WE CREATE THE SPACE FOR SUCCESS

Aareal Bank Group – Interim Report
1 January to 30 June 2014

Aareal Bank Group

Key Indicators

	1 Jan-30 Jun 2014	1 Jan-30 Jun 2013
Income statement [1]		
Operating profit (€ mn)	282	92
Consolidated profit (€ mn)	221	43
Cost/income ratio (%) [2]	36.9	40.1
Earnings per share (€)	3.87	0.88
RoE before taxes (%) [3]	23.0	7.3
RoE after taxes (%) [3]	19.6	4.7

	30 Jun 2014	31 Dec 2013
Statement of financial position [4]		
Property finance (€ mn)	28,535	24,550
of which: international (€ mn)	21,609	20,802
Equity (€ mn)	2,653	2,450
Total assets (€ mn)	48,608	42,981
Regulatory indicators [4] [5]		
Risk-weighted assets (€ mn)	16,399	
Common equity tier 1 ratio (%) – fully phased – [6]	12.2	
Common equity tier 1 ratio (%)	14.3	
Tier 1 ratio (%)	16.3	
Total capital ratio (%)	22.4	
Employees [4]	2,532	2,375
Rating		
Fitch Ratings, London		
long-term [7]	A- (outlook: negative)	A- (outlook: stable)
short-term [7]	F1 (outlook: negative)	F1 (outlook: stable)
Fitch Pfandbrief ratings	AAA	AAA
oekom	prime	prime

[1] The disclosures covering the current period under review include negative goodwill from the acquisition of COREALCREDIT BANK AG ("Corealcredit") as at 31 March 2014. Corealcredit's operating results have been included in the Income Statement of Aareal Bank Group since the beginning of Q2 2014.

[2] Structured Property Financing segment only

[3] On an annualised basis

[4] Current period under review, including Corealcredit

[5] Since 1 January 2014, regulatory indicators have been determined in accordance with CRD IV/CRR, based on carrying amounts in accordance with IFRSs. Until 31 December 2013, these indicators were calculated in accordance with the German Solvency Regulation (SolvV) and based on local GAAP (book values in accordance with the German Commercial Code (HGB)). The Bank therefore decided against stating comparative amounts.

[6] Excluding silent participation from the German Financial Markets Stabilisation Fund (SoFFin)

[7] At the end of the first quarter of 2014, rating agency Fitch Ratings changed its outlook for the Long-Term Issuer Default Rating (IDR) of 18 banks within the European Union from "stable" to "negative". The corresponding outlook for an additional 18 European commercial banks remained "negative". This revision reflects a global re-assessment of government support for banks.

Contents

Letter from the Management Board

Dear Shareholders,
business associates and Aareal Bank staff,

Following a subdued start to the year, global economic development picked up speed during the second quarter of the 2014 financial year. The business environment for Aareal Bank – and for the banking sector as a whole – benefited from this slight economic tailwind. However, the ECB's persistent low interest rate policy presents a growing challenge.

As in the previous quarter, as well as in the previous months, the underlying economic momentum showed regional differences. Whilst economic output in the euro zone increased, also due to the continued recovery in the southern European economies, economic growth on the whole remained muted. The US economy, which at the start of the year suffered from an unusually hard winter, clearly picked up momentum during the second quarter. Catch-up effects were a key driver of this trend. Asian markets have continued their consolidation during the course of the year.

The European Central Bank further loosened its monetary policy, also against the background of continued low euro zone inflation. At the beginning of June, it lowered its key interest rate by another 10 basis points, to 0.15 per cent, setting a negative interest rate for deposits from commercial banks for the first time ever. Whether these decisions will indeed have the desired effect of adding further stimulus to the euro zone economy remains to be seen. In fact, it is unclear whether the ECB will be able to solve the euro zone's structural and economic problems – or if it is just buying time through monetary policy measures, which comprise targeted long-term repurchase operations (TLTRO) on top of interest rate cuts. The risk of bubbles building up on the back of ample market liquidity is set to increase, however.

Once again, the banking sector as a whole was the focus of numerous regulatory initiatives. The ECB's Comprehensive Assessment has been carrying particular weight: the initiative, which is designed to prepare for the assumption of regulatory responsibility by the ECB, comprises a regulatory risk assessment, an Asset Quality Review (AQR), and a stress test. Whilst participating banks have expressly welcomed these steps taken by the ECB, the scope and complexity of the Comprehensive Assessment present significant legal, reputational and stability risks for regulators and regulated institutions alike. For instance, the AQR results will not be communicated to the banks within a short period of time. Looking at the ECB's stress test in particular, this may lead to implausibilities or misconceptions. All banks directly supervised by the ECB – including Aareal Bank – are subject to the Comprehensive Assessment, which will last until the autumn of this year.

In this environment, Aareal Bank posted very good results for the second quarter of 2014. Aareal Bank Group's consolidated income statement for the second quarter included operating results from COREAL-CREDIT BANK AG ("Corealcredit") for the first time. These impact mainly on net interest income, and administrative expenses. Consolidated operating profit of € 65 million exceeded the figure for the same quarter of the previous year (€ 45 million). This increase was mainly attributable to the decidedly positive development of net interest income, driven both by the higher lending volume and by non-recurring effects from early loan repayments.

We are very pleased with the results for the second quarter. We consider these results as evidence that Aareal Bank is continuing to tread the successful path it has enjoyed during recent financial years – undeterred, as also seen with the successful closing of the Corealcredit acquisition at the end of the first quarter.

Aareal Bank Group's ongoing success is based on our strong market position, our robust business model, and our sustainable business policy. These factors have distinguished the Bank in the past, and will remain the guiding principle of our activities in the future – especially against the background of further intensified competition in international commercial property financing over recent months; this applied to the markets in most European countries as well as to North America and Asia. Investors continued to focus on first-class properties in top locations. At the same time, a shortage of supply combined with investors' growing risk appetite boosted demand outside metropolitan areas and top-tier properties.

At € 71 million, the operating profit achieved in the Structured Property Financing segment was significantly higher than the figure for the same quarter of the previous year (€ 50 million). New business of € 2.6 billion slightly exceeded the same quarter of the previous year. The share of newly-originated loans once again increased slightly year-on-year, remaining at a high level of 63.6 per cent. New business totalled € 4.2 billion in the first half of the year (H1 2013: € 4.4 billion).

At € 32 million, allowance for credit losses was up slightly year-on-year during the second quarter, and thus remained within the pro-rata forecast range of € 110 million to € 150 million for the full financial year. This was once again evidence of the high quality of our credit portfolio, also extended by Corealcredit.

As in the previous period, results in our Consulting/Services segment continued to be influenced by two key factors during the second quarter of the current financial year: the performance of our subsidiary Aareon AG, which remained on schedule, and the impact of historically low interest rate levels. For Aareon, the megatrend of digitisation continues to be the focus of its research and development activities. With this in mind, our IT subsidiary is continuously expanding its product range, and already enjoys an outstanding position from which to benefit from the digitisation of the housing industry.

On the other hand, the segment's banking business remained burdened by the historically low interest rate levels. At an average of € 8.5 billion during the quarter under review, the volume of customer deposits from the housing industry remained high. It is evidence of the strong level of trust which the Bank continues to enjoy as the long-standing lead bank to the German housing industry.

Following the ECB's decision with regard to interest rates, the interest rate environment will remain a challenge for segment results for a longer period of time. Nonetheless, to us there is no doubt that the importance of the deposit-taking business in the Consulting/Services segment goes far beyond the interest margin generated from the deposits – which is under pressure in the current market environment. For Aareal Bank, deposits from the housing industry are a strategically important additional source of funding for the property financing business, and one that is largely independent of developments on the capital markets. In addition to the German Pfandbrief and unsecured bank bonds, they represent an important pillar in the Bank's long-term funding mix. The deposit-taking business has been (and remains) a strategic competitive advantage, not least against the background of the current changes to the regulatory framework.

We once again successfully carried out our funding activities during the second quarter of 2014: we raised an aggregate of € 400 million in long-term funds, through various refinancing instruments, and thus continue to maintain our long-term funding at a very high level. At its council meeting on 5 June 2014, the ECB resolved various measures, including a deposit rate of -0.1 per cent – the first time it has imposed a negative rate. At the same time, the ECB suspended its weekly liquidity-absorbing operations, whereby banks were able to deposit one-week funds with the central bank, with effect from 18 June. In response, Aareal Bank started placing a part of its short-term excess liquidity via securities repurchase agreements.

As at 30 June 2014, the Bank's Tier 1 ratio was 16.3 per cent, which is comfortable on an international level. The Common Equity Tier 1 (CET 1) ratio was 14.3 per cent. Aareal Bank thus remains very solidly financed and already fully complies today with the capital requirements under Basel III.

Hence, our conclusion when looking at the second quarter of the 2014 financial year is once again decidedly positive. We held course in an increasingly competitive environment.

Looking ahead over the next months, we are confident that we will be able to maintain our successful performance. The performance of the developed economies is likely to further improve, also in Europe – although the turbulence in early July showed just how fragile the recovery of the markets continues to be. Uncertainty thus remains, with the global economy still susceptible to disruptions. Moreover, increased competition in the property financing business and especially the persistently low interest rate environment are challenges Aareal Bank Group must deal with. We slightly raise our earnings forecasts for the 2014 financial year: thanks to the good business development during the first two quarters of the year, we now believe there is a good chance to generate consolidated operating profit at the upper end of a range between € 380 million to € 400 million, including the negative goodwill from the acquisition of Corealcredit. Adjusted for this non-recurring effect, we anticipate consolidated operating profit between € 230 million and € 250 million.

We remain optimistic on a medium-term horizon, too: Aareal Bank is in excellent shape: solid and reliable. Our success is based on the expertise of our employees, as well as on the swift and streamlined decision-making processes within our mid-sized bank. Besides our viable business model, these are key factors with which we earn the trust of our clients – each and every day. We will not ease up on our efforts to continue doing business in a risk-aware manner, with a focus on profitability and geared toward sustainable success.

For the Management Board

Yours Sincerely, Wolf Schumacher

Dr Wolf Schumacher
Chairman

Group Management Report

Report on the Economic Position

Macro-economic environment

Economy

Although the global economy showed poor momentum at the beginning of the year, indicators suggest that expansion picked up somewhat in the second quarter, albeit with significant regional differences still in place.

The indicators suggest that economic output in the euro zone is likely to have increased further during the second quarter. However, fundamental momentum remained poor and growth muted, with the latter being burdened by the situation on the labour market. These trends were also apparent within most euro zone member states. The economy in the European countries outside the euro zone is also likely to have posted growth in the previous quarter. Economic growth is likely to have been relatively strong in the UK in particular.

In the US, the economy was noticeably burdened by the unusually harsh winter at the start of the year. However, it should have moved to a clear uptrend in the second quarter. Catch-up effects also played a role here.

The very high growth rates which China used to achieve in the past have not been reached anymore for quite some time now. This trend continued in the second quarter, although the growth rates picked up marginally compared with the first quarter. The growth rates remained high by international comparison. Value-added tax was raised from 5 % to 8 % in Japan as at 1 April 2014. While the economy had benefited from pre-emptive effects on expenditure in the first quarter, in order to avoid the higher tax burden, these effects impacted in particular on consumer spending in the second quarter and led to a considerable decline in real gross domestic product.

The trend towards stabilisation seen on the European labour markets in previous months remained intact. The average unemployment rate in the euro zone fell slightly. The unemployment rates were also stable to slightly lower at individual country level both in the euro zone and in other EU member states. Germany and Austria continued to post the lowest unemployment rates in the EU. In contrast, unemployment was high in France, Italy and Spain. In Spain, in particular, the trend towards a slight reduction in the unemployment rate in recent months could be sustained, however. At the start of the year, the improvement in employment in the US faltered on account of the harsh winter. The unemployment rate fell significantly in the second quarter, due to a rise in employment on the one hand and to a decline in the number of persons available to the labour market on the other. The unemployment rate fell slightly in Japan.

Financial and capital markets, monetary policy and inflation

The situation on the financial and capital markets of the developed economies eased further in the second quarter. The markets continued to afford numerous banks, companies and countries the opportunity to place securities at favourable terms.

Following considerable tension on the financial and capital markets of various emerging market economies at the start of the year, when international investors withdrew significant amounts of capital, this eased to a certain extent on these markets during the second quarter. Government bond yields, which fell noticeably in various countries, such as Turkey, were an indication of this.

Government bond yields of developed economies declined further – as was the case already in the first quarter. Yields fell to a somewhat greater extent in Italy and Spain than in euro member states such as Germany, which are seen as relatively stable by investors. The yield differentials between these countries therefore continued to tighten. It must be taken into account that the yields for the vast majority of euro zone countries have reached a very low level.

The support programme from the European Stability Mechanism (ESM) for Portugal expired in mid-May, without Portugal applying for a precautionary credit line instead. Portugal then successfully raised finance on the free financial and capital markets in the following month via long-term bonds – for the first time (since the beginning of the financial markets crisis) without the ESM's backing. At the end of the quarter (and also on subsequent days), concerns about the future of a major Portuguese commercial bank led to unrest on the country's financial and capital markets.

In June, the Eurogroup agreed on rules, according to which banks could be recapitalised directly via the ESM. However, this agreement was still subject to the approval within the scope of individual national proceedings. Accordingly, a system-relevant bank can receive direct recapitalisation if it is no longer in a position to meet the capital requirements (or this situation is likely to be imminent) and it is unable to raise the necessary funds from private sources or with the participation of its shareholders and creditors. Further requirements are that the state in question is unable to provide the bank with adequate support without threatening its own financial stability, and indirect recapitalisation via an ESM loan to the country is not possible. However, the country in question must participate in the support to a certain extent. The aggregate amount for the direct bank recapitalisation by the ESM was limited to €60 billion.

Long-term interest rates fell further during the second quarter in most of the important currencies in which Aareal Bank is active, in spite of their low levels. The pound sterling was an exception, with long-term interest rates remaining virtually unchanged. Short-term euro and Swedish krona interest rates fell slightly. They were largely constant on the other hand for the remaining currencies that are important for us.

The euro depreciated in the quarter under review vis-à-vis the pound sterling, the Japanese yen, the Canadian dollar and – to a minor extent – against the US dollar. The euro exchange rate appreciated against the Swedish krona. It changed only minimally relative to the Danish krone and the Swiss franc. However, certain links to the euro or foreign exchange rate caps are evident in the central banks' monetary policy.

The ECB eased its monetary policy further at the start of June. It justified it on the one hand with driving the current low rate of inflation closer to its target of just below 2 %, and on the other to support lending to companies. In the ECB's opinion, the weak performance of corporate lending activity in the euro zone is a reflection of delayed reaction to the economic cycle, the credit risk, and balance sheet adjustments by banks and companies. Besides lowering the key interest rate by 0.1 percentage points to 0.15 %, the measures include setting a negative interest rate for deposits from commercial banks (-0.1 %) for the first time ever. Furthermore, for commercial banks the ECB agreed to implement longer-term refinancing transactions that are linked to lending activities, to continue the refinancing operations as fixed-rate tenders with full allocation until at least the end of the maintenance period at the end of December 2016, as well as suspending the fine-tuning operations with which the ECB "sterilises" the liquidity provided within the scope of the programme for the securities markets.
The ECB also announced its intention to enhance preparatory work for outright purchases on the market for asset-backed securities.

The US Federal Reserve Bank (the Fed), on the other hand, continued to gradually step back from its very loose monetary policy by further reducing the volume of its monthly bond purchases in the second quarter. The vast majority of central banks left their key interest rates unchanged in the quarter under review. By contrast, the Turkish central bank cut its key interest rate twice in the second quarter by a total of 1.25 percentage points, having raised it drastically by 5.5 percentage points at the start of the year. The Russian central bank, on the other hand, raised its key interest rate by 0.5 percentage points in the second quarter. The sharp increase in residential property prices in the UK, especially London, is a cause for concern. For this reason, the Bank of England (BoE) announced a limit, whereby new mortgage loans extended may not reach a loan-to-income ratio that is equal to or greater than 4.5. This ratio may only be exceeded by a maximum 15 % of the new mortgage loans granted by a bank.

Inflationary developments meanwhile moved in different directions – even among the developed economies. Inflationary pressure in the euro zone was very low in the second quarter, with an annual average rate of 0.6 %. Some European countries like the Netherlands, Poland, Sweden and Spain featured inflation rates just above the zero percent mark. In the United States, however, the rate of inflation rose to around 2 %. Average annual inflation in Japan also recorded a marked increase to above 3 %, especially due to the increase in value-added tax in April. In contrast, the inflation rate in China was at a slightly lower, moderate level of above 2 %.

Regulatory environment

The emphasis in the banking sector remains on the numerous regulatory and reform measures. The focus remains in particular upon the extensive ECB Comprehensive Assessment, which includes a regulatory risk assessment, an asset quality review and a stress test. All banks which will come under direct ECB supervision began to implement the assessment before the responsibility for supervision will be transferred to the ECB; the assessment will run until autumn 2014.

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

Sector-specific and business developments

Structured Property Financing segment

New business in the second quarter of 2014 was € 2.6 billion, and thus slightly higher than in the same quarter of the previous year (Q2 2013: € 2.4 billion). The total volume of new business for the first half-year therefore amounted to € 4.2 billion (2013: € 4.4 billion). The slight decline in new business relative to the first half of 2013 is only due to loan extensions, which were lower than in the previous year. This is due to a lower volume of loans from the portfolio set for renewal.

The total volume of newly-originated loans – € 2.7 billion in the first half of 2014 – was thus slightly higher than the previous year's level of € 2.5 billion. This also applied to the second quarter, with newly-originated loans amounting to € 1.6 bn (€ 1.4 billion). The share of newly-originated loans for the entire first half-year of 2014 therefore amounted to 63.6 % (previous year: 57.0 %) and to 61.3 % (55.0 %) in the quarter under review.

