefe (Section 28 (3) clause 1 of the PfandBG):

in € millions as of 31.12	Germany		Belgium		EU		Finland	
	2018	2017	2018	2017	2018	2017	2018	2017
Central state	–	–	–	–	6	53	–	–
Regional authority	1,662	1,911	125	50	–	–	10	11
Local authority	35	36	–	–	–	–	–	–
Other	572	884	125	140	151	199	–	–
<b>Total</b>	<b>2,269</b>	<b>2,832</b>	<b>250</b>	<b>190</b>	<b>157</b>	<b>252</b>	<b>10</b>	<b>11</b>

in € millions as of 31.12	France		UK		Italy		Japan	
	2018	2017	2018	2017	2018	2017	2018	2017
Central state	11	–	55	–	260	196	–	–
Regional authority	22	–	–	–	50	53	10	10
Local authority	–	–	–	–	–	–	–	–
Other	1	23	–	56	–	–	–	–
<b>Total</b>	<b>34</b>	<b>23</b>	<b>55</b>	<b>56</b>	<b>310</b>	<b>249</b>	<b>10</b>	<b>10</b>

in € millions as of 31.12	Canada		Latvia		Luxembourg		Netherlands	
	2018	2017	2018	2017	2018	2017	2018	2017
Central state	–	–	–	–	40	–	–	–
Regional authority	119	123	13	14	–	–	–	130
Local authority	–	–	–	–	–	–	–	–
Other	–	53	–	–	–	–	–	290
<b>Total</b>	<b>119</b>	<b>176</b>	<b>13</b>	<b>14</b>	<b>40</b>	<b>0</b>	<b>0</b>	<b>420</b>

in € millions as of 31.12	Austria		Poland		Sweden		Switzerland	
	2018	2017	2018	2017	2018	2017	2018	2017
Central state	463	456	32	107	–	–	–	–
Regional authority	10	39	–	–	8	16	67	64
Local authority	–	–	–	–	–	–	–	–
Other	–	–	–	–	–	–	–	–
<b>Total</b>	<b>474</b>	<b>495</b>	<b>32</b>	<b>107</b>	<b>8</b>	<b>16</b>	<b>67</b>	<b>64</b>

in € millions as of 31.12	Spain		USA		Total	
	2018	2017	2018	2017	2018	2017
Central state	–	–	–	–	867	812
Regional authority	16	50	95	93	2,208	2,565
Local authority	–	–	–	–	35	36
Other	–	16	–	–	848	1,662
<b>Total</b>	<b>16</b>	<b>66</b>	<b>95</b>	<b>93</b>	<b>3,958</b>	<b>5,075</b>

As of 31 December 2018, there were no payments overdue by at least 90 days which were owed by public authorities.

**Breakdown by size groups:**

in € millions	31.12.2018	31.12.2017
up to and including € 10 million	265	362
more than € 10 million up to and including € 100 million	3,542	4,574
more than € 100 million	150	139
<b>Total</b>	<b>3,958</b>	<b>5,075</b>

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

		31.12.2018	31.12.2017
<b>Pfandbriefe in circulation</b>	in € millions	8,095	8,376
of which share of fixed-rate Pfandbriefe (Section 28 (1) clause 9 of the PfandBG)	%	93.97	96.51
<b>Cover pool</b>	in € millions	9,010	9,369
of which total amount of claims that exceed 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 28 (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)	%	74.54	69.33
Net cash value in accordance with Section 6 of the PfandBarwertV for each foreign currency (in € millions)	AUD	–	–
	CAD	–	–
	CHF	18.4	18.2
	GBP	494.1	784.2
Section 28 (1) clause 10 of the PfandBG (net of assets and liabilities)	JPY	–	–
	SEK	–	–
	USD	100.0	97.0
Volume-weighted average of age of claims (past term since credit award seasoning (Section 28 (1) clause 11 of the PfandBG)	years	4.5	4.2
Average weighted loan-to-value ratio (Section 28 (2) clause 3 of the PfandBG)	%	58.46	57.87
Average weighted loan-to-value ratio on a market basis	%	40.47	41.26



Balance sheet as of 31 December 2018 | Income statement for the period from 1 January to 31 December 2018 | Statement of changes in equity | Cash flow statement | Notes

### Public Pfandbriefe:

		31.12.2018	31.12.2017
<b>Pfandbriefe in circulation</b>	in € millions	3,719	4,389
of which share of fixed-rate Pfandbriefe (Section 28 (1) clause 9 of the PfandBG)	%	88.95	90.56
<b>Cover pool</b>	in € millions	3,958	5,075
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 28 (1) clause 9 of the PfandBG)	%	82.62	82.26
	AUD	–	–
Net cash value in accordance with Section 6 of the PfandBarwertV for each foreign currency (in € millions)	CAD	38.7	65.9
	CHF	77.7	80.3
	GBP	113.3	117.3
Section 28 (1) clause 10 of the PfandBG (net of assets and liabilities)	JPY	– 46.8	– 45.9
	SEK	–	7.4
	USD	173.9	289.4

### 32. Cover for bonds in circulation

in € millions	Mortgage Pfandbriefe		Public Pfandbriefe	
	31.12.2018	31.12.2017	31.12.2018	31.12.2017
<b>Ordinary cover</b>				
Receivables from financial institutions				
Public sector loans	–	–	290	474
Receivables from customers				
Mortgage loans	8,338	8,250	–	–
Public sector loans	–	–	2,550	3,470
Bonds of public sector issuers	–	–	1,118	1,131
	<b>8,338</b>	<b>8,250</b>	<b>3,958</b>	<b>5,075</b>
<b>Substitute cover</b>				
Other receivables from financial institutions	224	437	–	–
Bonds and other fixed interest securities	448	681	–	–
	<b>672</b>	<b>1,119</b>	<b>–</b>	<b>–</b>
<b>Total value of cover</b>	<b>9,010</b>	<b>9,369</b>	<b>3,958</b>	<b>5,075</b>
<b>Total amount in circulation requirement cover</b>	<b>8,095</b>	<b>8,376</b>	<b>3,719</b>	<b>4,389</b>
<b>Surplus cover</b>	<b>915</b>	<b>993</b>	<b>239</b>	<b>686</b>

