Aareal Bank

Press release

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Aareal Bank Group posts a solid result for the third quarter

- **Consolidated operating profit of € 64 million for the third quarter (Q2 2019: € 61 million; Q3 2018: € 70 million)**
- **Net interest income stable at € 134 million, in spite of the extreme low interest rate environment – further increase in net commission income thanks to revenue growth at IT subsidiary Aareon**
- **Strong new business in the Structured Property Financing segment**
- **Higher loss allowance due to accelerated de-risking**
- **Annual guidance specified: consolidated operating profit expected at the lower end of the € 240 million to € 280 million communicated range**
- **Chairman of the Management Board, Hermann J. Merkens: "A key reason for Aareal Bank Group's robustness is our unique structure – with two successful segments that we purposefully develop in line with our strategy"**

Wiesbaden, 12 November 2019 – Aareal Bank Group continued with its positive business development in the third quarter of the current year. In what continues to be a challenging market and competitive environment, consolidated operating profit reached € 64 million after € 70 million in the third quarter of the previous year and € 61 million in each of the two previous quarters. Aareal Bank Group's consolidated operating profit for the first nine months of 2019 has therefore totalled € 186 million; taking the costs for integrating former Düsseldorfer Hypothekenbank (DHB) into account, the figure was roughly in line with the previous year (9m 2018: € 199 million). Consolidated net income allocated to ordinary shareholders of Aareal Bank amounted to € 35 million for the third quarter (Q3 2018: € 41 million), and € 107 million for the first nine months of the year (9m 2018: € 117 million). Earnings per share amounted to € 0.60 for the third quarter and € 1.80 for the first nine months (Q3 2018: € 0.70; 9m 2018: € 1.97).

At € 134 million in the third quarter (Q3 2018: € 131 million), net interest income remained stable on a level with the previous quarters, despite the extremely low interest rate environment. Third-quarter loss allowance was € 27 million, compared to € 23 million in the previous quarter, and € 14 million in the same quarter of the previous year. The higher figure is predominantly attributable to the announced acceleratedde-risking, which accounted for approximately € 20 million in the third quarter alone. Aareal Bank's motivations for this include the Bank's determination to reduce its portfolio of non-performing loans (NPLs) – especially in Italy – as announced. The NPL volume in the third quarter fell by around € 350 million, or around 20 per cent, compared to the preceding quarter.

Net commission income continued to develop favourably. At € 54 million in the third quarter, it exceeded the comparative figure for the previous year, as it had done in the first two quarters of this year. This once again reflects the positive performance of the IT subsidiary Aareon, which was able to increase its sales revenue considerably in the third quarter. Sales revenue in the traditional ERP business increased by 5 % year-on-year during the first nine months, while the business with digital products and solutions continued to prove very dynamic – as expected – with an increase of 21 %. Aareon also continued to consistently drive its strategic growth initiative forward in the quarter under review, with market entries in Switzerland and Austria, an extended range of offerings within the scope of the newly-developed, integrated “Aareon Smart Platform” and, as announced, commencement of the investment programme for tapping new digital growth opportunities.

CEO Hermann J. Merkens explained: “We are maintaining our very solid performance this year. Once again, we have demonstrated the robustness of our business in a challenging environment. A key reason for this is Aareal Bank Group’s unique structure, with two successful segments that we purposefully develop in line with our strategy. As an integral component of the Group, Aareon plays a significant role thanks to its excellent growth prospects and the cross-relationships with our banking business at numerous levels. Against this background, we continue to have no intention of selling a majority stake in our subsidiary, nor do we plan a full disposal – in line with the strategy we have pursued to date. Rather, we are concentrating instead on successfully implementing the growth programme for Aareon, which was presented in May, and – in our role as responsible owners – to use all sensible options to allow Aareon to realise its full potential in the interest of our shareholders.

Structured Property Financing segment: strong new business, margins remain above the full-year target

Aareal Bank continued to originate strong new business during the third quarter in its Structured Property Financing segment, whilst maintaining its conservative lending policy. The volume of new business reached € 2.8 billion and was thus significantly higher than in the same quarter of the previous year (Q3 2018: € 1.9 billion). The new business activities were focused on Europe. After nine months, new business totalled € 6.0 billion, in line with the previous year’s level (€ 6.1 billion). New business volume for the current year is expected at the upper end of the € 7 billion to € 8 billion communicated range.