At 78.9 %, we continued to achieve the highest share of new business in the first two quarters in Europe, followed by North America with 17.5 % and Asia with 3.6 %.[1)]

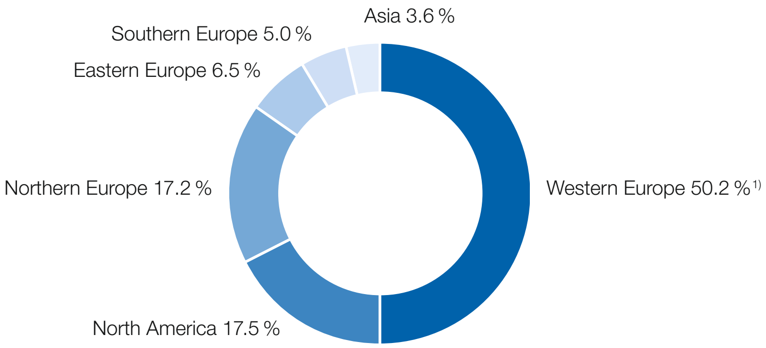
The volume of Aareal Bank Group's property financing portfolio stood at € 28.5 billion as at 30 June 2014, up by approximately 16 % since the end of the previous year. The increase is attributable to the acquisition of Corealcredit, amongst other things.

The commercial property financing business continued to be characterised by intense competition during the second quarter of 2014; this applied to the vast majority of European countries as well as to North America and various Asian markets.

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

New business 1 January - 30 June 2014

by region (%) Total volume: € 4.2 bn



[1)] including Germany

Competition in Southern European countries, such as Italy and Spain, has also increased in the course of the current year relative to the previous year. In some markets, lenders continued to show more willingness to accept higher loan-to-value ratios and lower margins.

Investor demand for commercial property remained high in the quarter under review, and global transaction volumes for commercial property increased significantly compared with the second quarter of 2013. Although demand remained particularly focused on premium properties in the big cities, limited supply and investors' growing readiness to assume risk has led to greater demand outside of the big cities or the prime segments. Investors have therefore been increasingly willing to buy properties in second-class locations or those that feature potential for creating value, e.g. in the course of modernisation measures. In view of the sustained robust demand, yields for newly acquired first-class commercial properties were stable or slightly lower than in the previous quarter.[2)] The rents for first-class commercial property were predominantly stable to slightly positive.

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

Europe

In the vast majority of the leading European economic centres, rents for first-class commercial properties remained stable compared with the previous quarter; this development applied to office, retail and logistics properties. There were only few markets showing an increase of corresponding rents. This was the case, for example, in the markets for high-quality office properties in London's West End and in Madrid, for first-class shopping centres in Istanbul – and also for high-quality logistics properties in Istanbul and Rotterdam. The rents for first-class commercial properties declined in only a few European economic centres, for example, on the office markets in Rome and Warsaw and the logistics markets in Milan and Rome.

The hotel markets in the big European cities presented a mixed picture during the second quarter. This was the case on the one hand between the different months of the quarter, which was influenced by the late Easter holiday, and to developments between the individual cities on the other. In different cities, including Hamburg, Copenhagen and London, but also in the big Italian and Spanish cities of Milan, Rome, Barcelona and Madrid, the average revenues per available hotel room increased compared with the corresponding period of the previous year. However, average revenues per available hotel room also fell in some cases, such as Helsinki and Paris.

Transaction volumes in commercial property rose significantly in the second quarter of 2014 over the corresponding period of the previous year. Investor interest in commercial property therefore remained high. In the European economic centres, robust investor demand compared with the previous quarter led to constant to slightly falling yields on newly acquired first-class commercial property. Yields rose only very sporadically in the economic centres for high-quality properties, e.g. on the office markets in The Hague and Rotterdam, as well as on the London logistics market.

In Europe, we generated new business in the amount of € 2.1 billion in the second quarter of 2014, and therefore € 3.3 billion in the first half of the year in total. Western European accounted for the highest share by far, followed by Northern Europe, Eastern Europe and Southern Europe.

North America (NAFTA states)

In the second quarter of 2014, the trend continued towards slightly higher rents on a national average in the US, compared with the previous quarter. This was evident on the office, retail and logistics property markets, and also applied to numerous markets in the leading economic hubs of the US. However, there were deviations in the form of sharp rent increases in, for example, the markets of the three different property types in New York and San Francisco. Rents were stable to marginally lower on the retail market in Chicago and on the office and retail property markets in Washington DC. Average vacancy ratios in the US fell noticeably compared with the previous quarter.

On the hotel market in the US, the average revenues per available hotel room rose compared with the corresponding quarter of the previous year – as has been the case for several quarters now. This was a result of growth in the average occupancy ratios and in room prices. Average revenues per available hotel room also increased in Canada and to an even greater extent in Mexico in the second quarter.

Demand was also vivid for commercial property in North America, and transaction volumes picked up significantly in the quarter under review compared with the corresponding period of the previous year. As a consequence of great investor demand, investment yields for newly acquired commercial property in the US were down slightly on average compared with the previous quarter.

We originated new business in the amount of € 0.5 billion in North America during the second quarter, and thus a total of € 0.7 billion for the first two quarters of the year.

Asia

Rents in the quarter under review were stable or increasing compared to the previous quarter, in the leading big cities of China, Japan and in Singapore. While rents on the markets for high-quality retail properties in Beijing, Shanghai, Tokyo and Singapore increased on average, first-class office properties painted a mixed picture. Average rents for these properties in Tokyo and Singapore rose, while remaining virtually constant in the big Chinese cities of Beijing and Shanghai. In the logistics sector, rents in Beijing, Tokyo and Singapore were also almost stable, whilst rising in Shanghai.

Different developments were evident on the hotel markets in relation to the indicator of average revenues per available hotel room. This indicator changed only marginally in Beijing and Singapore compared with the second quarter of the previous year, while a marked increase was noticeable in Shanghai and Tokyo.

In the second quarter too, transaction volumes in the Asia / Pacific region were slightly lower than the corresponding figure for the previous year. The Japanese market in particular featured declines, while investments in China recovered. Investment yields in the big Chinese cities Beijing and Shanghai for high-quality commercial property remained largely stable. However, the situation was less consistent for the different types of property in Singapore and Tokyo, although a stable to slightly falling trend dominated. Nonetheless, a slight increase in yields for newly acquired logistics properties was recorded in Singapore.

We concluded only little new business in Asia in the second quarter. Our new business for the entire first half of the year amounted to € 0.2 billion.

Acquisition of COREALCREDIT BANK AG (Corealcredit)

Aareal Bank Group closed the acquisition of Corealcredit, announced on 22 December 2013: The purchase was completed with effect from 31 March 2014 (the closing date). Corealcredit is now a legally independent subsidiary under the umbrella of Aareal Bank Group. The (provisional) purchase price paid amounted to € 343 million. The provisional nature of this purchase price relates to the possibility of potential compensation payments to the seller. Further information is included in the notes to the consolidated financial statements.

Within the scope of the acquisition of Corealcredit, Aareal Bank assumed, among others, € 3.2 billion in loans and advances to customers, and non-trading assets in the amount of € 1.4 billion. A (provisional) negative goodwill of € 152 million arose from the acquisition and was charged against income at the time of initial consolidation on 31 March 2014. The figures from the operating business of Corealcredit have been included in Aareal Bank Group's consolidated net income in the second quarter of 2014 for the first time. Excluding negative goodwill, Corealcredit's contribution to the consolidated operating profit of Aareal Bank Group amounted to € 4 million during the first half of 2014. As part of the integration of Corealcredit into Aareal Bank Group, a control and profit and loss transfer agreement was concluded.

Consulting/Services segment

Bank division Housing Industry

The housing and commercial property industries in Germany have proven to be a stable market segment in the second quarter of 2014, too. Reliable rental payments generated from a highly-diversified tenant portfolio provide a solid foundation. The stability of rental cash flows is also bolstered by the fact that management tools for letting and rental claims handling are becoming more professional and more efficient all the time. The members of the German Housing Enterprises (Bundesverband deutscher Wohnungs- und Immobilienunternehmen – "GdW") have reported a 45 % decline in rental claims to € 346 million since 2003.

Based on the robust demand for residential property, residential rents continued to rise in the course of the year, even though the increase in rents eased in the big cities – with the exception of Berlin. Rents offered in April 2014 were some 1.8 % higher throughout Germany than the previous year's level, whereby rents in rural areas increased by 1.9 %, and in the major cities by 1.7 %.

Corporate investments in this sector continue to focus on improving the degree and quality of energy efficiency, and creating a sustainable quality of housing. To strengthen its long-term commitment to sustainability, the housing industry has subscribed to the German Sustainability Code (Deutscher Nachhaltigkeitskodex – "DNK") and refines the Code in line with industry-specific developments.

In view of the positive development on the residential property market, demand on the market for German residential property portfolios remained strong. Institutional investors are still mainly interested in residential property in regional conurbations. As investors' readiness to assume risk grows, the emphasis is also shifting to high-growth upper and middle-level centres as well as to east German influx regions. Domestic investors once again dominated market events on the buyer side. One of the largest residential property transactions of this quarter was the acquisition by a French real estate investment trust (REIT) of around 3,400 apartments in Dresden and Berlin.

Our clients continue to make strong use of the combination of our specialist services in conjunction with automated mass electronic payments processing, together with the related advice we offer, as well as cash investment schemes. This enables us to maintain a strong position in the market, despite strong competitive pressure – which is also evident in new client acquisition; the business partners acquired in the second quarter of 2014 currently manage a good 65,000 residential units between them. The volume of deposits remained high, averaging € 8.5 billion during the quarter under review (Q1 2014: € 8.1 billion).

However, the persistently low interest rate environment in the quarter under review burdened income generated from the deposit-taking business, and therefore the segment result. Yet the importance of the deposit-taking business in the Consulting/Services segment goes far beyond the interest margin generated from the deposits – which is under pressure in the current market environment. For Aareal Bank, deposits from the housing industry are a strategically important additional source of funding for the lending business, and one that is largely independent of capital markets developments. In addition to the German Pfandbrief and unsecured bank bonds, they represent an important pillar in the Bank's long-term funding mix. Especially in the current capital market environment, Aareal Bank therefore sees this business as representing a particular competitive advantage.

Aareon

Research and development activities continue to focus on the hot topic of digitisation. Essentially, this involves deploying IT resources in order to optimise external and internal processes. Housing enterprises enhance their integration with business partners (B2B), tenants (B2C) and their field service staff (B2E). This is enhanced by networking devices (M2M) and objects via the internet (the "internet of things"). At present, the focus is on digital document management, customer relationship management (CRM), and mobile solutions.

Aareon held the 24th Aareon Congress in Garmisch-Partenkirchen in the second quarter of 2014. This is the largest get-together of the property industry in Germany. Digitisation in the housing industry was one of the topics here. Aareon had already extended its product range in relation to this in 2013, and developed the so-called "digital ecosystem". This constitutes an IT infrastructure comprising a large number of integrated systems. All important business processes, whether renting or maintenance, are supported fully and digitally throughout. The ERP systems form the controlling centre at the heart of the digital ecosystem.

The mobile property inspection programme that was introduced in the fourth quarter of 2013 for the Wodis Sigma ERP system was extended in the current financial year to include comprehensive innovations. Additional customers decided in favour of Wodis Sigma – also as a service from the exclusive Aareon Cloud.

Demand was visible for the SAP® solutions and Blue Eagle – in Aareon's advisory solutions for SAP® and for consultancy services. The existing SAP consulting partner status was extended in May to include the Value Added Reseller status.

Business volumes generated with GES declined slightly, as planned. Numerous GES customers are in the process of reviewing their long-term IT strategy with a view to a technological upgrade, or have already done so. Generally, this goes hand in hand with the decision to migrate from GES to Wodis Sigma. Aareon has the necessary resources in place for future migrations of GES customers, to ensure that such migrations are executed smoothly and safely.

In the Integrated Services area, the Mareon service portal, the BauSecura insurance management, and Aareon's invoicing services all showed strong performances. Aareon Archiv kompakt, the digital archiving solution launched in 2013, met with increased demand. The Aareon invoicing service has been available as an online portal as of the second quarter.

The positive business trend in the international business continued in the second quarter. New customers were acquired and products were rolled out successfully. The Dutch subsidiary SG|automatisering reported several significant renewals, amongst them de Alliantie, a large customer based in Hilversum. The product development of digitisation for the Dutch market, which has an international focus, is progressing. In the UK, the mobile services provided by 1st Touch met with increased demand. The QL Housing ERP solution was rolled out successfully for Barnet Group, a major London-based customer. In France, market response to Aareon France's CRM system remains positive. In Sweden, MKB, Malmö one of the largest public sector property management companies, decided in favour of the ERP solution Incit Expand. The integration of the Swedish subsidiary Incit AB, Mölndal (acquired in 2013) into Aareon Group was successfully concluded in the quarter under review.

In order to optimise the group structure and enhance process efficiency, Aareon AG merged its subsidiary Aareon Wodis GmbH with Aareon Deutschland GmbH by entering it in the Commercial Register as at 23 May 2014.

Profit before taxes and interest (EBIT) for the first half of 2014 amounted to € 11 million (previous year: € 11 million).

Financial position and performance

Financial performance

Group

Since the start of the second quarter, the figures from the operating business of Corealcredit (acquired 31 March 2014) have been included in consolidated net income. These are reflected mainly in net interest income and in administrative expenses.

Consolidated operating profit amounted to € 282 million during the first six months of the financial year. Adjusted for the day-one gain from the initial consolidation of Corealcredit (€ 152 million), operating profit was € 130 million and thus markedly higher year-on-year (H1 2013: € 92 million). The expected cost increase was offset by clearly higher net interest income.

Net interest income of € 313 million for the first six months of the current financial year was up significantly on the same period of the previous year (€ 247 million), as predicted. The increase was particularly due to the higher lending volume, also in conjunction with the acquisition of Corealcredit. Net interest income for the first half of the year included € 12 million in non-recurring effects from early loan repayments.

Allowance for credit losses amounted to € 69 million during the first six months of the financial year (H1 2013: € 45 million), comprising € 39 million in specific allowance for credit losses plus € 30 million in portfolio-based allowance

Consolidated net income of Aareal Bank Group

€ mn	1 Jan-30 Jun 2014	1 Jan-30 Jun 2013
Net interest income	313	247
Allowance for credit losses	69	45
Net interest income after allowance for credit losses	**244**	**202**
Net commission income	79	77
Net result on hedge accounting	3	-3
Net trading income/expenses	4	11
Results from non-trading assets	0	-6
Results from investments accounted for using the equity method	–	–
Administrative expenses	216	182
Net other operating income/expenses	16	-7
Negative goodwill from the acquisition of Corealcredit	152	–
Operating profit	**282**	**92**
Income taxes	41	29
Consolidated net income/loss	**241**	**63**
Allocation of results		
Consolidated net income/loss attributable to non-controlling interests	10	10
Consolidated net income/loss attributable to shareholders of Aareal Bank AG	231	53
Appropriation of profits		
Consolidated net income/loss attributable to shareholders of Aareal Bank AG	231	53
Silent participation by SoFFin	10	10
Consolidated profit/loss	**221**	**43**

for credit losses. The higher amount of portfolio-based allowance for credit losses was largely due to a change in individual measurement parameters, and thus non-recurring. Allowance for credit losses was therefore within the pro-rata forecast range of € 100 million to € 150 million for the full financial year.

As expected, net commission income rose slightly in the first half-year compared with the previous year to € 79 million (2013: € 77 million). This increase was largely due to higher sales revenue achieved by Aareon.

Net trading income / expenses, the net result on hedge accounting and the result from non-trading assets totalled € 7 million (2013: € 2 million).

Administrative expenses of € 216 million were significantly higher than the prior-year level (€ 182 million). The rise is due, among other things, to the running costs for Corealcredit, included in expenditure since the second quarter. Furthermore, higher project costs were incurred during the reporting period, including those in conjunction with the acquisition of Corealcredit and regulatory measures such as the Asset Quality Review.

Net other operating income / expenses includes € 18 million in non-recurring income from the reversal of provisions for settlement risks.

The negative goodwill is a result of the acquisition of Corealcredit. It represents the difference between the (provisional) purchase price paid and the higher net balance of assets and liabilities acquired and measured at fair value. Further information is included in the section "Reporting entity structure" in the notes to the consolidated financial statements.

This results overall in consolidated operating profit of € 282 million for the first half of 2014 (H1 2013: € 92 million). Taking into consideration income taxes of € 41 million and non-controlling interest income of € 10 million, consolidated net income attributable to shareholders of Aareal Bank AG amounted to € 231 million. Taking into consideration the net interest payable on the SoFFin silent participation, the consolidated profit stood at € 221 million.

Structured Property Financing segment

Since the start of the second quarter, the figures from the operating business of Corealcredit, which was acquired as at 31 March 2014, are also

Structured Property Financing segment result

€ mn	Quarter 2 2014	Quarter 2 2013
Net interest income	168	124
Allowance for credit losses	32	28
Net interest income after allowance for credit losses	**136**	**96**
Net commission income	1	3
Net result on hedge accounting	1	0
Net trading income/expenses	2	5
Results from non-trading assets	0	-5
Results from investments accounted for using the equity method	–	–
Administrative expenses	68	47
Net other operating income/expenses	-1	-2
Negative goodwill from the acquisition of Corealcredit	–	–
Operating profit	**71**	**50**
Income taxes	23	15
Segment result	**48**	**35**

included in the segment result. These are reflected mainly in net interest income and in administrative expenses.

Consolidated operating profit in the segment amounted to € 71 million for the quarter under review, and was therefore considerably higher than the corresponding figure for the previous year (€ 50 million). The anticipated rise in costs is offset by a sharp rise in net interest income.