### 33. Members of the Board of Managing Directors

**ANDREAS POHL**

(until 28 February 2018)

– Chairman of the Board of Managing Directors (until 28 February 2018) –

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**SABINE BARTHAUER****ANDREAS REHFUS**

### 34. Members of the Supervisory Board

**THOMAS S. BÜRKLE**

Chairman of the Board of Managing Directors of NORD/LB

– Chairman of the Supervisory Board –

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**GÜNTER TALLNER**

Member of the Board of Managing Directors of NORD/LB

– Vice Chairman of the Supervisory Board –

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**CHRISTOPH DIENG**

Member of the Board of Managing Directors of NORD/LB

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**THOMAS KRÜGER**

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

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**DIRK METZNER**

Bank employee, Deutsche Hypo

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**ANDREA BEHRE**

Bank employee, Deutsche Hypo



Balance sheet as of 31 December 2018 | Income statement for the period from 1 January to 31 December 2018 | Statement of changes in equity | Cash flow statement | Notes

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

in € thousands	2018	2017
<b>Total emoluments</b>		
Board of Managing Directors	912	1,269
Former members of the Board of Managing Directors and their surviving dependants	1,332	1,173
Supervisory Board	120	120

in € thousands	2018	2017
<b>Provisions for pension obligations owed to former members of the Board of Managing Directors and their surviving dependants</b>		
of which in reserves	16,501	11,993
	16,501	11,993

### 36. Size of workforce on average over the year

	2018	2017
Female employees	190	182
Male employees	240	232
<b>Total</b>	<b>430</b>	<b>414</b>

### 37. Auditor's fees

KPMG AG Wirtschaftsprüfungsgesellschaft audited the annual financial statements of Deutsche Hypo. The audit included the audit and/or audit review of Group reporting packages as well as the audit review of the half-yearly financial report. Furthermore, a comfort letter was issued, confirmations were provided relating to the requirements of the Sparkassen-Finanzgruppe's institute-specific protection scheme and a quality-control check was performed on the efficiency review of Supervisory Board activities.

As in the previous year, the disclosures in accordance with Section 285 clause 17 of the HGB have not been made. Instead, reference has been made to the inclusion of the Bank in NORD/LB's consolidated financial statements. The auditor's fees incurred by Deutsche Hypo are taken into account in the corresponding disclosure in the consolidated financial statements.

Hanover, 2 April 2019

The Board of Managing Directors



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, 2 April 2019

The Board of Managing Directors



Barthauer



Rehfus





# INDEPENDENT AUDITOR'S REPORT

To Deutsche Hypothekenbank (Actien-Gesellschaft), Hannover

## Report on the Audit of the Annual Financial Statements and of the Management Report

### Opinions

We have audited the annual financial statements of Deutsche Hypothekenbank (Actien-Gesellschaft), Hannover, which comprise the balance sheet as at 31 December 2018, the statement of profit and loss, the statement of cash flows and the statement of changes in equity for the financial year from 1 January to 31 December 2018, and notes to the financial statements, including the recognition and measurement policies presented therein. In addition, we have audited the management report of the Company for the financial year from 1 January to 31 December 2018.

In our opinion, on the basis of the knowledge obtained in the audit,

- the accompanying annual financial statements comply, in all material respects, with the requirements of German commercial law applicable to business corporations and give a true and fair view of the assets, liabilities and financial position of the Company as at 31 December 2018 and of its financial performance for the financial year from 1 January to 31 December 2018 in compliance with German Legally Required Accounting Principles, and
- the accompanying management report as a whole provides an appropriate view of the Company's position. In all material respects, this management report is consistent with the annual financial statements, complies with German legal requirements and appropriately presents the opportunities and risks of future development.

Pursuant to Section 322 (3) sentence 1 HGB [Handelsgesetzbuch: German Commercial Code], we declare that our audit has not led to any reservations relating to the legal compliance of the annual financial statements and of the management report.

### Basis for the Opinions

We conducted our audit of the annual financial statements and of the management report in accordance with Section 317 HGB and the EU Audit Regulation No. 537/2014 (referred to subsequently as "EU Audit Regulation") and in compliance with German Generally Accepted Standards for Financial Statement Audits promulgated by the Institut der Wirtschaftsprüfer [Institute of Public Auditors in Germany] (IDW). Our responsibilities under those requirements and principles are further described in the "Auditor's Responsibilities for the Audit of the Annual Financial Statements and of the Management Report" section of our auditor's report. We are independent of the Company in accordance with the requirements of European law and German commercial and professional law, and we have fulfilled our other German professional responsibilities in accordance with these requirements. In addition, in accordance with Article 10 (2) point (f) of the EU Audit Regulation, we declare that we have not provided non-audit services prohibited under Article 5 (1) of the EU Audit Regulation. We believe that the evidence we have obtained is sufficient and appropriate to provide a basis for our opinions on the annual financial statements and on the management report.

### **Significant uncertainty in connection with the continuation of business activity**

We refer to the statements in section 4.1.2.4 of the management report “Dependencies of Deutsche Hypo on NORD/LB” and in section 4 of the notes “Statements on the continuation of business activity”, where the legal representatives set out that the assumption about the continuation of business activity (going concern) for accounting and valuation purposes and the survival of Deutsche Hypo is dependent on the survival of NORD/LB.