Thanks to the strong new business, at € 28 billion the portfolio volume as at 30 September 2019 was at the upper end of the € 26 to € 28 billion range targeted for the year 2019 as a whole. At around 195 basis points, the average gross margin on newly-originated business (excluding currency effects) for the first nine months of the year continued to exceed the projected full-year range of 180 to 190 basis points.

Consulting/Services segment: Aareon continues to post significant growth in sales revenue

Operating profit in the Consulting/Services segment totalled € -10 million in the third quarter of 2019 (Q3 2018: € -7 million). Subsidiary Aareon's profit contribution was stable, at € 7 million (Q3 2018: € 7 million), despite the investment in growth. Its contribution for the first nine months was therefore € 24 million (9m 2018: € 21 million). Aareon’s sales revenue rose by 7 per cent to € 60 million in the third quarter (Q3 2018: € 56 million), and by 8 per cent to € 182 million in the first nine months of the year (9m 2018: € 168 million). Digital products recorded the highest growth rates this year so far, with a 21 per cent increase in sales over the same period of the previous year.

Averaging € 10.6 billion, the volume of deposits from the housing industry remained at a high level during the third quarter of 2019 (2018 average: € 10.4 billion). The persistently low interest rate environment continued to burden income generated from the deposit-taking business, and therefore the segment result. Nonetheless, the importance of this business goes way beyond the interest margin generated from deposits – which is under pressure in the current market environment. Deposits from the housing industry are a strategically important additional source of funding for Aareal Bank.

Comfortable funding situation and a solid capital base

Aareal Bank continued to be very well-funded during the third quarter of 2019, maintaining its long-term funding inventory at a comfortable level. No new Mortgage Pfandbrief issues or benchmark bonds were placed in the third quarter, as Aareal Bank had already taken advantage of the good market conditions in the first half-year, thereby largely meeting its funding requirements for the full year.

Aareal Bank continues to have a very solid capital base. As at 30 September 2019, the Bank's Common Equity Tier 1 (CET 1) ratio was 17.1 %, which is comfortable on an international level, and the Total Capital Ratio was 26.7 %. The CET1 ratio determined on the basis of the Basel Committee's final framework – the estimated so-called 'Basel IV' ratio, which is relevant for capital planning – was 12.6 %.

Notes to Group financial performance

Net interest income for the third quarter of 2019 was € 134 million (Q3 2018: € 131 million). It therefore totalled € 403 million (9m 2018: € 400 million) for the first nine months of the financial year.

Loss allowance amounted to € 27 million for the third quarter (Q3 2018: € 14 million) and € 55 million for the first nine months (9m 2018: € 33 million).

Net commission income increased over the same period of the previous year, to € 54 million (Q3 2018: € 51 million), driven once again by Aareon's strong performance. Net commission income totalled € 164 million for the first nine months of the financial year, a significant increase on the same period last year (9m 2018: € 152 million).

Net derecognition gain amounted to € 15 million for the third quarter (Q3 2018: € 5 million) and € 42 million for the first nine months of the year (9m 2018: € 16 million). In particular, this reflected adjustments to the Treasury portfolio (in connection with de-risking and the integration of DHB) as well as market-driven effects from early loan repayments.

The net gain or loss from financial instruments (fvpl) and from hedge accounting totalled € 2 million (Q3 2018: € 1 million). The net figure for the first nine months of the year was € 1 million (9m 2018: € -3 million), and resulted largely from the measurement changes of other derivatives (fvpl) used to hedge interest rate and currency risks.

Consolidated administrative expenses totalled € 114 million for the third quarter (Q3 2018: € 107 million) and € 370 million for the first nine months of the year (9m 2018: € 344 million). The increase – which was in line with expectations – was attributable in particular to the running costs and integration expenses incurred in conjunction with the integration of former Düsseldorfer Hypothekenbank, as well as to Aareon's business expansion.

Consolidated operating profit totalled € 64 million for the quarter under review (Q3 2018: € 70 million). Taking into consideration tax expenses of € 24 million and non-controlling interest income of € 1 million, consolidated net income attributable to shareholders of Aareal Bank AG amounted to € 39 million (Q3 2018: € 45 million). Assuming the pro-rata temporis accrual of net interest payable on the AT1 bond, consolidated net income allocated to ordinary shareholders amounted to € 35 million (Q3 2018: € 41million).

Aareal Bank Group's consolidated operating profit for the first nine months of the financial year totalled € 186 million (9m 2018: € 199 million). Taking tax deductions of € 65 million into account and after deducting € 2 million in non-controlling interest income, and assumed pro-rata net interest payable on the AT1 bond of € 12 million, consolidated net income allocated to ordinary shareholders of Aareal Bank AG amounted to € 107 million (9m 2018: € 117 million).