Net interest income was € 168 million in the second quarter. It therefore exceeded both the figure for the previous quarter (€ 143 million) and the same quarter of the previous year (€ 124 million). The rise in net interest income, compared to the previous quarter, was attributable, among other things, to the higher loan volume as a result of the acquisition of Corealcredit. Net interest income for the second quarter of the year included € 8 million in non-recurring effects from early loan repayments.

Allowance for credit losses from April to June amounted to € 32 million (2013: € 28 million). Allowance for credit losses was therefore within the pro-rata forecast range of € 100 million to € 150 million for the financial year.

Administrative expenses of € 68 million in the quarter under review were significantly higher than the prior-year level (€ 47 million). The rise is due, among other things, to the running costs for Corealcredit that are included in expenditure since the second quarter. Furthermore, higher project costs were incurred during the reporting period, including those in conjunction with the acquisition of Corealcredit, and regulatory measures such as the Asset Quality Review.

Overall, operating profit for the second quarter in the segment was € 71 million (Q2 2013: € 50 million). After tax deductions of € 23 million, the quarterly result in the Structured Property Financing segment was € 48 million (2013: € 35 million).

Consulting/Services segment

Sales revenue generated in the Consulting/Services segment during the second quarter of 2014, which amounted to € 45 million, was slightly higher than the corresponding figure of the previous year (€ 44 million). Whilst Aareon's sales revenue were up, the persistent low interest rate environment burdened the margins from the deposit-taking business that are reported in sales revenue.

Consulting/Services segment result

€ mn	Quarter 2 2014	Quarter 2 2013
Sales revenue	45	44
Own work capitalised	1	1
Changes in inventory	0	0
Other operating income	2	1
Cost of materials purchased	5	5
Staff expenses	32	29
Depreciation, amortisation and impairment losses	3	4
Results from investments accounted for using the equity method	–	–
Other operating expenses	14	13
Interest and similar income/expenses	0	0
Operating profit	**-6**	**-5**
Income taxes	-2	-1
Segment result	**-4**	**-4**

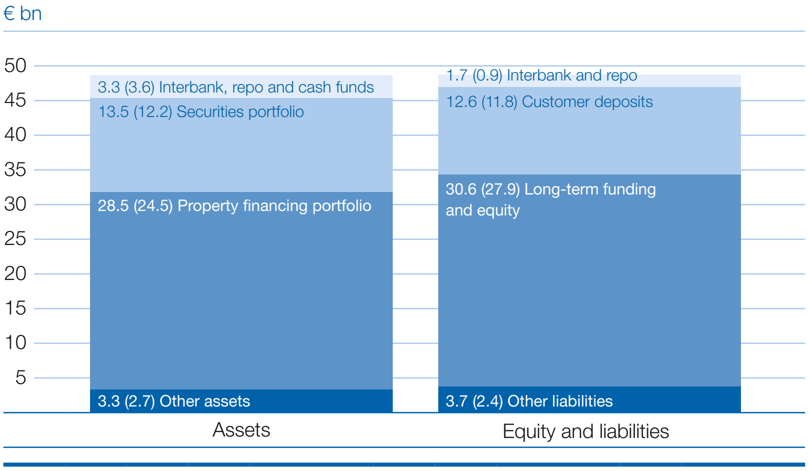
Staff expenses in the quarter under review amounted to € 32 million. The increase compared to the second quarter of 2013 (€ 29 million) was also attributable to Incit Group, which has been consolidated since 1 July 2013.

On the whole, other items were roughly unchanged from the previous year's levels.

In the second quarter of 2014, the operating profit of the Consulting / Services segment totalled € -6 million (2013: € -5 million). Aareon posted an operating profit of € 6 million (2013: € 6 million).

After taking taxes into consideration, the segment result for the second quarter amounted to € -4 million (Q2 2013: € -4 million).

Statement of financial position – structure as at 30 Jun 2014 (31 Dec 2013)



Financial position

Corealcredit was consolidated in the consolidated financial statements of Aareal Bank Group for the first time as at the reporting date of 31 March 2014. Aareal Bank's consolidated statement of financial position thus includes all of Corealcredit's line items.

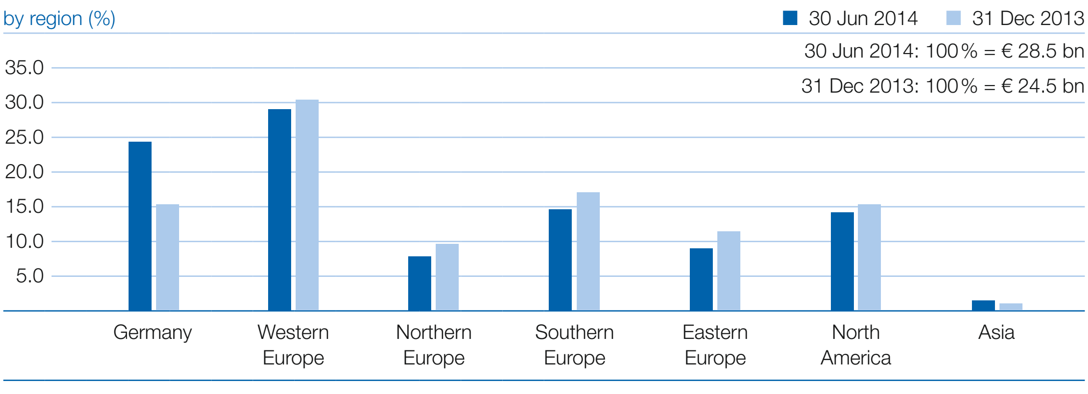
Aareal Bank Group's total assets as at 30 June 2014 amounted to € 48.6 billion, after € 43.0 billion as at 31 December 2013.

Property financing portfolio

The volume of Aareal Bank Group's property financing portfolio stood at € 28.5 billion as at 30 June 2014. Relative to year-end 2013 (€ 24.5 billion), this equates to an increase of around 16 %, which is largely attributable to the acquisition of Corealcredit. The acquisition, effective 31 March 2014, exclusively increased the German property financing portfolio, by € 3.4 billion. Accordingly, the international share of the portfolio fell to 75.7 % (31 December 2013: 84.7 %).

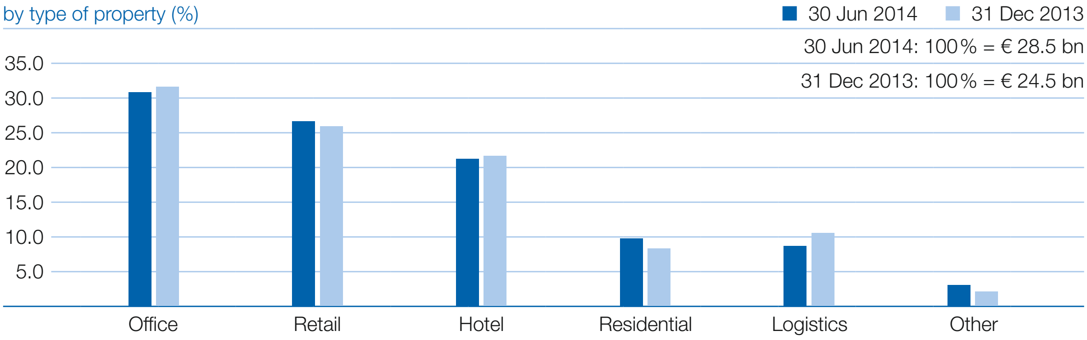
At the reporting date, Aareal Bank Group's property financing portfolio was composed as indicated below, compared with year-end 2013.

Property financing volume (amounts drawn)



Property financing volume (amounts drawn)

by type of property (%)



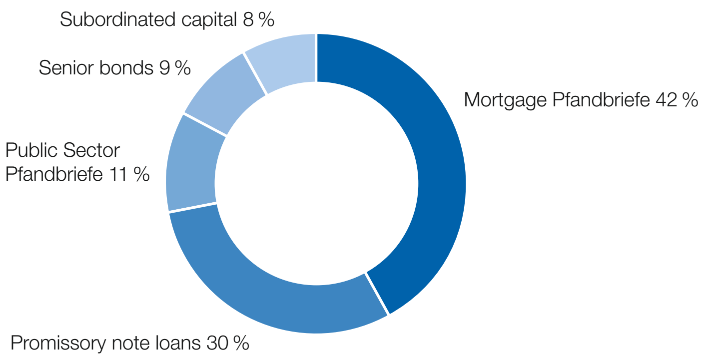
The acquisition of Corealcredit led to a marked increase in the portfolio share attributable to Germany. Accordingly, the share of other regions in the entire property financing portfolio mostly declined.

The portfolio breakdown by property type remained largely unchanged during the period under review. Only the share of housing property finance showed a more pronounced increase, due to the takeover of Corealcredit.

All in all, the high degree of diversification by region and property type within the property financing portfolio was maintained in the 2014 period under review.

Capital market funding mix as at 30 June 2014

% Total volume: € 28.5 bn



Securities portfolio

The securities portfolio[1] as at 30 June 2014 was worth € 11.6 billion (nominal volume) compared with € 10.8 billion as at 31 December 2013, of which € 1.2 billion was attributable to Corealcredit, which was acquired as at 31 March 2014. The securities portfolio comprises four asset classes: public-sector borrowers, covered bonds and Pfandbriefe, bank bonds, and asset-backed securities (ABS).

97 %[2] of the total figure is denominated in euros and 98 %[2] have an investment-grade rating.[3]

Financial position

Refinancing and equity

Refinancing

Aareal Bank Group continued to successfully conduct its funding activities in the second quarter of 2014, thereby securing its very solid liquidity situation. Total long-term funding as at 30 June 2014 amounted to € 28.5 billion (31 December 2013: € 26.0 billion). This comprises Pfandbrief issues, senior unsecured and subordinated issues. As at the reporting date, Aareal Bank also had € 7.5 billion at its disposal from deposits gener-

[1] As at 30 June 2014, the securities portfolio was carried at € 13.5 billion (31 December 2013: € 12.2 billion).
[2] Details based on the nominal volume
[3] All rating details are based on composite ratings.

ated from the business with the housing industry (31 December 2013: € 7.0 billion). Institutional money market investors' deposits amounted to € 5.1 billion (31 December 2013: € 4.8 billion).

Aareal Bank Group raised € 400 million in long-term funds on the capital market during the second quarter. This sum comprised Mortgage Pfandbriefe in the amount of € 100 million, unsecured refinancing of € 200 million, as well as subordinated liabilities of € 100 million. Aareal Bank has therefore maintained its long-term funding at a high level.

The total volume of long-term funding raised in the first half of 2014 amounted to € 2.1 billion, with Mortgage Pfandbriefe accounting for € 0.8 billion. Unsecured refinancing amounted to € 0.8 billion. In addition, € 0.5 billion in subordinated bonds were placed with investors.

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

Equity

As at 30 June 2014, Aareal Bank Group's consolidated equity amounted to €2.1 billion, excluding the SoFFin silent participation and trust preferred securities (31 December 2013: € 1.9 billion).

Regulatory indicators[1)]

	30 Jun 2014
€ mn	
Common equity tier 1	2,351
Tier 1	2,679
Total capital	3,672
Risk-weighted assets (incl. market risk)	16,399
%	
Common equity tier 1 ratio	14.3
Tier 1 ratio	16.3
Total capital ratio	22.4

The regulatory measurement of risk-weighted assets (RWAs) in the area of credit risks is based on both the Advanced Internal Ratings Based Approach (AIRBA) and on the standardised approach (CRSA). RWAs can be analysed as showed in the table below.

RWAs acquired through the takeover of Corealcredit were determined in accordance with the Credit Risk Standard Approach (CRSA).

30 June 2014[1)]

	EAD	Risk-weighted assets (RWA)			Regulatory capital requirements
		AIRBA	KSA	Total	
€ mn					
Credit risks	**49,335**	**11,032**	**3,436**	**14,468**	**1,158**
Companies	30,566	9,186	2,396	11,582	927
Institutions	6,456	755	108	863	69
Public-sector entities	10,872	0	15	15	1
Other	1,441	1,091	917	2,008	161
Market price risks				**616**	**49**
Operational risks				**1,315**	**105**
Total	**49,335**	**11,032**	**3,436**	**16,399**	**1,312**

1) Since 1 January 2014, regulatory indicators have been determined in accordance with CRD IV/CRR, based on carrying amounts in accordance with IFRSs. Until 31 December 2013, the rules of the German Solvency Regulation (SolvV), applied on the basis of German Commercial Code (HGB) carrying amounts, were applied for this purpose. The Bank therefore decided against stating comparative amounts.

Report on Material Events after the Reporting Date

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

Risk Report

Aareal Bank Group Risk Management

The Annual Report 2013 contains a comprehensive description of Aareal Bank Group's risk management approach, including the corresponding organisational structure and workflows in the lending and trading businesses, as well as the methods and procedures used for measuring and monitoring risk exposure. Within the scope of this interim report, we will once again briefly outline the key components of our risk management structure, together with the key developments during the period under review.

The business policy set by the Management Board, and approved by the Supervisory Board, provides the conceptual framework for Aareal Bank Group's risk management. Taking this as a basis, and in strict consideration of the Bank's risk-bearing capacity, we have formulated detailed strategies for managing the various types of risk. These risk strategies, as well as the Bank's business strategy, are adapted to the changed environment at least once a year, and adopted by the Management Board and the Supervisory Board. Suitable risk management and risk control processes are deployed to implement the risk strategies, and to ascertain the Bank's ability to bear risk.

Risk-bearing capacity and risk limits

The Bank's ability to carry and sustain risk is a core determining factor governing the structure of its risk management system. To ascertain its uninterrupted risk-bearing capacity, Aareal Bank has adopted a dual management approach whereby its risk management is primarily based on the assumption of a going concern. This approach ensures that risk positions are only established to an extent that the institution's continued existence will not be threatened should the risks materialise. A secondary management process ensures that risk positions are only established to an extent that even in the event of liquidation there will still be sufficient potential risk cover in order to service all liabilities (the "gone concern" approach). The statements below relate to the going-concern

Risk-bearing capacity of the Aareal Bank Group as at 30 June 2014
– Going concern approach –

€ mn	30 Jun 2014	31 Dec 2013
Own funds for risk cover potential	2,530	2,504
less 8 % minimum core tier 1 (CET 1)	1,442	1,282
Freely available funds	**1,088**	**1,222**
Utilisation of freely available funds		
Credit risks	244	225
Market risks	156	220
Operational risks	53	44
Investment risks	37	28
Total utilisation	**490**	**516**
Utilisation as a percentage of freely available funds	**45 %**	**42 %**

approach which the Bank has implemented as a primary management process.

In accordance with this approach, potential risk cover is determined using data derived from the income statement and from the statement of financial position; this derivation also forms the basis for determining regulatory capital. This involves setting aside the maximum amount of own funds required as potential risk cover to offset risks without causing a breach of minimum requirements pursuant to the German Solvency Regulation (SolvV). Aareal Bank has decided to considerably exceed this minimum requirement, and to prudently apply a Common Equity Tier 1 (CET 1) ratio (calculated in accordance with Basel III) of 8 % to its risk-bearing capacity concept. Only free own funds exceeding this level are applied as potential risk cover, of which a further 12 % is retained as a risk cushion. This cushion is not applied to risk limits, and is thus available for risk types that cannot be quantified (for example, reputational or strategic risks).

We adopt an equally conservative stance with respect to setting risk limits. The aggregation of individual limits is based on the assumption that no risk-mitigating correlation effects exist amongst different types of risk. Taking into account the prior deduction of a minimum Common Equity Tier 1 (CET 1) ratio of 8 %, the value-at-risk models used to quantify risks are based on a confidence interval of 95 % and a one-year holding period (250 trading days). A monthly report submitted to the Management Board provides information regarding the utilisation of individual limits for the material types of risk, as well as on the overall limit utilisation. The table before (p. 20) summarises the Bank's overall risk exposure as at 30 June 2014.

Since aggregate risk cover is an inadequate measure to assess the risk-bearing capacity for liquidity risk, we have defined special tools for managing this type of risk. These tools are described in detail in the section "Liquidity risks".

Credit risks

Definition

Aareal Bank defines credit risk or counterparty credit risk as the risk of losses being incurred due to (i) a business partner defaulting on contractual obligations; (ii) collateral being impaired; or (iii) a risk arising upon realisation of collateral. Both credit business and trading activities may be subject to counterparty credit risk. Counterparty credit risk exposure from trading activities may refer to risk exposure vis-à-vis counterparties or issuers. Country risk is also defined as a form of counterparty credit risk.