The survival of NORD/LB in turn faces significant uncertainty and is premised in particular on

- the intended capital strengthening measures at NORD/LB level being implemented, completed and approved by all relevant stakeholders, in particular the regional parliaments of Lower Saxony and Saxony-Anhalt as well as the Deutscher Sparkassen- und Giroverband e. V., enabling renewed compliance the capital ratios and buffers and thresholds required under regulatory law,
- banking regulation authorities, in particular the European Central Bank, the German Federal Institute for the Supervision of Financial Services and the Deutsche Bundesbank, tolerating a shortfall of the regulatory minimum capital quotas up to the point of the completion of the intended measures for capital strengthening at NORD/LB level,
- all official approvals required for implementation, in particular from the EU Commission and the relevant banking regulation authority, being granted and
- the realignment of the business model and the intended restructuring measures are implemented as planned.

If the intended capital strengthening measures at NORD/LB level are not performed as planned, the outcome may be the winding up of NORD/LB. This eventuality or a rating downgrade or other adverse developments may trigger significant outflows of short-term funds, fundamentally limiting the funding options for NORD/LB.

A successful implementation of the realignment of the NORD/LB business model also presupposes the requisite acceptance by the market participants and other relevant stakeholders.

A winding up of NORD/LB could result in a winding up or a sale of Deutsche Hypothekbank. Such a situation or a rating downgrade of NORD/LB or other adverse developments may fundamentally limit the funding options of Deutsche Hypo.

As set out in the statements in section 4.1.2.4 of the management report “Dependencies of Deutsche Hypo on NORD/LB” and in section 4 of the notes “Statements on the continuation of business activity”, this points to significant uncertainty that may cast substantial doubt on the Bank’s capability to continue its business activity and that represents an existential risk as defined in section 322 (2) sentence 3 German Commercial Code (HGB). Our audit opinions have not been modified in respect of this circumstance.



### **Further key Audit Matters in the Audit of the Annual Financial Statements**

Key audit matters are those matters that, in our professional judgment, were of most significance in our audit of the annual financial statements for the financial year from 1 January to 31 December 2018. These matters were addressed in the context of our audit of the annual financial statements as a whole, and in forming our opinion thereon, we do not provide a separate opinion on these matters.

### **Recognition and valuation of the restructuring reserves**

In terms of the accounting and valuation principles applied by Deutsche Hypothekenbank (Actien-Gesellschaft), we refer to the information in the notes, section "Accounting and valuation principles".

### **THE FINANCIAL STATEMENT RISK**

As at 31 December 2018, restructuring reserves totalling € 15.8 million were recognised in the annual financial statements of Deutsche Hypothekenbank (Actien-Gesellschaft).

In terms of restructuring measures, corresponding reserves should be created if the general and substantiating recognition criteria of the relevant provisions apply. The valuation of the substantial restructuring reserves depends largely on the assessments and assumptions made by the Bank's legal representatives, in particular in terms of the structure of the social plans, the settlement amounts, the costs of part-time early retirement contracts and the costs of granting leave to employees.

Risks to the annual financial statements come from an absence of the requirements for the recognition of the restructuring provisions or an improper valuation of these.

### **OUR AUDIT APPROACH**

In the first instance our audit assessed whether the recognition criteria for restructuring reserves were satisfied as at 31 December 2018. In this respect we assessed in particular whether a detailed, formal restructuring plan was in place and the key components of the restructuring measures had been communicated to the Works Council as the employees' representative body.

The legal representatives then explained to us the assumptions underlying the valuation of the restructuring reserves. We evaluated the level to which the assumptions were consistent with the detailed, formal restructuring plan. We also compared the assumptions with the restructuring measures implemented in the past and also critically evaluated contracts and agreements entered into as at the key date.

### **OUR OBSERVATIONS**

The assumptions underlying the determination of the restructuring reserves were properly selected and are consistent with the accounting principles applicable to the valuation of restructuring reserves.

### **Appropriateness of the loan loss provisions created for receivables from customers from commercial real estate finance**

We refer to the disclosures in the “Accounting and Measurement Principles” section in the notes for the accounting and measurement principles applied at Deutsche Hypothekbank (Actien-Gesellschaft).

#### **THE FINANCIAL STATEMENT RISK**

The Company recognises, among others, mortgage loans relating to commercial real estate finance, which is the focus of the Company's lending business, under receivables from customers. The determination of the amount of loan loss provisions for receivables from customers is discretionary.

To calculate loan loss provisions for commercial real estate finance, the Company must estimate its expected cash flows from interest and principal payments and from the realisation of collateral provided. The cash flows are estimated on the basis of the expected development of material assumptions and parameters that have an impact on value. These include, in particular, the future development of the respective real estate markets and especially rents from the financed properties as well as the expected recoverable collateral. These estimates are subject to a degree of uncertainty.

Inaccurate assumptions regarding the amount of the expected cash flows or the realisation of collateral provided can lead to receivables being incorrectly valued and counterparty default risks not being adequately taken into account. In view of this, it was particularly important for our audit that the assumptions regarding the above-mentioned evaluative parameters were made in accordance with the applicable accounting principles.

#### **OUR AUDIT APPROACH**

In terms of our risk assessment and the evaluation of error risks, we based our audit opinion on control-based audit procedures as well as substantive audit procedures.

Within the scope of the control-based audit procedures, we assessed the implementation and effectiveness of relevant controls installed by the Bank to ensure the appropriateness of the loan loss provisions for commercial real estate finance.

We examined, according to materiality and risk aspects, the appropriateness of the determined loan loss provisions for receivables from commercial real estate finance for consciously selected individual exposures. In this context, we especially reviewed the appropriate estimation of expected cash flows while taking into account the anticipated development of material assumptions and parameters that have an impact on value. This includes in particular assessing the appropriate reflection of the future development of the respective real estate markets and especially rents from the financed properties, as well as the expected recoverable collateral.

#### **OUR OBSERVATIONS**

The underlying assumptions for the calculation of the loan loss provisions for commercial real estate finance were properly selected and comply with the applicable accounting principles for measuring loan loss provisions.