Group targets specified for the 2019 financial year

Following the solid performance overall in the first three quarters – and in spite of additional burdens from the extreme low interest rate environment – Aareal Bank Group continues to expect net interest income (excluding the net derecognition gain) in a range of € 530 million to € 560 million for the full year 2019. Aareal Bank has actively pursued the accelerated de-risking announced with the presentation of second-quarter results, recognising loss allowance of around € 30 million in this respect. Accordingly, the anticipated range for full-year loss allowance has been increased to between € 80 million and € 110 million. At the same time, Aareal Bank now expects a net derecognition gain of € 40 million to € 60 million, which is about € 20 million higher than the original estimate.

Net commission income, which continues to gain importance for the Group due to the strategic expansion of business in the Consulting/Services segment, is anticipated to rise further year-on-year, to between € 225 million and € 245 million. Administrative expenses – including Aareon's additional investments for accelerated growth, as well as costs for the integration of Düsseldorfer Hypothekenbank (DHB), which has now been concluded – are expected to range between € 470 million and € 510 million, in line with the previous guidance.

Despite the burdens from accelerated de-risking and further deterioration in the interest rate environment (which were not accounted for in the original guidance), Aareal Bank continues to anticipate consolidated operating profit for the current year in the communicated range between € 240 million and € 280 million, albeit at the lower end of this range. Accordingly, RoE before taxes and earnings per share (EpS) are likely to be at the lower end of the communicated ranges of 8.5% to 10% and of around € 2.40 to € 2.80. Opportunities for further accelerated de-risking will be assessed if they emerge, additional burdens cannot be excluded.

Overall, Aareal Bank Group's property financing portfolio in the Structured Financing Segment is expected to range in size between € 26 billion and € 28 billion, subject to exchange rate fluctuations. From today's perspective, the volume of new business is likely to be at the upper end of the € 7 billion to € 8 billion communicated range. Aareal Bank continues to expect its IT subsidiary Aareon to contribute approximately € 35 million to consolidated operating profit, taking strategic investments for accelerated growth into account. Excluding strategic investments, the contribution is anticipated at around € 41 million.

Note to editors: the Interim Financial Information as at 30 September 2019 is available at www.aareal-bank.com/financial-reports.

Aareal Bank Group
Aareal Bank Group, headquartered in Wiesbaden, is a leading international property specialist. It provides smart financings, software products, and digital solutions for the property sector and related industries, and is present across three continents: Europe, North America and Asia/Pacific. Aareal Bank AG, whose shares are included in Deutsche Börse's MDAX index, is the Group's parent entity. It manages the various entities organised in the Group's two business segments: Structured Property Financing and Consulting /Services. The Structured Property Financing segment encompasses all of Aareal Bank Group's property financing and funding activities. In this segment, the Bank facilitates property investment projects for its domestic and international clients, within the framework of a three-continent strategy covering Europe, North America and the Asia/Pacific region. In its Consulting/Services segment Aareal Bank Group offers its European clients from the property and energy sectors a unique combination of specialised banking services as well as innovative digital products and services, designed to help clients optimise and enhance the efficiency of their business processes.

Aareal Bank Group – Key Indicators

	1 Jan - 30 Sep 2019	1 Jan - 30 Sep 2018
Results		
Operating profit (€ mn)	186	199
Consolidated net income (€ mn)	121	131
Consolidated net income allocated to ordinary shareholders (€ mn) [1]	107	117
Cost/income ratio (%) [2]	42.2	41.8
Earnings per ordinary share (€) [1]	1.80	1.97
RoE before taxes (%) [1] [3]	8.7	9.7
RoE after taxes (%) [1] [3]	5.6	6.3

	30 Sep 2019	31 Dec 2018
Statement of Financial Position		
Property finance (€ mn) [4]	27,139	26,395
Equity (€ mn)	2,817	2,928
Total assets (€ mn)	43,155	42,687
Regulatory Indicators [5]		
Risk-weighted assets (€ mn)	12,656	13,039
Common Equity Tier 1 ratio (CET1 ratio) (%)	17.1	17.2
Tier 1 ratio (T1 ratio) (%)	19.5	19.5
Total capital ratio (TC ratio) (%)	26.7	26.2
Common Equity Tier 1 ratio (CET1 ratio) (%) – Basel IV (estimated) [6]	12.6	13.2
Employees	2,816	2,748