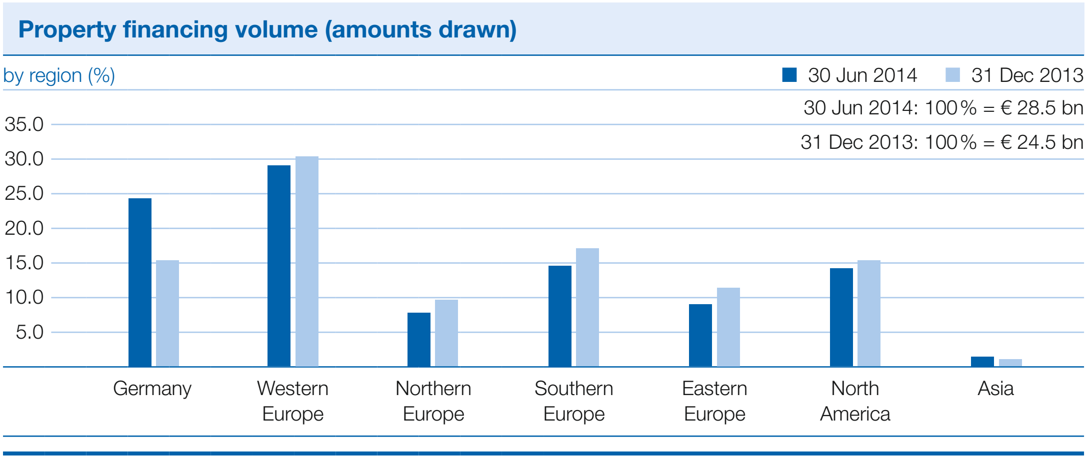
Risk measurement and monitoring

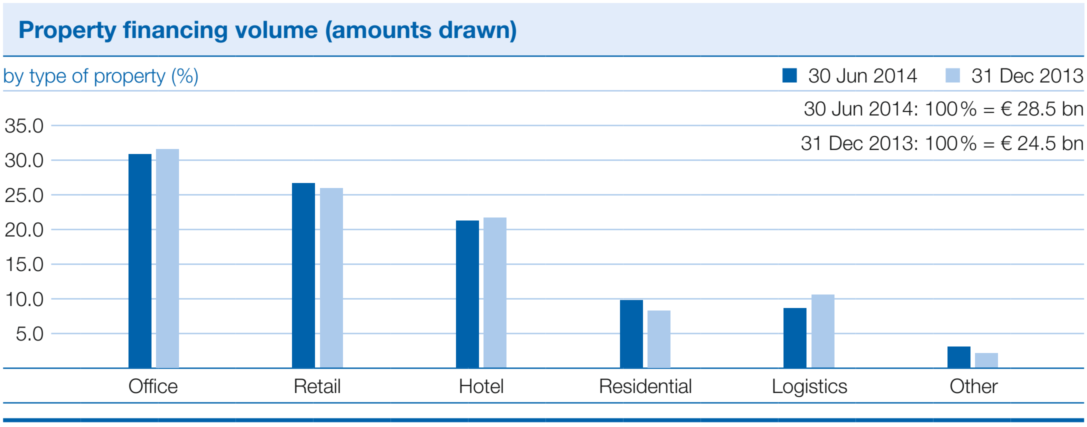
Aareal Bank's structural organisation and business processes are consistently geared towards effective and professional risk management. Regulatory requirements are fully taken into account for the organisation of operations and workflows in the credit and trading business.

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

Aareal Bank employs various risk classification procedures for the initial, regular, or event-driven assessment of counterparty risk; these procedures are adapted specifically to meet the requirements of the relevant business activity and are subject to permanent review and improvement. Responsibility for development, quality assurance, and monitoring implementation of risk classification procedures, is held outside of the Sales units.

Methods used to measure, control and monitor concentration and diversification effects on a portfolio level include two diverse credit risk models. Based on these models, the Bank's decision-makers





are regularly informed of the performance and risk content of property financing exposures, and of business with financial institutions. The models in question allow the Bank to include in particular, rating changes and correlation effects in the assessment of the risk concentrations.

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

A credit risk report that complies with the Minimum Requirements for Risk Management (MaRisk) is prepared and submitted to the Bank's Management Board and Supervisory Board on a regular basis, at least quarterly. This report contains extensive information on the development of the credit portfolio (covering countries, types of property and product types, risk classes and categories of collateral), with a particular focus on risk concentrations.

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

In principle, Aareal Bank pursues a "buy, manage and hold" strategy in managing its credit portfolio: this means that loans are generally held until maturity; sales of loans to third parties during their term are only used on a selective basis. Loan syndication is used as an active element of portfolio management.

In summary, during the period under review, the existing set of tools and methods continued to enable the Bank to adopt suitable risk management or risk mitigation measures, where required, at an early stage.

Country risks

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

Market price risks

Definition

Market price risk is broadly defined as the threat of losses due to changes in market parameters. Aareal Bank Group's market price risk exposure predominantly comprises interest rate risks, whilst currency risks are largely eliminated through hedges. Commodity and other price risks are irrelevant for the Bank's business. Hence, the primary market price risk exposures are related to the risk parameters interest rates, equity prices, exchange rates, and implied volatilities. All relevant parameters are covered by our management and monitoring tools. Derivative financial instruments are primarily used as hedging instruments. Spread risks between the various yield curves (e.g. government, Pfandbrief and swap curves) are taken into account. The risk exposure from bonds that is not related to market price or interest rate risks is managed as part of "specific risk", in particular, credit and liquidity risk exposure of the bond portfolio.

Risk measurement and monitoring

Risk Controlling informs the members of the Management Board responsible for Treasury and risk monitoring about the risk position and the market price risk exposure on a daily basis. In addition, the entire Management Board is informed on a monthly basis, within the scope of an extensive risk report. A quarterly report is submitted to the Supervisory Board.

Value-at-risk (VaR) has been broadly accepted as the predominant method for measuring general market price risk. The VaR for market price risk quantifies the exposure as a negative divergence from the current aggregate value of the Bank's financial transactions. This absolute amount indicates the potential loss incurred before countermeasures take effect. Since this is a statistical approach, the forecast for the potential loss that may be incurred within a specific period of time is for a given confidence interval only.

A variance-covariance approach (delta-normal method) is used throughout the Group to determine the VaR indicator. Determined on a daily basis for the Group and all its operating units, the VaR figure takes into account the correlation between individual risk types. Statistical parameters used in the VaR model are calculated directly from a 250-day historical data pool maintained within the Bank. The loss potential is determined applying a 95 % confidence interval and a 250-day holding period.

By their very nature, VaR calculations are based on assumptions regarding the future development of the business, and the related cash flows. Key assumptions used include current account balances which are factored into calculations for a period of up to five years, using the average residual amount of deposits observed in the past. Loans are taken into account using their fixed-interest period (for fixed-rate exposures), or using their expected maturity (variable-rate exposures). Aareal Bank's equity is not taken into account as a risk-mitigating item. This tends to overstate VaR, demonstrating the conservative approach adopted in our risk measurement processes.

The limit set for the VaR figure is derived from the analysis of the Bank's risk-bearing capacity, which is carried out at least once a year. Limits are defined at Group level, as well as for the individual Group entities. Being authorised to maintain a trading book, Aareal Bank AG has defined an additional trading book limit, plus a separate value-at-risk limit for fund assets held.

When interpreting the VaR figures stated below, it should be taken into account that these refer to the overall portfolio (thus including all non-trading positions as defined in IFRSs). Hence, the analysis provided represents a very extensive disclosure of market price risks by industry standards.

€ mn	MAX	MIN	Mean	Limit
Q2 2014 (2013 year-end values) 95%, 250-day holding period				
Aareal Bank Group – general market price risk	181.7 (260.8)	111.8 (137.1)	136.4 (184.5)	– (–)
Group VaR (interest rates)	167.2 (248.8)	97.2 (136.2)	122.7 (177.3)	– (–)
Group VaR (FX)	58.8 (46.5)	46.4 (31.2)	54.5 (39.0)	– (–)
VaR (funds)	0.3 (7.0)	0.3 (0.3)	0.3 (3.6)	20.0 (20.0)
Aggregate VaR in the trading book (incl. specific VaR)	0.0 (0.0)	0.0 (0.0)	0.0 (0.0)	5.0 (5.0)
Trading book VaR (interest rates)	0.0 (0.0)	0.0 (0.0)	0.0 (0.0)	– (–)
Trading book VaR (FX)	0.0 (0.0)	0.0 (0.0)	0.0 (0.0)	– (–)
VaR (equities)	0.0 (0.0)	0.0 (0.0)	0.0 (0.0)	– (–)
Group VaR (specific risks)	135.6 (227.7)	96.7 (132.9)	116.0 (183.6)	– (–)
Aggregate VaR – Aareal Bank Group	226.7 (318.6)	148.5 (205.2)	179.2 (262.2)	390.0 (400.0)

To ensure that Aareal Bank's figures are comparable to those published by other institutions, the risk parameters shown below were determined for a one-day holding period:

€ mn	MAX	MIN	Mean	Limit
Q2 2014 (2013 year-end values) 95%, 1-day holding period				
Aareal Bank Group – general market price risk	11.5 (16.5)	7.1 (8.7)	8.6 (11.7)	– (–)
Group VaR (interest rates)	10.6 (15.7)	6.1 (8.6)	7.8 (11.2)	– (–)
Group VaR (FX)	3.7 (2.9)	2.9 (2.0)	3.4 (2.5)	– (–)
VaR (funds)	0.0 (0.4)	0.0 (0.0)	0.0 (0.2)	1.3 (1.3)
Aggregate VaR in the trading book (incl. specific VaR)	0.0 (0.0)	0.0 (0.0)	0.0 (0.0)	0.3 (0.3)
Trading book VaR (interest rates)	0.0 (0.0)	0.0 (0.0)	0.0 (0.0)	– (–)
Trading book VaR (FX)	0.0 (0.0)	0.0 (0.0)	0.0 (0.0)	– (–)
VaR (equities)	0.0 (0.0)	0.0 (0.0)	0.0 (0.0)	– (–)
Group VaR (specific risks)	8.6 (14.4)	6.1 (8.4)	7.3 (11.6)	– (–)
Aggregate VaR – Aareal Bank Group	14.3 (20.1)	9.4 (13.0)	11.3 (16.6)	24.7 (25.3)

Aggregate VaR – Aareal Bank Group

Group-wide limits are being continuously monitored as part of the analysis of the Bank's risk-bearing capacity. These limits were adjusted during the first quarter, due to the consolidation of Corealcredit into Aareal Bank Group. No limit breaches were detected even after this re-calibration.

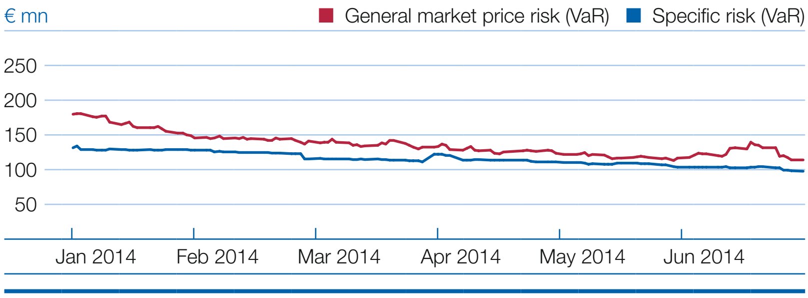
Backtesting

The quality of forecasts made using this statistical model is checked through a weekly backtesting process. The quality of the statistical procedure used to measure risk is checked using a binomial test, whereby daily profits and losses from market fluctuations are compared with the upper projected loss limit (VaR) forecast on the previous day (known as "clean backtesting"). In line with the selected confidence level of 95 %, only a small number of events are expected to break out of the VaR projection (≤ 17 for a 250-day period). No negative outliers at Group level occurred during the last 250 trading days, affirming the high forecasting quality of the VaR model we use.

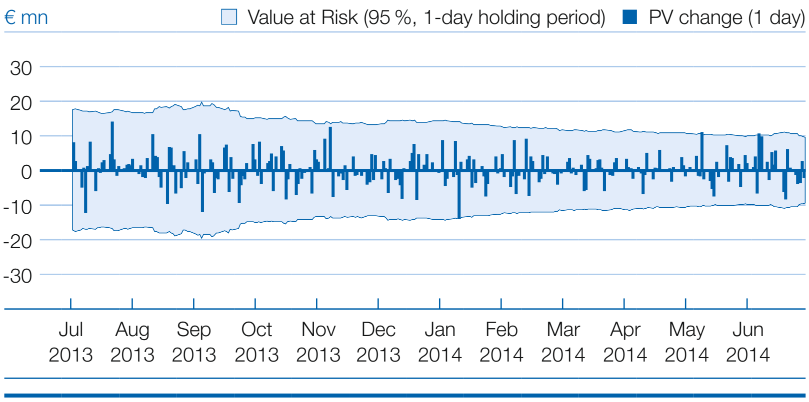
Trading book

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

General market price risk and specific risk during 2014



Present values and 1-day VaR during 2013/2014



Liquidity risks

Liquidity risk in the narrower sense is defined as the risk that current or future payment obligations cannot be met in full or on time. Aareal Bank Group's liquidity risk management system is designed to ensure that the Bank has sufficient cash and cash equivalents to honour its payment obligations at any future point in time. The risk management and monitoring processes have been designed to cover refinancing and market liquidity risks in addition to liquidity risk in the narrower sense.

Treasury is responsible for managing liquidity risks, whilst Risk Controlling ensures the continuous monitoring, including a daily liquidity report submitted to Treasury, and a contribution to the monthly risk report to the entire Management Board.

The appropriateness of the Bank's liquidity is assessed in a liquidity report prepared using an internal liquidity risk model: the aggregate of all potential cash inflows and outflows over a three-month period is compared to the liquidity stock. There were no liquidity shortages throughout the period under review. The requirements of the liquidity ratio in accordance with the Liquidity Ordinance, which is relevant to liquidity management, were always complied with, as were the limits set by reference to the liquidity run-off profile. Further details are provided in the comments on the Bank's liquidity in the section on "Refinancing and Equity".

Operational risks

Aareal Bank defines operational risk as the threat of losses caused by inappropriate internal procedures, human resources and systems (or their failure); or through external events. This includes legal risks. Aareal Bank's legal department (Corporate Development – Legal) compiles all information concerning any legal disputes involving Aareal Bank Group, whether in or out of court. The involvement of the legal department is based on corresponding Group-wide guidelines. The Bank's decentralised operating legal entities, as well as the legal departments of subsidiaries submit semi-annual as well as event-driven reports on legal risks identified to Aareal Bank's legal department, which reports to the Management Board, also (at least) on a semi-annual basis. Moreover, information about legal risks is also included in operational risk reporting. Strategic, reputational and systematic risks are not covered by operational risk management. These risks are managed largely through qualitative measures.

Aareal Bank's policy for managing and monitoring operational risks is geared to achieving a risk-minimising or loss-limiting effect at an early stage, by employing a pro-active approach. The Risk Report in the 2013 Annual Report contains a detailed description of controlling tools employed by the Bank to manage operational risk, plus the relevant responsibilities.

Within the scope of the acquisition of Corealcredit, Aareal Bank also assumed legal, tax and credit risks, among others. These risks were assessed on a conservative basis and are hedged comprehensively.

The current analysis conducted using these control instruments has shown that the Bank is not exposed to disproportionate operational risks; nor did it indicate any material risk concentration.

Operational risk management also includes the reporting to the Bank's Management Board about outsourced activities and processes.

Investment risks

We define investment risk as the threat of unexpected losses incurred due to an impairment of the investment's carrying amount, or a default of loans extended to investees. The concept of investment risk also encompasses additional risks arising from contingencies vis-à-vis the relevant Group entities.

Due to the special character of some exposures (e.g. marketing risks), special methods and procedures are employed to deal with investment risk. All relevant Group entities are subject to regular audits, including a review and assessment of their risk situation. A quarterly investment risk report is submitted to the Bank's Management Board. There were no significant changes in investment risk during the period under review.

Report on Expected Developments

Macro-economic environment

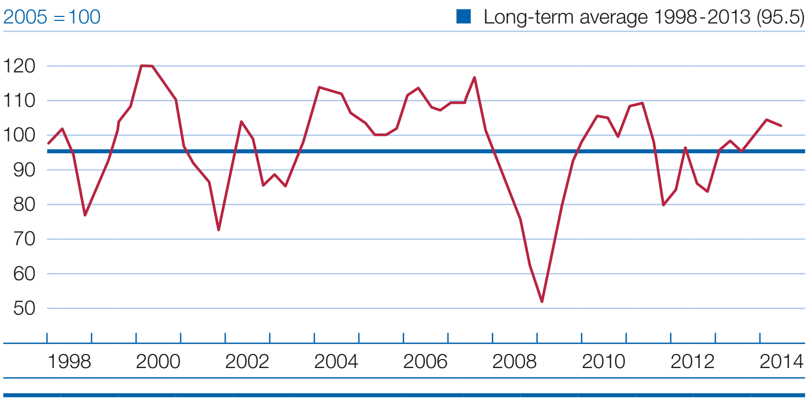
Economy

Global economic growth is expected to grow at a slightly stronger rate this year than in 2013. The economy could gradually gain momentum in the second half of the year, particularly in the developed economies. This is supported by the fact that uncertainty concerning the further development of the European sovereign debt crisis has meanwhile eased considerably. Additionally, deleveraging processes in the private sector have taken hold over a significant period of time in some economies, especially in the US and the UK. Private household incomes have increased in those countries, not least thanks to the growth in employment. This could stimulate demand. Nonetheless, significant impediments still exist that could prevent the dynamic growth of the global economy. These include the consolidation processes in various economies and the still high level of unemployment in many euro zone countries. Deteriorating financial frameworks in some emerging economies, brought about by capital outflows at the start of the year, represent major burdens and risk factors for economic development. This demonstrates clearly that the global economy will recover only slightly and at a slow pace, and that there are likely to be significant regional differences in economic development.

Furthermore, economic development is subject to significant risk and uncertainty factors that can significantly threaten the forecasted muted economic growth. The tensions between the Ukraine and Russia could significantly impair economic development in Europe through trade channels, developments in the commodities sector and financial interdependence. Other geopolitical tensions could also drive up commodity prices. Although uncertainty surrounding the European sovereign debt crisis has eased considerably, a rekindling (and hence a renewed burden on the economy) cannot be ruled out entirely. There is a lack of broad fundamental support for economic development. In this respect, overly slow or inadequate risk defences are increasing the threat that systemic risks pose to monetary stability or the stability of the euro system. The current low interest rate environment, which is likely to persist for quite some time yet in Europe in particular, is associated with risks and side-effects. It tempts market players to enter into higher risks and also carries the threat of a bubble on the capital markets as well as mis-allocation of capital. This could in turn threaten financial stability. In addition, the low interest rate environment could lead to delays on the reform and consolidation efforts undertaken in the public sector, as well as in the private and banking sectors. The longer the low interest rate environment persists, the greater the risk of negative implications.