### Other Information

Management is responsible for the other information. The other information comprises:

- the remaining parts of the annual report, with the exception of the audited annual financial statements and management report and our auditor's report,
- the Corporate Governance Report in accordance with No. 3.10 of the German Corporate Governance Code,
- the insurance in accordance with § 264 (2) sentence 3 HGB for the annual financial statements and the insurance in accordance with § 289 (1) sentence 5 HGB for the management report

Our opinions on the annual financial statements and on the management report do not cover the other information, and consequently we do not express an opinion or any other form of assurance conclusion thereon.

In connection with our audit, our responsibility is to read the other information and, in doing so, to consider whether the other information

- is materially inconsistent with the annual financial statements, with the management report or our knowledge obtained in the audit, or
- otherwise appears to be materially misstated.

### Responsibilities of Management and the Supervisory Board for the Annual Financial Statements and the Management Report

Management is responsible for the preparation of the annual financial statements that comply, in all material respects, with the requirements of German commercial law applicable to business corporations, and that the annual financial statements give a true and fair view of the assets, liabilities, financial position and financial performance of the Company in compliance with German Legally Required Accounting Principles. In addition, management is responsible for such internal control as they, in accordance with German Legally Required Accounting Principles, have determined necessary to enable the preparation of annual financial statements that are free from material misstatement, whether due to fraud or error.

In preparing the annual financial statements, management is responsible for assessing the Company's ability to continue as a going concern. They also have the responsibility for disclosing, as applicable, matters related to going concern. In addition, they are responsible for financial reporting based on the going concern basis of accounting, provided no actual or legal circumstances conflict therewith.

Furthermore, management is responsible for the preparation of the management report that as a whole provides an appropriate view of the Company's position and is, in all material respects, consistent with the annual financial statements, complies with German legal requirements, and appropriately presents the opportunities and risks of future development. In addition, management is responsible for such arrangements and measures (systems) as they have considered necessary to enable the preparation of a management report that is in accordance with the applicable German legal requirements, and to be able to provide sufficient appropriate evidence for the assertions in the management report.

The supervisory board is responsible for overseeing the Company's financial reporting process for the preparation of the annual financial statements and of the management report.

### **Auditor's Responsibilities for the Audit of the Annual Financial Statements and of the Management Report**

Our objectives are to obtain reasonable assurance about whether the annual financial statements as a whole are free from material misstatement, whether due to fraud or error, and whether the management report as a whole provides an appropriate view of the Company's position and, in all material respects, is consistent with the annual financial statements and the knowledge obtained in the audit, complies with the German legal requirements and appropriately presents the opportunities and risks of future development, as well as to issue an auditor's report that includes our opinions on the annual financial statements and on the management report.

Reasonable assurance is a high level of assurance, but is not a guarantee that an audit conducted in accordance with Section 317 HGB and the EU Audit Regulation and in compliance with German Generally Accepted Standards for Financial Statement Audits promulgated by the Institut der Wirtschaftsprüfer (IDW) will always detect a material misstatement. Misstatements can arise from fraud or error and are considered material if, individually or in the aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of these annual financial statements and this management report.

We exercise professional judgment and maintain professional scepticism throughout the audit. We also:

- Identify and assess the risks of material misstatement of the annual financial statements and of the management report, whether due to fraud or error, design and perform audit procedures responsive to those risks, and obtain audit evidence that is sufficient and appropriate to provide a basis for our opinions. The risk of not detecting a material misstatement resulting from fraud is higher than for one resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal controls.
- Obtain an understanding of internal control relevant to the audit of the annual financial statements and of arrangements and measures (systems) relevant to the audit of the management report in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of these systems.
- Evaluate the appropriateness of accounting policies used by management and the reasonableness of estimates made by management and related disclosures.
- Conclude on the appropriateness of management's use of the going concern basis of accounting and, based on the audit evidence obtained, whether a material uncertainty exists related to events or conditions that may cast significant doubt on the Company's ability to continue as a going concern. If we conclude that a material uncertainty exists, we are required to draw attention in the auditor's report to the related disclosures in the annual financial statements and in the management report or, if such disclosures are inadequate, to modify our respective opinions. Our conclusions are based on the audit evidence obtained up to the date of our auditor's report. However, future events or conditions may cause the Company to cease to be able to continue as a going concern.
- Evaluate the overall presentation, structure and content of the annual financial statements, including the disclosures, and whether the annual financial statements present the underlying transactions and events in a manner that the annual financial statements give a true and fair view of the assets, liabilities, financial position and financial performance of the Company in compliance with German Legally Required Accounting Principles.



- Evaluate the consistency of the management report with the annual financial statements, its conformity with [German] law, and the view of the Company's position it provides.
- Perform audit procedures on the prospective information presented by management in the management report. On the basis of sufficient appropriate audit evidence we evaluate, in particular, the significant assumptions used by management as a basis for the prospective information, and evaluate the proper derivation of the prospective information from these assumptions. We do not express a separate opinion on the prospective information and on the assumptions used as a basis. There is a substantial unavoidable risk that future events will differ materially from the prospective information.

We communicate with those charged with governance regarding, among other matters, the planned scope and timing of the audit and significant audit findings, including any significant deficiencies in internal control that we identify during our audit.

We also provide those charged with governance with a statement that we have complied with the relevant independence requirements, and communicate with them all relationships and other matters that may reasonably be thought to bear on our independence, and where applicable, the related safeguards.

From the matters communicated with those charged with governance, we determine those matters that were of most significance in the audit of the annual financial statements of the current period and are therefore the key audit matters. We describe these matters in our auditor's report unless law or regulation precludes public disclosure about the matter.

## Other Legal and Regulatory Requirements

### Further Information pursuant to Article 10 of the EU Audit Regulation

We were elected as auditor by the annual general meeting on 24 May 2018. We were engaged by the supervisory board on 10 July 2018. We have been the auditor of the Company without interruption since the financial year 2012.

We declare that the opinions expressed in this auditor's report are consistent with the additional report to the audit committee pursuant to Article 11 of the EU Audit Regulation (long-form audit report).

## German Public Auditor Responsible for the Engagement

The German Public Auditor responsible for the engagement is Rainer Thiede.