[1] The allocation of earnings is based on the assumption that net interest payable on the AT1 bond is recognised on an accrual basis.
[2] Structured Property Financing segment only
[3] On an annualised basis
[4] Excluding € 0.5 billion in private client business (31 December 2018: € 0.6 billion) and € 0.4 billion in local authority lending business by the former Westdeutsche ImmobilienBank AG (WestImmo) (31 December 2018: € 0.5 billion)
[5] When calculating own funds as at 30 September 2019, interim profits were taken into account, deducting the pro-rata dividend in line with the dividend policy, and incorporating the pro-rata accrual of net interest payable on the AT1 bond. Moreover, the expected relevant impact of the TRIM exercise on commercial property financings, and of the SREP recommendations concerning the NPL inventory as well as the ECB's NPL guidelines for exposures newly classified as NPLs, were taken into account for determining regulatory indicators.
[6] Underlying estimate, given a 72.5% output floor based on the final Basel Committee framework dated 7 December 2017. The calculation of the material impact upon Aareal Bank is subject to the outstanding EU implementation as well as the implementation of additional regulatory requirements (CRR II, EBA requirements etc.).

Consolidated income statement for the first nine months of 2019 (in accordance with IFRSs)

	1 Jan - 30 Sep 2019	1 Jan - 30 Sep 2018	Change
	€ mn	€ mn	%
Net interest income	403	400	1
Loss allowance	55	33	67
Net commission income	164	152	8
Net derecognition gain or loss	42	16	163
Net gain or loss from financial instruments (fvpl)	5	-1	-600
Net gain or loss from hedge accounting	-4	-2	100
Net gain or loss from investments in companies accounted for using the equity method	0	-	
Administrative expenses	370	344	8
Net other operating income/expenses	1	11	-91
Negative goodwill from acquisitions	-	-	
Operating profit	**186**	**199**	**-7**
Income taxes	65	68	-4
Consolidated net income	**121**	**131**	**-8**
Consolidated net income attributable to non-controlling interests	2	2	0
Consolidated net income attributable to shareholders of Aareal Bank AG	119	129	-8
Earnings per share (EpS)			
Consolidated net income attributable to shareholders of Aareal Bank AG [1]	119	129	-8
of which: allocated to ordinary shareholders	107	117	-9
of which: allocated to AT1 investors	12	12	
Earnings per ordinary share (in €) [2]	1.80	1.97	-9
Earnings per AT1 unit (in €) [3]	0.12	0.12	

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

[2] Earnings per ordinary share are determined by dividing the earnings allocated to ordinary shareholders of Aareal Bank AG by the weighted average of ordinary shares outstanding during the financial year (59,857,221 shares). Basic earnings per ordinary share correspond to (diluted) earnings per ordinary share.

[3] Earnings per AT1 unit (based on 100,000,000 AT1 units with a notional amount of € 3 each) are determined by dividing the earnings allocated to AT1 investors by the weighted average of AT1 units outstanding during the financial year. Earnings per AT1 unit (basic) correspond to (diluted) earnings per AT1 unit.

Consolidated income statement for the third quarter of 2019 (in accordance with IFRSs)

	Q3 2019	Q3 2018	Change
	€ mn	€ mn	%
Net interest income	134	131	2
Loss allowance	27	14	93
Net commission income	54	51	6
Net derecognition gain or loss	15	5	200
Net gain or loss from financial instruments (fvpl)	5	0	
Net gain or loss from hedge accounting	-3	1	-400
Net gain or loss from investments in companies accounted for using the equity method	0	-	
Administrative expenses	114	107	7
Net other operating income/expenses	0	3	-100
Negative goodwill from acquisitions	-	-	
Operating profit	**64**	**70**	**-9**
Income taxes	24	24	0
Consolidated net income	**40**	**46**	**-13**
Consolidated net income attributable to non-controlling interests	1	1	0
Consolidated net income attributable to shareholders of Aareal Bank AG	39	45	-13
Earnings per share (EpS)			
Consolidated net income attributable to shareholders of Aareal Bank AG [1]	39	45	-13
of which: allocated to ordinary shareholders	35	41	-15
of which: allocated to AT1 investors	4	4	
Earnings per ordinary share (in €) [2]	0.60	0.70	-14
Earnings per AT1 unit (in €) [3]	0.04	0.04	

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

[2] Earnings per ordinary share are determined by dividing the earnings allocated to ordinary shareholders of Aareal Bank AG by the weighted average of ordinary shares outstanding during the financial year (59,857,221 shares). Basic earnings per ordinary share correspond to (diluted) earnings per ordinary share.