We anticipate a slight increase in real gross domestic product for the euro zone for the full year. We also expect slight growth in the second half of the year. The growth should be supported by declining uncertainty in conjunction with the sovereign debt crisis. However, the aforementioned burdens and risk factors, such as the persistently high unemployment levels in many places, imply

ifo Global Economic Climate*



* Arithmetic mean of the assessment of the current situation and expected developments,
Source: ifo World Economic Survey (WES) II/2014

that economic growth will be both muted and hesitant. This expected development is supported by a restrictive fiscal policy in many countries, albeit less pronounced than in previous years. We are also likely to see considerable differences between the individual countries of the euro zone. Germany and Austria have relatively good growth prospects within the euro zone, with moderate growth in real gross domestic product. In contrast, we expect a lower, slight economic growth for Belgium, France and Spain. However, the economy in Spain has not only stabilised, but also shows signs of cautious recovery for the future. The economy in the Netherlands and Italy that was also in recession last year, as was the case in Spain has stabilised. Nonetheless, expectations are reserved and we anticipate only a marginal increase in real gross domestic product for this year in these countries. We forecast stable to marginally lower real gross domestic product for Finland. The threat of deflation cannot be ruled out for the euro zone, which would also have considerable implications for economic development due to restrained demand.

Economic growth in numerous European countries outside the euro zone is expected to post much stronger numbers than the euro zone average. Notable growth is anticipated for the UK and Poland in particular. The Czech Republic could also achieve considerable growth rates after a two-year recession. Although the growth rates forecast for Denmark, Sweden and Switzerland are lower than those of the aforementioned countries, they are expected to reach moderate levels. They would be on par with Germany and therefore – as a benchmark – above the euro zone average. However, there are concerns in some countries in Europe, especially in the UK, that sharp price increases on the residential property markets could lead to longer-term risks. In light of the political tensions and potential economic consequences, we anticipate practically no growth in Russia's economy this year. In our view, economic growth in Turkey will be substantially below the previous year's level.

Following the weather-related difficult start to the year in the US, we anticipate vivid economic growth in the second half of the year. Given the burden arising from the unusually harsh winter, we also revised our expectations for economic growth downwards to slightly lower than the previous year – after the US statistics office revised gross domestic product for the first quarter significantly downwards several times. The positive expectations for the US for the remainder of the year are supported by the fact that private households have clearly concluded their debt reduction processes, which should stimulate consumption. Construction activity could also provide support here. Unlike the previous year, fiscal policy will hardly act any longer as a brake. Although the expected end to the Fed's bond purchasing programme should lead to a slight increase in long-term interest rates, it is not expected to impact heavily on investment. Nonetheless, it still poses a certain degree of risk for economic development. We now expect real gross domestic product in Canada to progress at roughly the same rate as in the previous year, while the growth rate in Mexico is supposed to rise slightly.

We anticipate economic growth to be slightly below the previous year's level in Japan. The increase in value-added tax in April of this year is likely to have a weakening effect for the year as a whole, despite an economic stimulus programme. Economic momentum is no longer as dynamic in some countries of the Asia-Pacific region. At present, the Chinese economy no longer reaches the growth rates experienced in previous years. We believe a moderate slowdown in growth compared with the previous year is likely. Even so, the growth rates remain high by international standards. We anticipate growth rates in Singapore, too, to be slightly lower than the year before.

Unemployment will change only marginally or fall slightly in numerous European countries. It will therefore remain high in Southern Europe in particular. The unemployment rate will also be just above 10 % in France. However, the slight decline in unemployment should persist in Spain, coming from a very high level. A marked decline is likely for the UK. Germany and Austria should continue to record the lowest unemployment rates within the euro zone. A further significant decline is expected here for the US.

Financial and capital markets, monetary policy and inflation

The situation on the financial and capital markets of the developed economies eased further compared with the previous years. At present, there are no signs of significant changes in this respect for the current year. While uncertainty about the further development of the European sovereign debt crisis has meanwhile eased considerably, risks continue to persist, and it cannot be ruled out that the financial and capital markets are still very susceptible to shocks, should the sovereign debt crisis escalate again. Unrest on Portugal's financial and capital markets, which arose in June and July as a consequence of concerns surrounding a major Portuguese bank, highlight the fact that the markets could experience higher volatility in the future as well. Renewed tensions are possible on the financial and capital markets of various emerging market economies, in the event that significant capital outflows are once again an issue.

In view of the low inflationary pressure, we continue to assume that the central banks of developed economies will keep their key interest rates low this year. Consequently, under current conditions, short-term interest rates are also expected to remain at low levels. An anticipated exit from the bond purchasing programme in the US this year could lead to a slight increase in long-term interest rates. This development could spread further to other countries, although we continue to forecast very low interest rate levels for the euro zone, even in the long-term segment, which involves risks for the economy – as was outlined above. Risk premiums for countries in the euro zone periphery should continue to flatten during the year, provided no new uncertainty arises in conjunction with the European sovereign debt crisis. Nonetheless, marked yield premiums should remain in place for now.

In light of the subdued economic development, inflationary pressure in the euro zone is low and likely to remain clearly below the previous year's level. Deflation could therefore be a potential development. Inflation rates ranging from around the zero per cent mark, as is the case in Sweden, up to 3 % in the UK, are forecast for European countries outside the euro zone. Inflation rates in Russia and Turkey are expected to be significantly higher. Moderate inflation – slightly higher than the previous year's level – is likely in the US. In Japan, the increase in value-added tax and extremely expansive monetary policy should drive inflation for the year as a whole above the two per cent mark. China's average annual inflation should also fluctuate around this level. Geopolitical tensions could, however, drive up commodity prices and hence inflation in various regions.

Regulatory environment

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

The ECB's Comprehensive Assessment in particular has raised requirements and ties up additional resources. Furthermore, additional regulatory requirements will need to be dealt with. These include the Minimum Requirements for the Design of Recovery Plans ("MaSan") on a national level as well as the EU Bank Recovery and Resolution Directive (BRRD).

Regulators have yet to come up with final details for some of these additional regulatory requirements; likewise, the various technical regulatory standards still have to be finalised. To nevertheless facilitate the timely implementation, we have already started to deal with and pursue the various issues in numerous projects – devoting considerable resources to this task.

Sector-specific and business developments

Structured Property Financing segment

Competition in commercial property financing can still be described as intense. We assume that this persistent intense competition will remain intact for the rest of the year. The finance providers are likely to become ever more willing to accept lower margins and higher loan-to-value ratios. This applies for numerous European countries and for North America, as well as for countries in the Asia / Pacific region, including for example, China, Japan and Singapore. Even though the willingness to provide finance should continues to be a little more cautious in the Southern European countries, we can expect further, moderate easing of the lending conditions and an increase in competition for Italy and Spain too in the future.

The providers of finance are likely to remain particularly interested in financing first-class commercial property in the corresponding locations, although the willingness to finance properties with a higher risk profile and large-volume projects will continue to grow noticeably.

Investors currently hold high levels of liquidity. Commercial property represents an attractive investment for investors looking for yield in the current low interest rate environment. We expect this situation will remain largely unchanged for the rest of the year. The resulting demand for commercial property should support property values in numerous markets. We cannot rule out the threat of bubbles on property markets in the course of the low interest rate environment. A muted, slow recovery in many economies and high unemployment in many parts of Europe must be taken into consideration in relation to the future developments on the commercial property markets.[1)]

Against this background, we assume an increase this year in commercial property values on average for most of the European markets that are relevant to us. These increases may vary on average for each country. We consider a sharper rise likely in commercial property values in Germany and the UK, given that they enjoy great popularity among investors and in light of a reasonably positive economic outlook for both nations. The increase in property values in Denmark and Poland might also possibly be stronger this year on account of the good economic prospects. A slight to moderate increase in the average values for commercial property is also likely, in our view, in Belgium, Austria and Switzerland. A corresponding recovery in commercial property prices is also possible in Italy and Spain, with somewhat greater momentum in Spain. In Sweden and France, where only slight economic growth is expected, property values are likely to remain virtually stable on average. Although we assume the same scenario for the Russian commercial property market, the effects on the market of the political tension between Russia and the Ukraine cannot be assessed at present. We anticipate a stable to slightly positive rental development on the aforementioned European commercial property markets. A slight to moderate fall in property values and rents is possible on average in Finland, the Netherlands and Turkey, due to the muted economic development.

Taking the high levels of liquidity and US investor demand into account, together with the positive economic outlook there, a moderate increase in rents and market values for commercial property is likely to be seen during the current year. This also takes into account an anticipated slight increase in US long-term interest rates. We assume property values and rents in Canada to remain stable, and have the same expectation for the commercial property market in Singapore. For Japan, we forecast a markedly positive trend. Considering expected interest rate increases, we adopt a more reticent stance in our assessment for China, assuming less dynamic economic growth by historical standards. Property values are likely to decline moderately on a country average.

The developments outlined above should, in our view, tend to apply to office, retail and logistics property markets. On the hotel markets, we find average earnings indicators that are unchanged from the previous year conceivable in Europe and Asia. However, the forecast takes into consideration a relatively high volatility and deviations on individual markets are probable. With regard to North America, we assume that the upward trend in hotel sector revenues will continue to a moderate extent compared with the previous year.

Investor interest in properties with a higher risk profile is likely to continue to intensify markedly. This should be seen especially in the light of the high level of investor liquidity and the limited number of premium properties. Accordingly, funds are likely to flow far more heavily into markets and properties outside the premium segment.

Macro-economic risks and uncertainty factors will continue to be important for the further development of the commercial property markets. If these factors were to materialise in a way that places a significant burden on forecast economic developments, or the economy even falls into a marked recession, this would likely trigger significant declines in property values and rents.

We have determined our target for new business in line with market conditions on the financing and commercial property markets and expected economic developments, amongst other things. Our target for aggregate new business originated this year is at the upper end of the forecast range between € 8 billion and € 9 billion.

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

We want to continue to use club deals and syndicated financing in the future, to allow us to participate in large-volume financings and to diversify risk.

The acquisition of Corealcredit in particular will significantly increase our property finance portfolio compared with year-end 2013. The regional focus will continue to be on Western Europe and North America; we continue to strive for a broad diversification by region and by property type.

These forecasts are based on the assumption that uncertainty and risks related to the macro-economic environment and the property markets will not materialise to any significant extent – for example, in the form of a deep recession. If this were to happen, new business might be influenced and it could lead to a noticeable reduction in newly-originated loans.

Consulting/Services segment

Bank division Housing Industry

We also anticipate a stable development of the housing and commercial property industries in Germany during the rest of 2014.

Companies will continue to pursue a sustainable development of their portfolios, largely aimed at improving energy efficiency in the properties. At the same time, the conversion of existing housing stock to create affordable housing that is suitable for families or the elderly is becoming increasingly important. Against this background, member companies of the Federation of German Housing Enterprises (GdW) plan to increase investments in their existing properties by close to 11 % this year to almost € 11.4 billion. Only 27 % of the investments are earmarked for new construction projects.

By year-end, we expect the positive trend on the housing market to have remained intact. The increase in the rental and purchase prices is likely to be less dynamic. Rents are likely to rise especially in the secondary locations, since property prices in good locations have probably reached their limits in terms of price.

In view of the low interest rate levels, residential property is becoming more important as solid tangible assets for national and international investors. The limited supply means that demand will focus mainly on the small and medium-sized market segment. Listed companies in particular will continue to be active on the transaction market as investors. The growing trend among investors towards secondary locations with a higher risk profile is expected to continue during the year. Against the background of the ongoing attraction of residential property investments, we anticipate a transaction volume in the region of € 10 billion by the end of the year.

We see good opportunities during 2014 to acquire new clients and to intensify the business relationships with our existing client base. This also applies to the settlement of payment transactions for companies from the utilities and waste disposal industries. In view of the deposit volume, we anticipate consolidation at a high level in relation to current account balances, and see the positive trend continuing in rent deposits. The interest rate levels that are relevant for the result from the deposit-taking business continue to fall. Against this background, we anticipate further pressure on segment results. However, the importance of this business goes way beyond the interest margin generated from the deposits, which is under pressure in the current market environment. This is because the deposits from the housing industry represent a strategically important additional source of funding for Aareal Bank.

Aareon

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

For 2014, Aareon expects significant sales growth and a slight increase in earnings before interest and taxes (EBIT). The acquisition of Sweden's Incit AB in 2013 in particular, the continued migration of GES customers to Wodis Sigma, and strong growth in the international business are decisive factors here.

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

Aareon expects unchanged sales revenues and EBIT in its ERP products segment in 2014, with a strong increase in sales revenues anticipated for the Wodis Sigma product line. This will be achieved largely through migration projects by GES customers. Business in the GES product line during the 2013 financial year was largely characterised by major one-off projects and the implementation of SEPA. Given the non-recurring character of these effects and the continued migration of GES customers to Wodis Sigma, Aareon expects markedly lower product revenues in 2014.

Due to additional consulting projects and application management services, sales revenue for the SAP® solutions and Blue Eagle products is expected to rise slightly.

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

In the International Business segment, significant sales and EBIT growth is expected in 2014, due among other things to the acquisition of Sweden's Incit AB. At the same time, we also forecast a modest to significant increase in sales revenues and results for Aareon's other international subsidiaries.

Overall, Aareon forecasts a marked increase in sales revenues for the next year, with EBIT of around € 28 million, slightly higher year-on-year. The EBIT margin is expected to be around 16 %.

Group targets

We are slightly increasing our original profit forecast of between € 370 million and € 390 million for the 2014 financial year. Thanks to the good business development during the first two quarters of the year, we now see good potential for generating consolidated operating profit at the upper end of a range between € 380 million and € 400 million, including negative goodwill from the acquisition of Corealcredit. Adjusted for the non-recurring effect from the Corealcredit transaction, we expect consolidated operating profit between € 230 million and € 250 million. Excluding said non-recurring effect, return on equity (RoE) before taxes is projected to be around 9 %.

We expect net interest income to be at the upper end of the forecasted € 610 million to € 640 million range. Allowance for credit losses is expected to be in the upper half of a range between € 100 million and € 150 million. As in previous years, the Bank cannot rule out additional allowance for unexpected credit losses that may be incurred during 2014.

Net commission income is projected to be in a range between € 170 million and € 180 million.

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

In the Structured Property Financing segment, we now project new business for the full year 2014 at the upper end of the forecast range between € 8 billion and € 9 billion.

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

Consolidated Financial Statements
Statement of Comprehensive Income

Income Statement

€ mn	Notes	1 Jan-30 Jun 2014	1 Jan-30 Jun 2013
Interest income		484	410
Interest expenses		171	163
Net interest income	1	**313**	**247**
Allowance for credit losses	2	69	45
Net interest income after allowance for credit losses		**244**	**202**
Commission income		94	89
Commission expenses		15	12
Net commission income	3	**79**	**77**
Net result on hedge accounting	4	3	-3
Net trading income/expenses	5	4	11
Results from non-trading assets	6	0	-6
Results from investments accounted for using the equity method		–	–
Administrative expenses	7	216	182
Net other operating income/expenses	8	16	-7
Negative goodwill from the acquisition of Corealcredit	9	152	–
Operating profit		**282**	**92**
Income taxes		41	29
Consolidated net income/loss		**241**	**63**
Allocation of results			
Consolidated net income/loss attributable to non-controlling interests		10	10
Consolidated net income/loss attributable to shareholders of Aareal Bank AG		231	53
Appropriation of profits			
Consolidated net income/loss attributable to shareholders of Aareal Bank AG		231	53
Silent participation by SoFFin		10	10
Consolidated profit/loss		**221**	**43**
€			
Earnings per share		3.87	0.88
Diluted earnings per share		3.87	0.88

Earnings per share are determined by dividing the earnings attributable to ordinary shareholders of Aareal Bank AG by the weighted average of shares outstanding during the reporting period.