Hannover, 10 April 2019

KPMG AG  
Wirtschaftsprüfungsgesellschaft

Thiede  
[German Public Auditor]

Röwekamp  
[German Public Auditor]





## PERSONNEL REPORT

As a reliable, modern employer, the Deutsche Hypo pursues the goal of supporting and advancing the employees who work here. This involves offering them varied tasks as well as attractive social benefits. The employees hold the international yet collegiate working environment in high regard. In the reporting year, the fundamental challenge for the staff remained reconciling the ambitious triad of the Bank's fixed income goals, the necessary cost discipline and also the constantly increasing regulatory requirements day by day. In 2018 the Bank succeeded in doing so with ideas, impetus and active contributions for the further development of the organisation by the colleagues who work here.

The HR department supports the employees with ongoing optimisation of the framework conditions and the working environment. However, it regards itself not only as a service provider, but also a shaper and as such is the strategic partner of corporate management and the respective departments. The aim is to develop the common understanding so that the employees – including management – are not merely consumers of HR products, but that they also shape them as co-designers. HR work takes place day in, day out in every organisational unit. The communicated understanding of HR development is that each individual accepts responsibility for their own development and is supported and advanced by their line manager, who acts as a champion and mentor.

The HR function creates the framework of instruments, offers and products that are crucial for modern HR development. The Bank believes that this approach promotes employees' individual responsibility, enhances the role of each manager as an "on-site HR developer" and ultimately clears the way to the Bank's successful and future-proof development. After all, everything that Deutsche Hypo offers its customers emanates from the people who work here.

### Remuneration system

The remuneration system of Deutsche Hypo follows and supports the company's business and risk strategies. Its objectives are sustainability and continuity in order to promote responsible and risk-conscious behaviour on the part of employees and to ensure sustainable business success. The remuneration system is also designed to ensure appropriate staffing in qualitative and quantitative terms and – in line with the Group remuneration strategy – to improve the attractiveness as an employer.

Under the Remuneration Ordinance for Institutions (Institutsvergütungsverordnung), the Bank is classified as a significant institution, so a risk analysis has been carried out according to section 18 of the Remuneration Ordinance for Institutions (identification of the so-called 'risk taker'). It also had to comply with provisions of the Remuneration Ordinance for Institutions applicable to major institutions. In the reporting year in particular, the new requirements of the Remuneration Ordinance for Institutions which was amended in 2017 ("IVV 3.0") were fed into the remuneration system in the form of corresponding modifications.

Deutsche Hypo is bound to a collective bargaining agreement, so the collective bargaining agreements for the private banking sector and the 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. Non-tariff employees receive a fixed annual salary, in twelve equal parts. The variable salary is determined for all employees in a formalised and transparent process. Accordingly, the Remuneration Ordinance for Institutions requires the Group context to be adequately considered for financial year 2018. As far as the risk takers are concerned, the variable remuneration

is determined taking proper account of the individual profit contribution alongside the Bank's (and where relevant the Group's) overall success and the profit contribution of the organisational unit. The variable remuneration is limited to 100 % of the fixed remuneration.

### **Personnel development**

Personnel development at Deutsche Hypo in 2018 continued to reflect the embedding of the competence model introduced in 2016. The assessment criteria adjusted to the competence model were used for the first time for the reporting year. Additionally, the seminar programme was expanded further with a focus on the competences under the competence model.

A further focal point for personnel development in 2018 was the systematic qualification of specific target groups. The "basic program for real estate financing" and "qualification program for project management" development series launched in 2017 were continued in the reporting year and successfully concluded. At the conceptual level an approach to the advancement of high-potential employees was developed in 2018 that will be implemented for the first time in the annual reviews at the start of 2019. Additionally, a concept for promoting digital competence at the Bank as well as "new leadership" has been developed in conjunction with the various groups of people at the Bank who are involved with issues around digitalisation or agile working and will also be implemented in 2019.

In addition to training courses, seminars, and numerous development measures in day-to-day operations, part-time study plays a key role in personnel development at Deutsche Hypo. It is for this reason that the Bank supports employees who are studying specialised or bank-related subjects part time. In 2018, a total of 14 employees attended part-time professional training activities funded by the Bank, such as master's degree programmes or subject-specific advanced training.

In 2018 in Germany a total of three colleagues took up management positions for the first time or moved into a more senior leadership role. These people are qualified through the corresponding development programs of NORD/LB. Additionally, Deutsche Hypo supplemented these measures with need-focused further training and a seminar programme for all executives. In 2018 training courses were held for example on the introduction of the psychological risk assessment and health-related issues.

### **Encouraging/attracting the next generation**

In fiscal year 2018, Deutsche Hypo also provided training in the classic work of bank personnel. Additionally, this offering was enhanced with the international Bachelor of Arts (B.A.) and the Bachelor of Science (B.Sc.) courses of study, which are offered in cooperation with the Leibniz FH School of Business. The Bank had 14 trainees and work-study students in the reporting year. As a result of the modified joint training venture with the NORD/LB, the trainees who started their training in 2017 and 2018 form a uniform cooperation across the Group along with the NORD/LB trainees. Additionally, the joint training venture in the Group, trainees of NORD/LB have the opportunity to work in real estate banking at Deutsche Hypo in Hanover. Conversely, trainees from Deutsche Hypo had the opportunity to sit in on different departments at NORD/LB. Further, our trainees availed themselves of the Group's wide offering of examination preparations and seminars.



Deutsche Hypo also gives interested students the chance to complete internships at Deutsche Hypo, providing them with their first insight into the workings of a real estate and Pfandbrief bank. In the year under review, a total of 17 internships were offered.

Since 2017 Deutsche Hypo has also been involved in a close partnership with HAWK (Hochschule für angewandte Wissenschaft and Kunst Hildesheim/Holzminden/Göttingen), Faculty of Management, Social Work, Construction at the Holzminden site. The HAWK students all have strong expertise in real estate matters as a result of their specific course of study, creating optimum conditions for collaborations for dissertations or internships.