[3] Earnings per AT1 unit (based on 100,000,000 AT1 units with a notional amount of € 3 each) are determined by dividing the earnings allocated to AT1 investors by the weighted average of AT1 units outstanding during the financial year. Earnings per AT1 unit (basic) correspond to (diluted) earnings per AT1 unit.

Segment results for the first nine months of 2019 (in accordance with IFRS)

€ mn	Structured Property Financing		Consulting/Services		Consolidation/Reconciliation		Aareal Bank Group	
	1 Jan-30 Sep 2019	1 Jan-30 Sep 2018	1 Jan-30 Sep 2019	1 Jan-30 Sep 2018	1 Jan-30 Sep 2019	1 Jan-30 Sep 2018	1 Jan-30 Sep 2019	1 Jan-30 Sep 2018
Net interest income[1)]	414	409	-11	-9	0	0	403	400
Loss allowance	55	33	0	0			55	33
Net commission income[1)]	6	6	163	150	-5	-4	164	152
Net derecognition gain or loss	42	16					42	16
Net gain or loss from financial instruments (fvpl)	5	-1					5	-1
Net gain or loss from hedge accounting	-4	-2					-4	-2
Net gain or loss from investments accounted for using the equity method			0				0	
Administrative expenses	195	182	180	166	-5	-4	370	344
Net other operating income/expenses	0	9	1	2	0	0	1	11
Negative goodwill from acquisitions								
Operating profit	**213**	**222**	**-27**	**-23**	**0**	**0**	**186**	**199**
Income taxes	74	77	-9	-9			65	68
Consolidated net income	**139**	**145**	**-18**	**-14**	**0**	**0**	**121**	**131**
Consolidated net income attributable to non-controlling interests	0	0	2	2			2	2
Consolidated net income attributable to shareholders of Aareal Bank AG	139	145	-20	-16	0	0	119	129
Allocated equity[2)]	2,131	2,045	205	177	225	263	2,561	2,485
Cost/income ratio (%)	42.2	41.8	117.4	115.3			60.5	59.7
RoE before taxes (%) [2) 3) 4)]	12.2	13.3	-18.5	-18.2			8.7	9.7

[1)] As of this reporting year, interest from housing industry deposits is shown in net interest income of the Consulting/Services segment (previously included in net commission income). The previous year's figures were adjusted accordingly.
[2)] Equity allocated to the Structured Property Financing segment for the same period of the previous year was adjusted to bring it into line with Basel IV; RoE before taxes was thus also changed accordingly.
[3)] On an annualised basis
[4)] The allocation of earnings is based on the assumption that net interest payable on the AT1 bond is recognised on an accrual basis.

Segment results for the third quarter of 2019 (in accordance with IFRSs)

€ mn	Structured Property Financing		Consulting/Services		Consolidation / Reconciliation		Aareal Bank Group	
	3rd quarter 2019	3rd quarter 2018	3rd quarter 2019	3rd quarter 2018	3rd quarter 2019	3rd quarter 2018	3rd quarter 2019	3rd quarter 2018
Net interest income[1]	138	134	-4	-3	0	0	134	131
Loss allowance	27	14	0	0			27	14
Net commission income[1]	2	2	54	51	-2	-2	54	51
Net derecognition gain or loss	15	5					15	5
Net gain or loss from financial instruments (fvpl)	5	0					5	0
Net gain or loss from hedge accounting	-3	1					-3	1
Net gain or loss from investments in companies accounted for using the equity method			0				0	
Administrative expenses	55	53	61	56	-2	-2	114	107
Net other operating income/expenses	-1	2	1	1	0	0	0	3
Negative goodwill from acquisitions								
Operating profit	**74**	**77**	**-10**	**-7**	**0**	**0**	**64**	**70**
Income taxes	27	27	-3	-3			24	24
Consolidated net income	**47**	**50**	**-7**	**-4**	**0**	**0**	**40**	**46**
Consolidated net income attributable to non-controlling interests	0	0	1	1			1	1
Consolidated net income attributable to shareholders of Aareal Bank AG	47	50	-8	-5	0	0	39	45

[1] As of this reporting year, interest from housing industry deposits is shown in net interest income of the Consulting/Services segment (previously included in net commission income). The previous year's figures were adjusted accordingly.