Statement of Comprehensive Income

Reconciliation from Consolidated Net Income/Loss to Total Comprehensive Income

€ mn	1 Jan-30 Jun 2014	1 Jan-30 Jun 2013
Consolidated net income/loss	**241**	**63**
Items that will not be reclassified subsequently to profit or loss		
Changes in the reserve from remeasurements of defined benefit plans	**-22**	**–**
Remeasurements	-32	–
Taxes	10	–
Items that are reclassified subsequently to profit or loss		
Changes in revaluation surplus	**44**	**28**
Gains and losses on remeasuring AfS financial instruments	59	36
Reclassifications to the income statement	–	–
Taxes	-15	-8
Changes in hedging reserves	**5**	**1**
Profit/loss from derivatives used to hedge future cash flows	4	1
Reclassifications to the income statement	3	–
Taxes	-2	0
Changes in currency translation reserves	**-1**	**-2**
Profit/loss from translating foreign operations' financial statements	-1	-2
Reclassifications to the income statement	–	–
Taxes	–	–
Other comprehensive income	**26**	**27**
Total comprehensive income	**267**	**90**
Allocation of total comprehensive income		
Total comprehensive income attributable to non-controlling interests	10	10
Total comprehensive income attributable to shareholders of Aareal Bank AG	257	80

Statement of Comprehensive Income

Income Statement (Quarterly Development)

€ mn	Quarter 2 2014	Quarter 2 2013
Interest income	258	206
Interest expenses	89	80
Net interest income	**169**	**126**
Allowance for credit losses	32	28
Net interest income after allowance for credit losses	**137**	**98**
Commission income	46	45
Commission expenses	7	6
Net commission income	**39**	**39**
Net result on hedge accounting	1	0
Net trading income/expenses	2	5
Results from non-trading assets	0	-5
Results from investments accounted for using the equity method	–	–
Administrative expenses	114	90
Net other operating income/expenses	0	-2
Negative goodwill from the acquisition of Corealcredit	–	–
Operating profit	**65**	**45**
Income taxes	21	14
Consolidated net income/loss	**44**	**31**
Allocation of results		
Consolidated net income/loss attributable to non-controlling interests	5	5
Consolidated net income/loss attributable to shareholders of Aareal Bank AG	39	26

Statement of Comprehensive Income

Reconciliation from Consolidated Net Income/Loss to Total Comprehensive Income (Quarterly Development)

€ mn	Quarter 2 2014	Quarter 2 2013
Consolidated net income/loss	**44**	**31**
Items that will not be reclassified subsequently to profit or loss		
Changes in the reserve from remeasurements of defined benefit plans	**-13**	**–**
Remeasurements	-19	–
Taxes	6	–
Items that are reclassified subsequently to profit or loss		
Changes in revaluation surplus	**15**	**8**
Gains and losses on remeasuring AfS financial instruments	20	9
Reclassifications to the income statement	–	–
Taxes	-5	-1
Changes in hedging reserves	**8**	**-1**
Profit/loss from derivatives used to hedge future cash flows	8	-1
Reclassifications to the income statement	3	–
Taxes	-3	–
Changes in currency translation reserves	**-1**	**-2**
Profit/loss from translating foreign operations' financial statements	-1	-2
Reclassifications to the income statement	–	–
Taxes	–	–
Other comprehensive income	**9**	**5**
Total comprehensive income	**53**	**36**
Allocation of total comprehensive income		
Total comprehensive income attributable to non-controlling interests	5	5
Total comprehensive income attributable to shareholders of Aareal Bank AG	48	31

Segment Reporting

Segment Results

	Structured Property Financing		Consulting/ Services		Consolidation/ Reconciliation		Aareal Bank Group	
	1 Jan - 30 Jun 2014	1 Jan - 30 Jun 2013	1 Jan - 30 Jun 2014	1 Jan - 30 Jun 2013	1 Jan - 30 Jun 2014	1 Jan - 30 Jun 2013	1 Jan - 30 Jun 2014	1 Jan - 30 Jun 2013
€ mn								
Net interest income	311	242	0	0	2	5	313	247
Allowance for credit losses	69	45					69	45
Net interest income after allowance for credit losses	**242**	**197**	**0**	**0**	**2**	**5**	**244**	**202**
Net commission income	2	5	80	78	-3	-6	79	77
Net result on hedge accounting	3	-3					3	-3
Net trading income/expenses	4	11					4	11
Results from non-trading assets	0	-6					0	-6
Results from investments accounted for using the equity method								
Administrative expenses	124	97	93	86	-1	-1	216	182
Net other operating income/expenses	15	-6	1	-1	0	0	16	-7
Negative goodwill from the acquisition of Corealcredit Bank AG	152						152	
Operating profit	**294**	**101**	**-12**	**-9**	**0**	**0**	**282**	**92**
Income taxes	45	31	-4	-2			41	29
Consolidated net income/loss	**249**	**70**	**-8**	**-7**	**0**	**0**	**241**	**63**
Allocation of results								
Consolidated net income/loss attributable to non-controlling interests	8	9	2	1			10	10
Consolidated net income/loss attributable to shareholders of Aareal Bank AG	241	61	-10	-8	0	0	231	53
Allocated equity	1,302	1,180	108	89	957	971	2,367	2,240
Cost/income ratio (%)	36.9	40.1	115.0	111.1			52.0	57.1
RoE before taxes (%) [1]	44.0	15.6	-25.7	-23.2			23.0	7.3
Employees (average)	**851**	**739**	**1,638**	**1,539**			**2,489**	**2,278**
Segment assets	**39,938**	**36,938**	**8,670**	**7,404**			**48,608**	**44,342**

[1] On an annualised basis

Segment Reporting

Segment Results (Quarterly Development)

€ mn	Structured Property Financing Quarter 2 2014	Structured Property Financing Quarter 2 2013	Consulting/ Services Quarter 2 2014	Consulting/ Services Quarter 2 2013	Consolidation/ Reconciliation Quarter 2 2014	Consolidation/ Reconciliation Quarter 2 2013	Aareal Bank Group Quarter 2 2014	Aareal Bank Group Quarter 2 2013
Net interest income	168	124	0	0	1	2	169	126
Allowance for credit losses	32	28					32	28
Net interest income after allowance for credit losses	**136**	**96**	**0**	**0**	**1**	**2**	**137**	**98**
Net commission income	1	3	40	39	-2	-3	39	39
Net result on hedge accounting	1	0					1	0
Net trading income/expenses	2	5					2	5
Results from non-trading assets	0	-5					0	-5
Results from investments accounted for using the equity method								
Administrative expenses	68	47	47	44	-1	-1	114	90
Net other operating income/expenses	-1	-2	1	0	0	0	0	-2
Negative goodwill from the acquisition of Corealcredit Bank AG								
Operating profit	**71**	**50**	**-6**	**-5**	**0**	**0**	**65**	**45**
Income taxes	23	15	-2	-1			21	14
Consolidated net income/loss	**48**	**35**	**-4**	**-4**	**0**	**0**	**44**	**31**
Allocation of results								
Consolidated net income/loss attributable to non-controlling interests	4	5	1	0			5	5
Consolidated net income/loss attributable to shareholders of Aareal Bank AG	44	30	-5	-4	0	0	39	26
Allocated equity	1,302	1,180	108	89	957	971	2,367	2,240
Cost/income ratio (%)	39.4	38.2	115.3	110.2			54.0	55.3
RoE before taxes (%) [1]	20.6	15.3	-26.0	-21.0			10.1	7.2

[1] On an annualised basis

Segment Reporting

Consulting/Services Segment – Reconciliation of the Income Statement

Reconciliation of the segment result from the income statement classification aligned to an industrial enterprise to a bank income statement classification (which is used for the purposes of segment reporting)

€ mn			Net interest income	Net commission income	Results from non-trading assets	Results from investments accounted for using the equity method	Administrative expenses	Net other operating income / expenses	Impairment of goodwill	**Operating profit**	Income taxes	**Segment result**
			Income statement classification – bank									
	Q2 2014		0	40			47	1		**-6**	-2	**-4**
	Q2 2013		0	39			44	0		**-5**	-1	**-4**
Income statement classification – industrial enterprise												
Sales revenue	Q2 2014	45		45								
	Q2 2013	44		44								
Own work capitalised	Q2 2014	1					1					
	Q2 2013	1					1					
Changes in inventory	Q2 2014	0						0				
	Q2 2013	0						0				
Other operating income	Q2 2014	2						2				
	Q2 2013	1						1				
Cost of materials purchased	Q2 2014	5		5								
	Q2 2013	5		5								
Staff expenses	Q2 2014	32					32					
	Q2 2013	29					29					
Depreciation, amortisation and impairment losses	Q2 2014	3					3					
	Q2 2013	4					4					
Results from investments accounted for using the equity method	Q2 2014											
	Q2 2013											
Other operating expenses	Q2 2014	14					13	1				
	Q2 2013	13					12	1				
Interest and similar income / expenses	Q2 2014	0	0									
	Q2 2013	0	0									
Operating profit	**Q2 2014**	**-6**	**0**	**40**			**47**	**1**				
	Q2 2013	**-5**	**0**	**39**			**44**	**0**				
Income taxes	Q2 2014	-2									-2	
	Q2 2013	-1									-1	
Segment result	**Q2 2014**	**-4**										
	Q2 2013	**-4**										

Statement of Financial Position

€ mn	Notes	30 Jun 2014	31 Dec 2013
Assets			
Cash funds		128	1,222
Loans and advances to banks	10	3,366	2,531
Loans and advances to customers	11	29,909	25,924
Allowance for credit losses	12	-416	-361
Positive market value of derivative hedging instruments		2,284	1,838
Trading assets	13	389	307
Non-trading assets	14	11,858	10,668
Investments accounted for using the equity method		1	1
Intangible assets	15	106	107
Property and equipment	16	97	98
Income tax assets		54	24
Deferred tax assets		231	110
Other assets	17	601	512
Total		**48,608**	**42,981**
Equity and liabilities			
Liabilities to banks	18	2,503	1,589
Liabilities to customers	19	27,643	25,476
Certificated liabilities	20	10,820	10,124
Negative market value of derivative hedging instruments		2,098	1,603
Trading liabilities	21	528	286
Provisions	22	640	289
Income tax liabilities		120	36
Deferred tax liabilities		6	9
Other liabilities	23	126	203
Subordinated capital	24	1,471	916
Equity	25, 26, 27		
Subscribed capital		180	180
Capital reserves		721	721
Retained earnings		1,289	1,112
Other reserves		-79	-105
Silent participation by SoFFin		300	300
Non-controlling interests		242	242
Total equity		2,653	2,450
Total		**48,608**	**42,981**

Statement of Changes in Equity

				Other reserves							
€ mn	Subscribed capital	Capital reserves	Retained earnings	Reserve from defined benefit plans	Revaluation surplus	Hedging reserves	Currency translation reserves	Silent participation by SoFFin	Total	Non-controlling interest	Equity
Equity as at 1 Jan 2014	**180**	**721**	**1,112**	**-40**	**-50**	**-17**	**2**	**300**	**2,208**	**242**	**2,450**
Total comprehensive income for the period			231	-22	44	5	-1		257	10	267
Payments to non-controlling interests										-10	-10
Dividends			-45						-45		-45
Silent participation by SoFFin											
Costs associated with the silent participation by SoFFin			-10						-10		-10
Other changes			1						1		1
Equity as at 30 Jun 2014	**180**	**721**	**1,289**	**-62**	**-6**	**-12**	**1**	**300**	**2,411**	**242**	**2,653**

				Other reserves							
€ mn	Subscribed capital	Capital reserves	Retained earnings	Reserve from defined benefit plans	Revaluation surplus	Hedging reserves	Currency translation reserves	Silent participation by SoFFin	Total	Non-controlling interest	Equity
Equity as at 1 Jan 2013	**180**	**721**	**1,020**	**-39**	**-99**	**-13**	**4**	**300**	**2,074**	**243**	**2,317**
Total comprehensive income for the period			53		28	1	-2		80	10	90
Payments to non-controlling interests										-10	-10
Dividends											
Silent participation by SoFFin											
Costs associated with the silent participation by SoFFin			-10						-10		-10
Other changes											
Equity as at 30 Jun 2013	**180**	**721**	**1,063**	**-39**	**-71**	**-12**	**2**	**300**	**2,144**	**243**	**2,387**

Statement of Cash Flows (condensed)

€ mn	2014	2013
Cash and cash equivalents as at 1 January	**1,222**	**3,667**
Cash flow from operating activities	-1,450	-350
Cash flow from investing activities	-144	1,055
Cash flow from financing activities	500	-22
Total cash flow	**-1,094**	**683**
Effect of changes in exchange rates	0	0
Cash and cash equivalents as at 30 June	**128**	**4,350**

Notes (condensed)

Basis of Accounting

Legal framework

Aareal Bank AG is a listed public limited company incorporated under German law, with its registered office in Wiesbaden, Germany. It is the parent company of an international property finance and services group.

This half-yearly financial report for the period ended 30 June 2014 was prepared pursuant to the provisions of section 37w in conjunction with section 37y no. 2 of the German Securities Trading Act (Wertpapierhandelsgesetz – "WpHG"). It comprises the present interim condensed consolidated financial statements, as well as an interim group management report (see Group Management Report), and was approved for publication by the Management Board on 5 August 2014.

Aareal Bank AG prepares its condensed interim consolidated financial statements in accordance with International Financial Reporting Standards (IFRSs) applicable within the European Union (EU) as at the reporting date, in connection with the provisions pursuant to section 315a (1) of the German Commercial Code (Handelsgesetzbuch – "HGB"). In particular, the interim consolidated financial statements comply with the requirements for interim financial reporting set out in IAS 34. The reporting currency is the euro (€).

Reporting entity structure

Subsidiaries of Aareal Bank AG are included in the consolidated financial statements by way of full consolidation. Companies over which Aareal Bank AG may exercise a significant influence ("associates") are included in the consolidated financial statements, using the equity method.

Aareal Finanz- und IT Beteiligungen GmbH (formerly Aareal IT Beteiligungen GmbH), Wiesbaden, a subsidiary of Aareal Bank AG, acquired all of the shares of COREALCREDIT BANK AG (Corealcredit), Frankfurt/Main, which specialises in commercial property financing in Germany. A corresponding agreement was concluded on 22 December 2013 with the previous owner, a fund owned by financial investor Lone Star (seller). The (provisional) cash purchase price amounted to € 343 million. The closing was completed after the approval of the respective authorities and the fulfilment of additional conditions as at 31 March 2014. Accordingly, Aareal Bank Group obtained control over Corealcredit and included the acquired company in the consolidated financial statements of Aareal Bank Group as at 31 March 2014 (date of initial consolidation).

Through the acquisition of Corealcredit, Aareal Bank exploited an attractive opportunity for external growth at a favourable point in time. With this transaction, Aareal Bank further expands its position as one of the leading specialists in commercial property financing. The reasons for the business combination also include optimising the allocation of equity capital as well as realising potential synergies which result from the combination of both companies, due to their very similar business models.

In accordance with IFRS 3, all identifiable assets and liabilities of the acquired entity have to be measured at their fair value at the time of acquisition (closing). These fair values also represent the amounts recognised upon initial consolidation. The excess of the net assets (i.e. the balance of assets and liabilities acquired and measured at fair value) over the (preliminary) purchase price paid is recognised as a day-one gain (negative Goodwill) in the income statement and directly increases the equity of Aareal Bank Group. This income currently amounts to € 152 million and is reported in the statement of comprehensive income in a separate item. This income primarily results from the utilisation of a favourable market environment for such transactions.

Since the transaction was completed only at the end of the first quarter 2014, the allocation of the purchase price in accordance with IFRS 3 and the related determination of the fair values for assets acquired and liabilities assumed are still provisional. There have been no material adjustments to the purchase price allocation since the date of initial consolidation. The final determination of fair values may yet give rise to material adjustments.

The following overview shows the preliminary purchase price allocation in accordance with IFRS 3 at the time of acquisition:

€ mn	Fair value as at 31 Mar 2014 (preliminary)
Cash funds	9
Loans and advances to banks	880
Loans and advances to customers	3,247
Allowance for credit losses (portfolio-based)	-17
Positive fair values of derivative hedging instruments and trading assets	150
Non-trading assets	1,393
Intangible assets	2
Property and equipment	1
Income tax assets	30
Deferred tax assets	152
Other assets	105
Total assets acquired	**5,952**
Liabilities to banks	1,280
Liabilities to customers	2,024
Certificated liabilities	1,143
Negative fair values of derivative hedging instruments and trading liabilities	387
Provisions incl. contingent liabilities	371
Income tax liabilities	101
Other liabilities	14
Subordinated capital	137
Total liabilities assumed	**5,457**
Total net assets acquired	**495**
Negative goodwill	152
(Preliminary) purchase price paid	**343**

Taking into consideration the (provisional) purchase price of € 343 million paid, the transaction led to an increase of total net assets as shown in the statement of financial position in the amount of the negative goodwill (currently € 152 million).

The costs associated with the business combination amounted to € 9 million and were recognised as administrative expenses, predominantly in the 2013 financial year.

Within the scope of the acquisition of Corealcredit, Aareal Bank assumed legal, tax and credit risks. These risks were assessed on a conservative basis and have been hedged comprehensively in the financial statements. The obligations in connection with the risks assumed are recognised in the statement of financial position at fair value, in line with the related claims for reimbursement or recourse. Accordingly, recognition and measurement in the IFRS consolidated financial statements differ from recognition and measurement in the financial statements of Corealcredit prepared under the German Commercial Code. In the consolidated statement of financial position, the obligations respectively the claims for reimbursement or recourse are reported under Provisions and Income tax liabilities respectively Other assets.

The fair value of the claims for reimbursement or recourse existing to the seller as well as to third parties in relation to tax and legal risks amounted to € 79 million as at the acquisition date. The seller provided cash collateral in the amount of € 50 million to cover individual credit risks.

Ongoing litigation mainly refers to legal actions initiated by holders of profit-participation certificates of Corealcredit in relation to loss assumption in the past, which – according to the plaintiffs – was unjustified. This has led to strongly reduced repayments compared to the nominal receivables at final maturity of the profit-participation certificates. Tax risks relate to risks from ongoing tax audits.

In the case of a positive outcome of the current legal disputes from the perspective of Aareal Bank AG, there may be compensation payments to the seller in the amount of 0 to € 73 million, which would lead to a utilisation of the provisions recognised for this purpose with no effect on profit or loss. Concerning the part of the credit portfolio that was acquired subject to credit-related purchase price discounts, compensation payments to the seller may occur in the future, in the amount of 0 to € 97 million plus interest with no effect on profit or loss. The potential level of such compensation payments largely corresponds to the surplus amount of future borrower payments relative to the carrying amount of the corresponding accounts receivable. The fair value of the contingent considerations as at 30 June 2014 amounts to € 9 million.

The measurement of legal, tax and credit risks is subject to several uncertainties. With regard to legal risks, there is a lack of comparable legal proceedings, among others. As far as tax risks are concerned, there was discussion with tax audit on the assessment of underlying facts. The assessment of risks often requires significant estimates made by the management. The final amount of the cash outflows may deviate significantly from the measurement previously made in accounting. The time period and the actual amount of any potential cash outflows in connection with liabilities assumed cannot be determined exactly. It is expected that the majority of cash outflows will occur until year-end 2017.

The fair value of the accounts receivable acquired as part of the business combination amounts to € 4.1 billion as at 31 March 2014, comprising € 3.2 billion in loans and advances to customers and € 0.9 billion in loans and advances to banks. The gross amount of these receivables' contractually agreed cash flows amounted to € 4.7 billion, of which € 3.7 billion relate to loans and advances to customers and € 1.0 billion to loans and advances to banks. € 97 million of contractually-agreed cash flows from these loans and advances to customers are considered uncollectable.

The effects on the income statement of the present interim consolidated financial statements are € 18 million in interest income and € 4 million in operating profit which are both attributable to Corealcredit. If the business combination would have taken effect at the beginning of the period under review, Aareal Bank Group would probably have reported additional interest income in the amount of approximately € 17 million as well as additional operating profit of approximately € 3 million.