### **Work-life balance and social affairs**

2018 was marked by a reorientation of the work-life balance and the Bank's offerings focusing on health. The aim was to replace existing measures with offerings that benefit many more employees than before. This has resulted for example in a renegotiation of the company agreement to 'promote the combination of family and work'. Instead of the nursery places that only benefit very few employees, the new company agreement to 'promote the combination of family and private life' that takes effect on 1 February 2019 covers the emergency childcare offering "Fluxx" from the city and region of Hanover, a holiday childcare offering supported by the Bank for children of school age up to 12, and advice and mediation services on issues relating to private life such as children, caring for family members and looking for household help.

The result of digitalisation and increasing technological progress are changing opportunities and conditions in the work environment. Since 2013 the Bank has been offering a group of people defined in more detail in the corresponding works agreement the opportunity to do some of their work from home via alternating teleworking. Initial experience with this first step towards mobile working has been positive. Because technical progress has quickly picked up speed, it was decided to go one step further in the reporting year and to roll out mobile working to all employees from 2019 onwards. The aim is to increase individual flexibility and the compatibility of family and work.

Additionally, the Bank takes its employees' health very seriously. In the context of health promotion, for example, Deutsche Hypo provides a company counselling service, run by an external service provider. 2018 also saw the "Time out at lunchtime" initiative take place. Additionally, a health day focusing on "back fitness" was offered in September 2018. As planned, the psychological risk assessment was introduced across the board in 2018.

### Cooperation with the Works Council

Good solutions and answers to the various challenges can always be found through trust and constructive cooperation with the Works Council. We sincerely thank the social partner for this.

	31.12.2018	31.12.2017	31.12.2016
<b>Employees</b>	430	414	395
of which: male	240	232	221
of which: female	190	182	174
<b>Employee structure</b>			
Trainees*)	3	15	11
Average age	45.3	45.0	44.0
<b>Other</b>			
Illness rate (in %)	4.5	4.5	3.3
10-year service anniversary (number of employees)	23	10	13
25-year service anniversary (number of employees)	12	10	5
40-year service anniversary (number of employees)	2	0	1

\*) As a result of the modified joint training venture with NORD/LB, the trainees who started their training in 2017 and 2018 for a uniform cooperation across the Group along with the NORD/LB trainees and are therefore no longer included here.



# CORPORATE GOVERNANCE REPORT

The trust of our owners, customers, investors, business partners and employees are the primary factor in the sustained corporate success of Deutsche Hypo. For us earning this trust day by day is an ongoing task. We satisfy this task by jointly creating added value – in accordance with our corporate culture. Responsibility, reliability and transparent decisions determine how we act.

Deutsche Hypo is committed to the principles of good corporate governance. We acknowledge the goals and purposes of the German Corporate Governance Code, which contains recommendations and suggestions and is regularly reviewed by the government commission for Corporate Governance and amended as need be. The current version of the Code was published on 24 April 2017 in the official part of the German Federal Gazette and can also be accessed on the Deutsche Hypo website at <http://www.deutsche-hypo.de> – as can the wording of the current Deutsche Hypo Declaration of Conformity.

In 2018 the governmental commission left the Code unchanged compared to the previous year. However, on 6 November 2018 it published the draft of a fundamental revision of the German Corporate Governance Code. This aims to increase the relevance and acceptance of the Code among companies and investors – for instance by making the Code leaner, more structured and easier to read. The new version of the Code (for which the consultation phase ended on 31 January 2019) contains new recommendations about independence and the remuneration of the Board of Managing Directors and is intended to set standards for as many stakeholders as possible. The aim of the changes is to avoid an unmanageable tangle of the Code with its statutory legitimation and a wide range of guidelines. We expect that the new version of the Code will be published during the first half of 2019, after changes arising from the consultation have been taken account of.

## Composition of the Supervisory Board

Pursuant to the Corporate Governance Code, the Supervisory Board should set concrete goals in terms of its composition and devise a competence profile for Board as a whole. Currently a team made up of representatives from NORD/LB, NORD/LB Luxembourg Covered Bond Bank and Deutsche Hypo is working on a Group-wide implementation of the EBA guideline for assessing the suitability of the management body and the holders of key roles. It is expected to conclude in the first half of 2019. As a result, concrete objectives for the composition of the Supervisory Board as well as a competence profile will be defined for the Board.

At Deutsche Hypo, Thomas Krüger is an independent Supervisory Board member as defined in the Corporate Governance Code. In terms of the number of employer's representatives on the Supervisory Board, the proportion of independent Supervisory Board members is therefore 25 %. We consider this quota to be adequate.

## Transparency

Open communication and transparency are very important at Deutsche Hypo. Alongside the information on the Corporate Governance Code, we also provide our current annual reports and half-yearly reports on our website and provide information about publication deadlines as well as key company developments and news that is announced via press releases. The website also features capital market information such as risk reporting of the cover pools, ad hoc notifications and information pursuant to the transparency rules of section 28 German Pfandbrief Act.

**Risk culture**

The business philosophy of Deutsche Hypo has long been based on the triad of stable income, efficient structures and low risks. The Bank therefore operates a risk culture that is geared towards safeguarding commercial success and enterprise value in the long term. This forms the basis of the Bank's risk awareness, risk willingness and risk management strategies. Deutsche Hypo's conservative risk culture is reflected e.g. in business processes, guidelines and ethical and financing principles and is apparent day-to-day in the decisions of the Bank's management and employees.

**Compliance**

Deutsche Hypo has a tried-and-tested compliance management system that monitors developments in prevailing legal and regulatory conditions and initiates implementation measures where necessary. The purpose of this is to protect the Bank and its customers and thus strengthens customers' trust in Deutsche Hypo. The Bank has set up a central compliance function that safeguards compliance of legal and regulatory projects and supports other departments in performing their tasks in terms of compliance-relevant aspects. The compliance management systems are complemented by cross-departmental committees. The compliance function also performs regular prevention measures as well as adequacy and efficiency surveys and produces risk analyses.