Accounting policies

Unless specifically indicated otherwise, the accounting policies applied in the preparation of the consolidated financial statements 2013 were also applied in the preparation of these condensed interim consolidated financial statements, including the calculation of comparative figures.

The following financial reporting standards (IASs/IFRSs) and interpretations (SICs and IFRICs) were required to be applied for the first time in the reporting period:

IFRS 10, IFRS 11, IFRS 12, IAS 27 and IAS 28

IFRS 10 replaces the guidance on control and consolidation included in IAS 27 Consolidated and Separate Financial Statements and SIC-12 Consolidation – Special Purpose Entities. The standard changes the definition of "control". According to the new definition, the same criteria are applied to all companies to determine whether a company controls an investee. The amendments to IFRS 10, which relate to investment entities, introduce new rules regarding the inclusion of controlled subsidiaries at investment entities. The application of IFRS 10 did not have any effects on the reporting entity structure of Aareal Bank in the reporting period.

IFRS 11 replaces IAS 31 Interests in Joint Ventures and SIC-13 Jointly Controlled Entities – Non-Monetary Contributions by Venturers that previously was applicable to the accounting for joint ventures. IFRS 11 governs the accounting for situations in which a company has joint control over a joint venture or a joint operation. The new standard eliminates the proportionate consolidation of joint ventures. In future, joint ventures will have to be accounted for using the equity method. In case of a joint operation, assets, liabilities, income and expenses directly attributable to the joint operator have to be recorded in the consolidated financial statements of that joint operator. The first-time application of IFRS 11 did not result in any adjustments required to be recorded within Aareal Bank Group.

IFRS 12 clarifies the disclosures required to be made by companies that apply the new standards IFRS 10 Consolidated Financial Statements and IFRS 11 Joint Arrangements. This standard replaces the disclosure requirements currently included in IAS 27, IAS 28 and IAS 31. The disclosure obligations set out in IFRS 12 are required to be applied to the fullest extent as at 31 December 2014.

Amendments to IAS 32 – Offsetting Financial Assets and Financial Liabilities

The amendments clarify some details in relation to offsetting financial assets and financial liabilities. As before, financial assets and financial liabilities are offset only when a company has a legally enforceable right to set off, and intends either to settle on a net basis or to realise the asset and settle the related liability simultaneously. The clarifications do not have any impact on the financial statements of Aareal Bank Group.

Novation of Derivatives and Continuation of Hedge Accounting (Amendments to IAS 39)

The amendments to IAS 39 provide companies relief from provisions related to the discontinuation of hedge accounting. Changes to derivative contracts required as a result of the introduction new laws or regulations, such as a switch to a central clearing counterparty, do not lead to a discontinuation of the hedging relationship in accordance with IAS 39. The amendments to IAS 39 have not had any material consequences for the financial statements of Aareal Bank Group.

IFRIC 21

IFRIC 21 Levies is an interpretation of IAS 37 Provisions, Contingent Liabilities and Contingent Assets and states that a company recognises levies imposed by government not until the activity that gives rise to a levy by law has occurred. The first-time application of IFRIC 21 does not have any impact on the financial statements of Aareal Bank Group.

The new and revised standards and interpretations do not have any additional material consequences for the consolidated financial statements of Aareal Bank Group.

Notes to the Statement of Comprehensive Income

(1) Net interest income

€ mn	1 Jan-30 Jun 2014	1 Jan-30 Jun 2013
Interest income from		
Property loans	386	321
Public-sector loans	7	9
Other lending and money market operations	43	29
Debt and other fixed-income securities	48	51
Current dividend income	0	0
Total interest income	**484**	**410**
Interest expenses for		
Bonds issued	55	52
Registered mortgage bonds	17	13
Promissory note loans	41	45
Subordinated capital	16	11
Term deposits	20	29
Payable on demand	14	13
Other interest expenses	8	0
Total interest expenses	**171**	**163**
Total	**313**	**247**

(2) Allowance for credit losses

€ mn	1 Jan-30 Jun 2014	1 Jan-30 Jun 2013
Additions	101	46
Reversals	30	3
Direct write-offs	2	5
Recoveries on loans and advances previously written off	4	3
Total	**69**	**45**

The additions to the allowance for credit losses include an amount of € 30 million related to the recognition of portfolio-based valuation allowances. The recognition of these valuation allowances is attributable, among others, to a change in measurement parameters used for the determination of the portfolio-based valuation allowance and, to that extent, is largely a one-off effect. Our forecast for the entire financial year (€ 100-150 million) is not affected by this one-off effect. Please also refer to our explanations in Note (12).

(3) Net commission income

€ mn	1 Jan-30 Jun 2014	1 Jan-30 Jun 2013
Commission income from		
Consulting and other services	86	80
Trustee loans and administered loans	1	1
Securities transactions	–	–
Other lending and money market operations	4	5
Other commission income	3	3
Total commission income	**94**	**89**
Commission expenses for		
Consulting and other services	11	10
Securities transactions	1	0
Securitisation transactions	0	–
Other lending and money market transactions	1	0
Other commission expenses	2	2
Total commission expenses	**15**	**12**
Total	**79**	**77**

Commissions from consulting and services primarily include commissions for IT services.

(4) Net result on hedge accounting

€ mn	1 Jan-30 Jun 2014	1 Jan-30 Jun 2013
Ineffective portion of fair value hedges	0	-3
Ineffective portion of cash flow hedges	3	0
Ineffective portion of net investment hedges	0	0
Total	**3**	**-3**

(5) Net trading income/expenses

€ mn	1 Jan-30 Jun 2014	1 Jan-30 Jun 2013
Net income/expenses from positions held for trading	5	10
Currency translation	-1	1
Total	**4**	**11**

Net trading income/expenses was primarily attributable to the measurement of derivatives used to hedge interest rate and currency risks.

(6) Results from non-trading assets

€ mn	1 Jan-30 Jun 2014	1 Jan-30 Jun 2013
Result from debt securities and other fixed-income securities	0	-4
of which: Loans and receivables (LaR)	0	-4
Available for sale (AfS)	–	–
Result from equities and other non-fixed income securities	0	-2
of which: Available for sale (AfS)	0	–
Designated as at fair value through profit or loss (dFVtPL)	0	-2
Results from equity investments (AfS)	0	–
Total	**0**	**-6**

(7) Administrative expenses

€ mn	1 Jan-30 Jun 2014	1 Jan-30 Jun 2013
Staff expenses	124	111
Other administrative expenses	82	61
Depreciation, amortisation and impairment of property and equipment and intangible assets	10	10
Total	**216**	**182**

(8) Net other operating income/expenses

€ mn	1 Jan-30 Jun 2014	1 Jan-30 Jun 2013
Income from properties	7	9
Income from goods and services	1	1
Miscellaneous	26	6
Total other operating income	**34**	**16**
Expenses for properties	7	3
Expenses for services used	0	0
Write-downs of trade receivables	0	0
Expenses for other taxes	2	1
Miscellaneous	9	19
Total other operating expenses	**18**	**23**
Total	**16**	**-7**

Miscellaneous other operating income includes one-off income in the amount of € 18 million from the reversal of provisions for settlement risks.

(9) Negative goodwill from the acquisition of Corealcredit

Further information is included in the section ”Reporting entity structure“ in the notes to the consolidated financial statements.

Notes to the Statement of Financial Position

(10) Loans and advances to banks

€ mn	30 Jun 2014	31 Dec 2013
Money market receivables	1,482	2,373
Promissory note loans	149	122
Securities repurchase agreements	1,710	–
Other loans and advances	25	36
Total	**3,366**	**2,531**

Loans and advances to banks are allocated to the measurement category "Loans and receivables" (LaR).

The increase in loans and advances to banks mainly results from the consolidation of Corealcredit as at 31 March 2014. In connection with the assets acquired and liabilities assumed within the context of the acquisition of the company, please refer to our statements in the section "Reporting entity structure" in the notes to the consolidated financial statements.

(11) Loans and advances to customers

€ mn	30 Jun 2014	31 Dec 2013
Property loans	27,622	23,848
Promissory note loans	1,489	1,435
Other loans and advances	798	641
Total	**29,909**	**25,924**

Loans and advances to customers are allocated to the measurement category "Loans and receivables" (LaR).

The increase in property loans mainly results from the consolidation of Corealcredit as at 31 March 2014. In connection with the assets acquired and liabilities assumed within the context of the acquisition of the company, please refer to our statements in the section "Reporting entity structure" in the notes to the consolidated financial statements.

(12) Allowance for credit losses

30 June 2014

€ mn	Specific valuation allowances	Portfolio impairment allowance	Total allowance for credit losses for recognised items	Provisions in the lending business for unrecognised items	Total allowance for credit losses and provisions in the lending business
Allowance for credit losses as at 1 January	**296**	**65**	**361**	**10**	**371**
Additions	71	30	**101**	0	**101**
Write-downs	27	–	**27**	–	**27**
Reversals	29	0	**29**	1	**30**
Unwinding	7	–	**7**	–	**7**
Changes in basis of consolidation	–	17	**17**	3	**20**
Currency adjustments	0	0	**0**	0	**0**
Balance as at 30 June	**304**	**112**	**416**	**12**	**428**

31 December 2013

€ mn	Specific valuation allowances	Portfolio impairment allowance	Total allowance for credit losses for recognised items	Provisions in the lending business for unrecognised items	Total allowance for credit losses and provisions in the lending business
Allowance for credit losses as at 1 January	**218**	**84**	**302**	**18**	**320**
Additions	151	–	**151**	0	**151**
Write-downs	50	–	**50**	3	**53**
Reversals	9	19	**28**	5	**33**
Unwinding	12	–	**12**	–	**12**
Changes in basis of consolidation	–	–	**–**	–	**–**
Currency adjustments	-2	0	**-2**	–	**-2**
Balance as at 31 December	**296**	**65**	**361**	**10**	**371**

The allowance for risks associated with unrecognised items relates to loans and advances to customers and loans and advances to banks classified as "Loans and receivables" (LaR). These allowances are reported under allowance for credit losses on the asset side of the statement of financial position. The provisions recognised for risks associated with unrecognised items relate to contingent liabilities and loan commitments. These provisions are reported under provisions on the liability side of the statement of financial position.

The addition to the portfolio-based valuation allowance (additions) is mainly attributable to a harmonisation related to the inclusion of the so-called LIP factor (LIP – Loss Identification Period). While previously different LIP factors were used for each exposure class in the context of the determination of the portfolio-based valuation allowance until 31 December 2013, the LIP factor was generally harmonised to 1 for all exposure classes as at 31 March 2014. The effect from the adjustment of the LIP factor amounts to € 35 million. The forecast in relation to the allowance for credit losses for the entire financial year (€ 100-150 million) is not affected by this.

The increase in the balance of portfolio-based valuation allowances (changes in basis of consolidation) results from the initial consolidation of Corealcredit as at 31 March 2014. In connection with the assets acquired and liabilities assumed within the context of the acquisition of the company, please refer to our statements in the section „Reporting entity structure“ in the notes to the consolidated financial statements.

(13) Trading assets

€ mn	30 Jun 2014	31 Dec 2013
Positive market value of trading assets	389	307
Total	**389**	**307**

Trading assets are allocated to the measurement category "Held for trading" (HfT). They are mainly used to hedge economic market price risks.

(14) Non-trading assets

€ mn	30 Jun 2014	31 Dec 2013
Debt and other fixed-income securities	11,836	10,647
of which: Loans and receivables (LaR)	4,185	4,259
Held to maturity (HtM)	1,099	–
Available for sale (AfS)	6,552	6,388
Equities and other non-fixed income securities	20	20
of which: Available for sale (AfS)	20	20
Designated as at fair value through profit or loss (dFVtPL)	–	–
Interests in affiliated companies (AfS)	–	–
Other investments (AfS)	2	1
Total	**11,858**	**10,668**

The item "Debt and other fixed-income securities" mainly consists of public-sector bonds as well as asset-covered bonds (Pfandbriefanleihen) and bank bonds.

This rise in debt and other fixed-income securities mainly results from the consolidation of Corealcredit as at 31 March 2014. In connection with the assets acquired and liabilities assumed within the context of the acquisition of the company, please refer to our statements in the section "Reporting entity structure" in the notes to the consolidated financial statements.

(15) Intangible assets

€ mn	30 Jun 2014	31 Dec 2013
Goodwill	66	66
Proprietary software	13	14
Other intangible assets	27	27
Total	**106**	**107**

(16) Property and equipment

€ mn	30 Jun 2014	31 Dec 2013
Land and buildings and construction in progress	76	77
Office furniture and equipment	21	21
Total	**97**	**98**

(17) Other assets

€ mn	30 Jun 2014	31 Dec 2013
Properties	425	413
Trade receivables (LaR)	28	34
Miscellaneous	148	65
Total	**601**	**512**

(18) Liabilities to banks

€ mn	30 Jun 2014	31 Dec 2013
Money market liabilities	1,662	838
Promissory note loans	381	385
Registered mortgage Pfandbriefe	344	254
Registered public-sector Pfandbriefe	44	46
Other liabilities	72	66
Total	**2,503**	**1,589**

Liabilities to banks are allocated to the measurement category "Liabilities measured at amortised cost" (LaC).

The increase in money-market liabilities mainly results from the consolidation of Corealcredit Bank AG as at 31 March 2014. In connection with the assets acquired and liabilities assumed within the context of the acquisition of the company, please refer to our statements in the section "Reporting entity structure" in the notes to the consolidated financial statements.

(19) Liabilities to customers

€ mn	30 Jun 2014	31 Dec 2013
Money market liabilities	12,715	11,779
Promissory note loans	8,289	7,802
Registered mortgage Pfandbriefe	3,582	3,186
Registered public-sector Pfandbriefe	3,057	2,709
Total	**27,643**	**25,476**

Liabilities to customers are allocated to the measurement category "Liabilities measured at amortised cost" (LaC).

The increase in liabilities to customers mainly results from the consolidation of Corealcredit as at 31 March 2014. In connection with the assets acquired and liabilities assumed within the context of the acquisition of the company, please refer to our statements in the section „Reporting entity structure" in the notes to the consolidated financial statements.

(20) Certificated liabilities

€ mn	30 Jun 2014	31 Dec 2013
Bearer mortgage Pfandbriefe	8,163	7,179
Bearer public-sector Pfandbriefe	30	35
Other debt securities	2,627	2,910
Total	**10,820**	**10,124**

Certificated liabilities are allocated to the measurement category "Liabilities measured at amortised cost" (LaC).

The increase in bearer mortgage Pfandbriefe mainly results from the consolidation of Corealcredit. In connection with the assets acquired and liabilities assumed within the context of the acquisition of the company, please refer to our statements in the section "Reporting entity structure" in the notes to the consolidated financial statements.

(21) Trading liabilities

€ mn	30 Jun 2014	31 Dec 2013
Negative market value of trading assets	528	286
Total	**528**	**286**

Trading liabilities are allocated to the measurement category "Held for trading" (HfT). They are mainly used to hedge economic market price risks.

The increase in trading liabilities mainly results from the consolidation of Corealcredit. In connection with the assets acquired and liabilities assumed within the context of the acquisition of the company, please refer to our statements in the section "Reporting entity structure" in the notes to the consolidated financial statements.

(22) Provisions

€ mn	30 Jun 2014	31 Dec 2013
Provisions for pensions and similar obligations	250	148
Other liabilities, including contingent liabilities 1)	390	141
Total	**640**	**289**

1) The contingent liabilities assumed in the context of the acquisition of Corealcredit pursuant to IFRS 3.23 amounted to € 37 million as at 30 June 2014 (date of initial consolidation: 31 March 2014: € 38 million).

The increase in provisions for pensions and similar obligations as well as the increase in other provisions mainly results from the consolidation of Corealcredit. In connection with the provisions and contingent liabilities assumed and recognised within the context of the acquisition of the company, please refer to our statements in the section „Reporting entity structure“ in the notes to the consolidated financial statements.

(23) Other liabilities

€ mn	30 Jun 2014	31 Dec 2013
Liabilities from outstanding invoices	5	8
Deferred income	12	11
Liabilities from other taxes	21	29
Trade payables (LaC)	17	9
Other liabilities (LaC)	71	146
Other liabilities	**126**	**203**

(24) Subordinated capital

€ mn	30 Jun 2014	31 Dec 2013
Subordinated liabilities	1,113	524
Profit-participation certificates	166	166
Contributions by silent partners [1]	192	226
Total	**1,471**	**916**

[1] The silent participation by SoFFin is classified as equity in accordance with IFRSs; it is therefore not reported under contributions by silent partners, but as a separate item in equity.

Items of subordinated capital are allocated to the measurement category ”Liabilities measured at amortised cost“ (LaC).

The Bank issued subordinated liabilities in the nominal amount of € 0.5 billion during the period under review.

The increase in subordinated liabilities also is due in part to the consolidation of Corealcredit. In connection with the assets acquired and liabilities assumed within the context of the acquisition of the company, please refer to our statements in the section ”Reporting entity structure“ in the notes to the consolidated financial statements.

(25) Equity

€ mn	30 Jun 2014	31 Dec 2013
Subscribed capital	180	180
Capital reserves	721	721
Retained earnings	1,289	1,112
Other reserves		
Reserve from remeasurements of defined benefit plans	-62	-40
Revaluation reserve	-6	-50
Hedging reserves	-12	-17
Currency translation reserves	1	2
Silent participation by SoFFin	300	300
Non-controlling interests	242	242
Total	**2,653**	**2,450**

(26) Treasury shares

No treasury shares were held during the period under review.

(27) Dividends

The Annual General Meeting of Aareal Bank AG on 21 May 2014 resolved to pay a dividend of € 0.75 per no-par value share, totalling € 44,892,915.75, from net retained profit (Bilanzgewinn) of € 49,892,915.75 as reported under the German Commercial Code (HGB) for the financial year 2013. The Annual General Meeting also resolved to transfer the remaining distributable profit of € 5,000,000.00 to other retained earnings.