To enhance existing contact options, Deutsche Hypo has implemented a whistle-blower system that can be used not only by employers, but also customers, business partners and other stakeholders. This includes the function of an external ombudsman whom the whistle-blower may approach confidentially if there are suspicious acts involving criminal deeds or illegal business processes.



# REPORT BY THE SUPERVISORY BOARD

The six-strong Supervisory Board of Deutsche Hypo and its committees performed the tasks required of them by law, under the Bank's articles of association and in accordance with the German Corporate Governance Code in 2018. During the past financial year, the Supervisory Board consistently advised, supervised and monitored the Board of Managing Directors and was notified by the Board of Managing Directors regularly, promptly and extensively about key developments at the Bank.

Regular information was also provided in the form of the risk reports prepared in accordance with the provisions of MaRisk and monthly reports on the Bank's performance and income situation. In addition, fundamental subjects such as adjustments to the business and risk strategy were discussed in detail with the Board of Managing Directors. For its part, the Board of Managing Directors provided continual reports about the Bank's situation, current business performance, the risk and liquidity situation and planning. The meetings also dealt extensively with measures relating to risk and liquidity management.

As in previous years, the Supervisory Board was involved in all material decisions. The Board passed resolutions on the transactions presented to it that require Supervisory Board approval under the law, the Bank's articles of association and the guidelines issued in that context. The corresponding draft resolutions are always presented to the Supervisory Board members sufficiently in advance so they can make a decision. If the adoption of resolutions was required between meetings, the appropriate resolutions were adopted by written circulation procedure.

The Members of the Board of Managing Directors cooperated closely with the Chair of the Supervisory Board over the whole year and notified him of all material developments in the Bank. In personal discussions they also discussed open questions and prepared the meetings of the Supervisory Board.

The Supervisory Board met four times in 2018. These dealt both with the aforementioned regular agenda items, and also the reports of the Board of Managing Directors about the activities on the real estate and capital markets as well as the intensive competition among the real estate financiers were discussed at length at the meetings. The Board also frequently discussed the current state of the NORD/LB Group's One Bank transformation project.

For reasons of efficiency, the Supervisory Board set up four committees that deal with subject specific matters and generally prepare the resolutions of the Supervisory Board. These are the Lending and Risk Committee, the Audit Committee, the Appointments Committee and the Remuneration Committee.

In 2018 the Lending and Risk Committee met four times. Alongside the risk reports, the committee discussed loans requiring approval and received reports from the Board of Managing Directors about trends on the Bank's target markets. Additionally, the committee dealt with a range of portfolio reports last year, with special focus on the UK portfolio due to the imminence of Brexit.

The Audit Committee met twice in the reporting year. The focus was on the discussion of the auditor's reports at the end of 2017 as well as the 2018 interim financial statements. At the same time, the committee was notified about the adequacy and effectiveness of the principles, methods and processes for compliance with the German Securities Trading Act (Wertpapierhandelsgesetz), the obligations relating to MaRisk compliance as well as the prevention of money laundering, the funding of terrorism and other criminal acts. Additionally, the Audit Committee dealt with the regular reports from Internal Audit as well as reports on the internal control system.

The Remuneration Committee met four times in 2018. In particular its focus was on looking at the remuneration systems of the employees and the Members of Board of Managing Directors. The committee also discussed the contents of the remuneration report and received regular updates from the Board of Managing Directors about the implementation status of IVV 3.0.

The Appointments Committee met twice during the reporting year. The meetings discussed both the results of the survey of the Supervisory Board conducted in 2018 with external support in terms of structure, size, composition and performance of management and Supervisory Board as well as the knowledge, capabilities and experience of all managers and Supervisory Board members. No recommendations for action arose from the survey. Second, the term of a Supervisory Board member was extended, and a decision was taken on the number of ordinary Members of the Board of Managing Directors following the departure of the previous Chairman of the Board of Managing Directors.

The members of the Supervisory Board were kept informed of the work and the topics dealt in the committees, partly through their own participation as guests at the meetings, and partly through the reports of the committee members in the Supervisory Board meetings. The Chairman of the Supervisory Board and the Chairmen of the committees also remained in contact between the meetings.

The following table provides information about the attendance of the Supervisory Board members at the meetings as a whole. Supervisory Board members who were unable to attend individual meetings gave notification of their absence specifying the reasons and submitted written votes for the respective meetings.

Supervisory Board member	Number of attendances / number of meetings (Supervisory Board and committees)
Thomas S. Bürkle (Chairman)	13 out of 16
Günter Tallner (Vice Chairman)	13 out of 16
Christoph Dieng	16 out of 16
Thomas Krüger	8 out of 10
Dirk Metzner (Employee's representative)	8 out of 8
Andrea Behre (Employee's representative)	4 out of 4





The auditor KPMG AG Wirtschaftsprüfungsgesellschaft, Hanover, elected by the Annual General Meeting and subsequently appointed by the Supervisory Board, audited the financial statements for the 2018 financial year 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 members of the Supervisory Board discussed the audit report extensively and approved the auditor's audit result. At its meeting of 16 April 2019, the Supervisory Board approved the management report and the annual financial statements as of 31 December 2018. The annual financial statements for 2018 are thereby approved.

The Supervisory Board thanks the employees of Deutsche Hypo for all their hard work during 2018. Deutsche Hypo was able to assert itself on the market in a difficult market environment and to achieve a good operating result.

Hanover, 16 April 2019

The Supervisory Board



Thomas S. Bürkle  
Chairman of the Supervisory Board

# CORPORATE BODIES

## Supervisory Board

### THOMAS S. BÜRKLE

Hanover

Chairman of the Board of Managing Directors of NORD/LB

– Chairman of the Supervisory Board –

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### GÜNTER TALLNER

Hanover

Member of the Board of Managing Directors of NORD/LB

– Vice chairman of the Supervisory Board –

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### CHRISTOPH DIENG

Hanover

Member of the Board of Managing Directors of NORD/LB

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### THOMAS KRÜGER

Hanover

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

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### DIRK METZNER

Hanover

Bank employee

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### ANDREA BEHRE

Hanover

Bank employee



## Committees of the Supervisory Board

### Lending and risk committee

CHRISTOPH DIENG

– Chairman –

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THOMAS S. BÜRKLE

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GÜNTER TALLNER

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THOMAS KRÜGER

– Substitute member –

### Audit committee

GÜNTER TALLNER

– Chairman –

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THOMAS S. BÜRKLE

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THOMAS KRÜGER

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CHRISTOPH DIENG

– Substitute member –

### Appointments committee

THOMAS S. BÜRKLE

– Chairman –

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CHRISTOPH DIENG

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GÜNTER TALLNER

### Remuneration committee

THOMAS S. BÜRKLE

– Chairman –

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CHRISTOPH DIENG

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GÜNTER TALLNER

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DIRK METZNER

## Board of Managing Directors

**ANDREAS POHL (UNTIL 28 FEBRUARY 2018)**

Hanover

– Chairman of the Board of Managing Directors (until 28 February 2018) –

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**SABINE BARTHAUER**

Hanover

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**ANDREAS REHFUS**

Hanover

## Public trustees

**ANDREAS WOLFF**

Ronnenberg

Lawyer

– Trustee –

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**DORIS VOGEL**

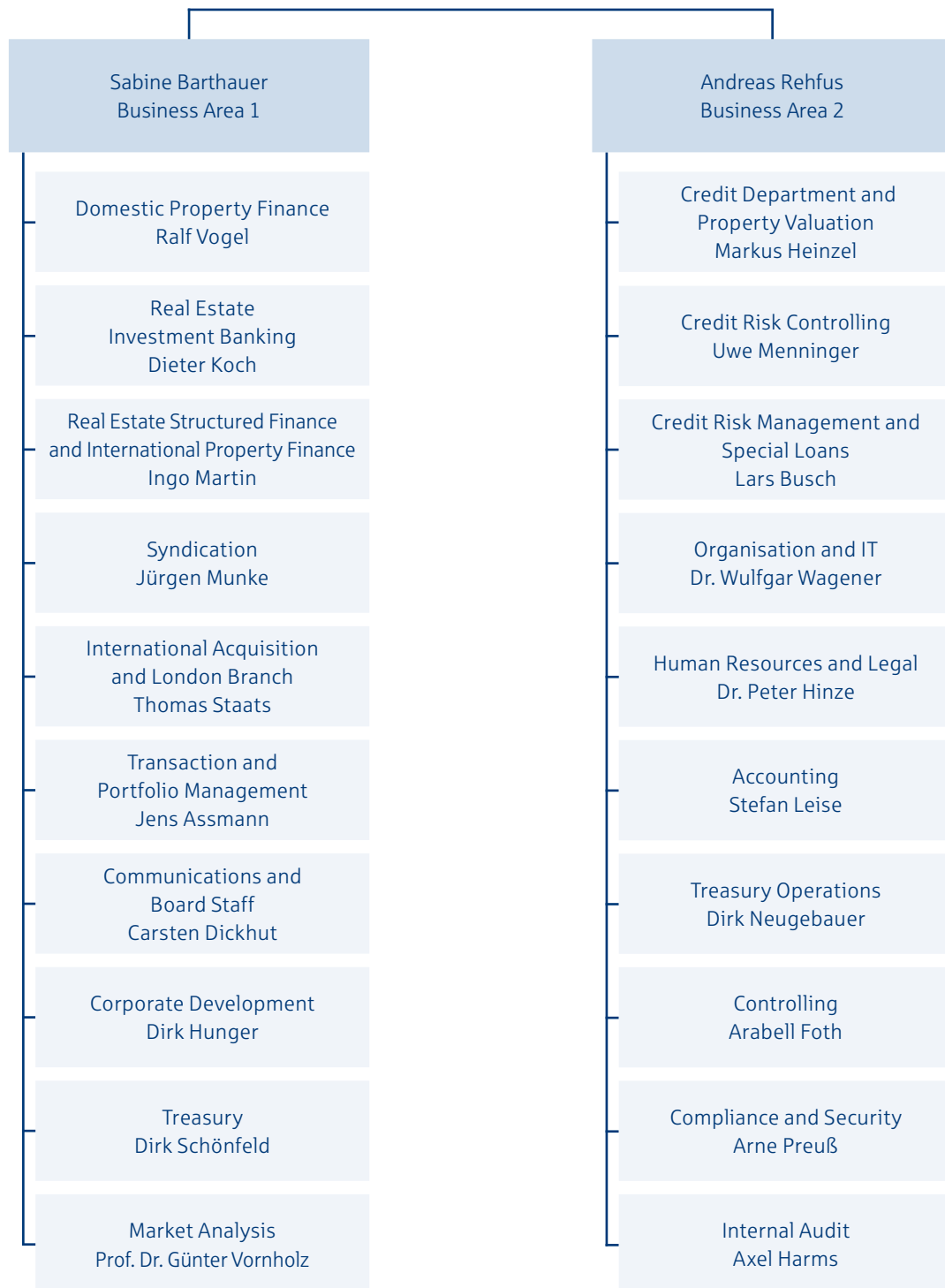
Hanover

Tax advisor

– Deputy trustee –



# ORGANISATIONAL STRUCTURE



# ADDRESSES IN GERMANY AND ABROAD

## Management

30159 Hannover

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Calle de Goya 6 · Telefon +34 91 0228414 · Telefax +34 91 4116183

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## Supervisory body

Europäische Zentralbank (EZB) · Sonnemannstraße 20 · 60314 Frankfurt am Main

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Bundesanstalt für Finanzdienstleistungsaufsicht · Graurheindorfer Straße 108 · 53117 Bonn





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(Actien-Gesellschaft)

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