Within Aareal Bank Group's consolidated statement of financial position, a dividend payment reduces the retained earnings item within consolidated equity.

Reporting on Financial Instruments

(28) Presentation of the fair value hierarchy in accordance with IFRS 13

The following table shows the carrying amounts of financial instruments held by Aareal Bank Group which are reported at fair value in the statement of financial position, according to the three-tier fair value hierarchy pursuant to IFRS 13.72 et seq. The classification into the individual hierarchy levels is based on the inputs used for fair value measurement.

30 June 2014

€ mn	Fair value total	Fair value level 1	Fair value level 2	Fair value level 3
Positive market value of derivative hedging instruments	**2,284**	**–**	**2,284**	**–**
Assets held for trading	**389**	**–**	**389**	**–**
Trading derivatives	389	–	389	–
Non-trading assets available for sale	**6,572**	**6,492**	**80**	**–**
Fixed-income securities	6,552	6,489	63	–
Equities/funds	20	3	17	–
Negative market value of derivative hedging instruments	**2,098**	**–**	**2,098**	**–**
Liabilities held for trading	**528**	**–**	**528**	**–**
Trading derivatives	528	–	528	–

31 December 2013

€ mn	Fair value total	Fair value level 1	Fair value level 2	Fair value level 3
Positive market value of derivative hedging instruments	**1,838**	**–**	**1,838**	**–**
Assets held for trading	**307**	**–**	**307**	**–**
Trading derivatives	307	–	307	–
Non-trading assets available for sale	**6,408**	**6,318**	**90**	**–**
Fixed-income securities	6,388	6,315	73	–
Equities/funds	20	3	17	–
Negative market value of derivative hedging instruments	**1,603**	**–**	**1,603**	**–**
Liabilities held for trading	**286**	**–**	**286**	**–**
Trading derivatives	286	–	286	–

The fair value of financial instruments is allocated to Level 1 of the fair value hierarchy if it is determined on the basis of unadjusted quoted prices in active markets for identical assets or liabilities. The determination of the fair value is based on the principal market for the asset or liability or, in the absence of a principal market, the most advantageous market for the asset or liability. Another factor to be taken into account is whether Aareal Bank can enter into a transaction for the relevant asset or liability at the price in that market at the measurement date.

Fair values determined using inputs other than quoted prices included within Level 1 that are observable for the financial instrument, either directly or indirectly, are included in Level 2 of the fair value hierarchy. Financial instruments whose fair value is allocated to Level 2 of the fair value hierarchy are measured using various valuation techniques.

In case of fixed-income securities or equities for which no current market price is available, the fair value is determined on the basis of comparable market prices to the extent possible. To this end, quoted prices on active markets for largely identical or quoted prices on inactive markets for identical or similar securities are used by adjusting the last available market price or the current fair value of another largely identical instrument, to take into account any changes in risk or new information known as at the measurement date. In the absence of comparable market prices for securities, they are measured through an analysis of future payments using the fully-capitalised earnings value approach, where the inputs are based on observable market data. These approaches include the discounted cash flow (DCF) method which is used to determine the present value of contractual cash flows until the expected end of the term. The present value is determined based on the benchmark curve applicable for the relevant market, taking into account mark-ups based on credit quality and liquidity. The valuation model used for options included in the transaction is the commonly used Black-Scholes model or appropriate numerical procedures.

The fair value of OTC derivatives included in the trading portfolio as well as of OTC hedging derivatives is determined on the basis of sector-specific standardised measurement models, such as the present value method or option pricing models. These techniques are based on inputs quoted on active markets, such as interest rates, yield curves and credit spreads. The fair value of foreign exchange forwards is generally based on current forward exchange rates quoted on active markets. Fair values determined using valuation techniques where one or more material inputs are not based on observable market data are assigned to Level 3 of the fair value hierarchy. Products that are allocated to this level are currently not held by Aareal Bank Group.

In the first half of 2014, there were no transfers between the hierarchy levels for the various financial instruments.

Aareal Bank reviews the allocation of a financial instrument in the fair value hierarchy on the previous year's balance sheet date of the preceding quarter in comparison with the allocation on the current reporting date, to determine whether reclassifications occurred between the individual levels of the fair value hierarchy. The date for recognising reclassifications into the hierarchy levels and for recognising reclassifications from the hierarchy levels is the same.

(29) Comparison of carrying amounts and fair values of the financial instruments

The following table is a comparison of the fair values of the financial instruments with their carrying amounts. The presentation is made for each class of financial instrument:

€ mn	Carrying amount 30 Jun 2014	Fair value 30 Jun 2014	Carrying amount 31 Dec 2013	Fair value 31 Dec 2013
Cash on hand and balances with central banks	**128**	**128**	**1,222**	**1,222**
Loans and advances to banks (LaR)	3,366	3,366	2,531	2,530
Loans and advances to customers (LaR)	29,492	31,270	25,563	27,298
Non-trading assets (LaR)	4,185	4,008	4,259	4,018
Other assets (LaR)	92	83	62	67
Total loans and receivables	**37,135**	**38,727**	**32,415**	**33,913**
Non-trading assets held to maturity	**1,099**	**1,100**	**–**	**–**
Non-trading assets available for sale	**6,572**	**6,572**	**6,409**	**6,409**
Positive market value of derivative hedging instruments	**2,284**	**2,284**	**1,838**	**1,838**
Assets held for trading	**389**	**389**	**307**	**307**
Liabilities to banks (LaC)	2,503	2,516	1,589	1,601
Liabilities to customers (LaC)	27,643	27,630	25,476	25,412
Certificated liabilities (LaC)	10,820	10,910	10,124	10,192
Other liabilities (LaC)	93	98	163	156
Subordinated capital (LaC)	1,471	1,516	916	914
Total liabilities measured at amortised cost	**42,530**	**42,670**	**38,268**	**38,275**
Negative market value of derivative hedging instruments	**2,098**	**2,098**	**1,603**	**1,603**
Liabilities held for trading	**528**	**528**	**286**	**286**
Financial guarantee contracts	**85**	**85**	**120**	**120**
Loan commitments	**1,331**	**1,331**	**1,852**	**1,852**

(30) Day-One Profit or Loss

Aareal Bank Group has entered into transactions that were not effected on the principal market or the most advantageous market for the asset or liability concerned. In these cases the transaction price does not correspond to the fair value of the asset or liability, because the determination of the fair value using a valuation technique which assumes a transaction on a principal market results in a fair value that deviates from the transaction price. The financial instruments are carried at the transaction price upon initial recognition. The difference between the transaction price and the fair value measured based on the valuation model (the so-called day-one profit or loss) is amortised over the term of the transaction in the income statement, since the fair value of these financial instruments of the trading portfolio is determined using valuation models whose inputs are not fully based on observable market factors.

The table below shows the development of the day-one profit during the quarter under review. The day-one profit is recognised as an item to be deducted from the carrying amount of trading assets:

€ mn	2014	2013
Balance as at 1 January	**27**	**10**
Additions from new transactions	7	12
Reversals through profit or loss in the period	4	2
Changes in basis of consolidation	9	–
Balance as at 30 June	**39**	**20**

(31) Reclassification of financial assets

In 2008 and 2009, Aareal Bank Group took advantage of the opportunity to reclassify financial assets into another measurement category. Specifically, securities with an aggregate volume of € 6.2 billion were reclassified from the IFRS measurement categories "Available for sale" (AfS) and "Held for trading" (HfT), to "Loans and receivables" (LaR). In all cases, we opted for reclassification since there was no longer an active market for the securities concerned (in spite of their good quality), and due to our intention to hold these issues for a longer term. Depending on prevailing market conditions, Aareal Bank Group may use this reclassification option again in the future.

The following table compares the carrying amounts of the reclassified assets to their fair values:

€ mn	Carrying amount 30 Jun 2014	Fair value 30 Jun 2014	Carrying amount 31 Dec 2013	Fair value 31 Dec 2013
from AfS to LaR	**3,806**	**3,611**	**3,849**	**3,600**
Asset-backed securities	26	27	27	27
Senior unsecured bank bonds	300	306	372	380
Covered bank bonds	469	488	495	509
Public-sector issuers	3,011	2,790	2,955	2,684
from HfT to LaR	**113**	**114**	**121**	**115**
Asset-backed securities	113	114	121	115
Total	**3,919**	**3,725**	**3,970**	**3,715**

If the Bank had not opted for reclassification, this would have resulted in a € 7 million profit (before tax) for the first six months of the current financial year (H1 2013: € 15 million), and € 37 million (after tax) (H1 2013: € 79 million) would have been recognised in the revaluation surplus.

(32) Bond and property financing portfolio in selected European countries

The following table is a breakdown of the bonds issued by public-sector entities and bank bonds of selected European countries, included in non-trading assets.

Bond portfolio as at 30 June 2014

	Carrying amount			Revaluation reserve[1]			Unrealised
	LaR + HtM	AfS	Total	LaR	AfS	Total	gains/losses[1]
€ mn							
Greece	–	–	**–**	–	–	**–**	–
Ireland	–	–	**–**	–	–	**–**	–
Italy	1,149	714	**1,863**	-46	4	**-42**	-100
Portugal	65	179	**244**	0	-2	**-2**	-8
Spain	714	208	**922**	-3	5	**2**	-31
Total	**1,928**	**1,101**	**3,029**	**-49**	**7**	**-42**	**-139**
Total as at 31 Dec 2013	1,834	952	**2,786**	-51	-22	**-73**	-177

[1] figures given on an after-tax basis

The revaluation surplus for bonds of the "Loans and receivables" (LaR) category is attributable to securities which were reclassified in the years 2008 and 2009 from the measurement category "Available for sale" (AfS) to the measurement category "Loans and receivables" (LaR). Unrealised gains and losses refer to securities accounted for amortised cost (LaR + HtM). When determining such unrealised gains and losses, the effects from interest rate-driven measurement of hedged securities were taken into account.

The maturities of the bonds set out above are mainly within the long-term range.

The presented AfS securities with a carrying amount of € 1,101 million (previous year: € 939 million) were allocated to Level 1 of the fair value hierarchy pursuant to IFRS 7 and measured based on quoted prices on active markets. No Level 2 securities were allocated to the fair value hierarchy as at the current record date (previous year: € 13 million). No quoted market prices of the fair value hierarchy level 1 were available for Level 2 securities as at the balance sheet date, however, measurement is also directly or indirectly based on observable market prices. Aareal Bank Group does not hold securities measured according to Level 3 of the fair value hierarchy.

The following table is a breakdown of property financing in selected European countries included in loans and advances to customers.

Property financing portfolio as at 30 June 2014

	Carrying amount [1]	Average LTV	Non-performimg loans
	€ mn	%	€ mn
Greece	–		–
Ireland	–		–
Italy	3,104	69.5	446
Portugal	–		–
Spain	1,029	88.8	92
Total	**4,133**		**538**
Total as at 31 Dec 2013	4,174		515

[1] Not including valuation allowances

Other Notes

(33) Contingent liabilities and loan commitments

€ mn	30 Jun 2014	31 Dec 2013
Contingent liabilities on guarantees and indemnity agreements	85	120
Loan commitments	1,331	1,852
of which: irrevocable	801	1,328

(34) Employees

The number of Aareal Bank Group employees at 30 June 2014 is shown below:

	30 Jun 2014	31 Dec 2013
Salaried employees	2,390	2,251
Executives	142	124
Total	**2,532**	**2,375**
of which: Part-time employees	434	423

The increase in the number of employees mainly results from the consolidation of Corealcredit Bank AG as at 31 March 2014.

The average number of Aareal Bank Group employees in 2014 is shown below:

	1 Jan-30 Jun 2014	1 Jan-30 Dec 2013
Salaried employees	2,353	2,196
Executives	136	123
Total	**2,489**	**2,319**
of which: Part-time employees	430	427

(35) Related party disclosures in accordance with IAS 24

In the first six months of the 2014 financial year, there were no material transactions with related parties that would have to be reported here.

(36) Events after the interim reporting period

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

Executive Bodies of Aareal Bank AG

Supervisory Board

Marija G. Korsch [1) 2) 3) 4) 5)], Frankfurt
Chairman of the Supervisory Board
Former partner of Bankhaus Metzler seel. Sohn & Co. Holding AG

Erwin Flieger [1) 2) 4) 5)], Geretsried
Deputy Chairman of the Supervisory Board
Chairman of the Supervisory Boards of Bayerische Beamten Versicherungsgruppe

York-Detlef Bülow [1) 2) 3) 6)], Messel
Deputy Chairman of the Supervisory Board
Aareal Bank AG

Christian Graf von Bassewitz [3) 4) 5)], Hamburg
Banker (ret'd.); former Spokesman of the General Partners of Bankhaus Lampe KG

Manfred Behrens, Hannover
CEO/Chairman of the Management Board of Swiss Life Deutschland Holding GmbH (until 31 March 2014)

Thomas Hawel [6)], Saulheim
Aareon Deutschland GmbH

Dieter Kirsch [2) 4) 6)], Nackenheim
Aareal Bank AG

Dr. Herbert Lohneiß [4) 5)], Gräfelfing
Former Chief Executive Officer of Siemens Financial Services GmbH (ret'd)

Joachim Neupel [3) 4) 5)], Dreieich
Chairman of the Audit Committee
German Chartered Accountant, tax consultant

Richard Peters, Kandel
President and Chairman of the Management Board of Versorgungsanstalt des Bundes und der Länder

Prof. Dr. Stephan Schüller [1) 2) 3)], Hamburg
Spokesman of the General Partners of Bankhaus Lampe KG

Helmut Wagner [6)], Hahnheim
Aareon Deutschland GmbH

Management Board

Dr Wolf Schumacher
Chairman of the Management Board

Dagmar Knopek
Member of the Management Board

Hermann Josef Merkens
Member of the Management Board

Thomas Ortmanns
Member of the Management Board

[1)] Member of the Executive and Nomination Committee; [2)] Member of the Remuneration Control Committee; [3)] Member of the Audit Committee; [4)] Member of the Risk Committee; [5)] Member of the Committee for Urgent Decisions; [6)] Employee representative

Responsibility Statement

Statement pursuant to section 37y of the German Securities Trading Act (WpHG) in conjunction with section 37w (2) no. 3 of the WpHG

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

Wiesbaden, 5 August 2014

The Management Board

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

Review Report

To Aareal Bank AG, Wiesbaden

We have reviewed the condensed interim consolidated financial statements – comprising the statement of financial position, statement of comprehensive income, condensed statement of cash flows, statement of changes in equity and selected explanatory notes – and the interim group management report of Aareal Bank AG, Wiesbaden, for the period from January 1, 2014 to June 30, 2014, which are part of the half-year financial report pursuant to § (Article) 37w of the WpHG (”Wertpapierhandelsgesetz“: German Securities Trading Act). The preparation of the condensed consolidated interim financial statements in accordance with the IFRS applicable to interim financial reporting as adopted by the EU and of the interim group management report in accordance with the provisions of the German Securities Trading Act applicable to interim group management reports is the responsibility of the parent Company's Board of Managing Directors. Our responsibility is to issue a report on the condensed interim consolidated financial statements and on the interim group management report based on our review.

We conducted our review of the condensed consolidated interim financial statements and the interim group management report in accordance with the German generally accepted standards for the review of financial statements promulgated by the Institut der Wirtschaftsprüfer (Institute of Public Auditors in Germany) (IDW) and additionally observed the International Standard on Review Engagements (ISRE 2410), ”Review of Interim Financial Information Performed by the Independent Auditor of the Entity“. Those standards require that we plan and perform the review so that we can preclude through critical evaluation, with moderate assurance, that the condensed consolidated interim financial statements have not been prepared, in all material respects, in accordance with the IFRS applicable to interim financial reporting as adopted by the EU and that the interim group management report has not been prepared, in all material respects, in accordance with the provisions of the German Securities Trading Act applicable to interim group management reports. A review is limited primarily to inquiries of company personnel and analytical procedures and therefore does not provide the assurance attainable in a financial statement audit. Since, in accordance with our engagement, we have not performed a financial statement audit, we cannot express an audit opinion.

Based on our review, no matters have come to our attention that cause us to presume that the condensed consolidated interim financial statements have not been prepared, in all material respects, in accordance with the IFRS applicable to interim financial reporting as adopted by the EU nor that the interim group management report has not been prepared, in all material respects, in accordance with the provisions of the German Securities Trading Act applicable to interim group management reports.

Frankfurt/Main, August 5, 2014

PricewaterhouseCoopers
Aktiengesellschaft
Wirtschaftsprüfungsgesellschaft

Stefan Palm	**ppa. Kay Böhm**
German Public Auditor (Wirtschaftsprüfer)	**German Public Auditor (Wirtschaftsprüfer)**

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53119 Bonn, Germany
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Deposit-taking

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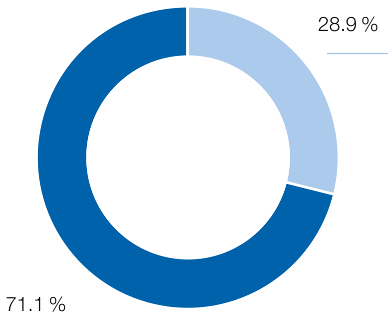
Fax: +353 1 6702785

Shareholder Structure | Financial Calendar

Shareholder Structure

■ Free float ■ Aareal Holding Verwaltungsgesellschaft mbH



6.9 %	Bayerische Beamten-Lebensversicherung a.G.
6.9 %	Swiss Life AG
5.2 %	Versorgungsanstalt des Bundes und der Länder
4.7 %	Dr. August Oetker Finanzierungs- und Beteiligungs-Gesellschaft mbH
2.7 %	Basler Lebensversicherungs-AG und Basler Sachversicherungs-AG
1.4 %	Deutscher Ring Krankenversicherungsverein a.G.
1.1 %	Condor-Lebensversicherungs Aktiengesellschaft

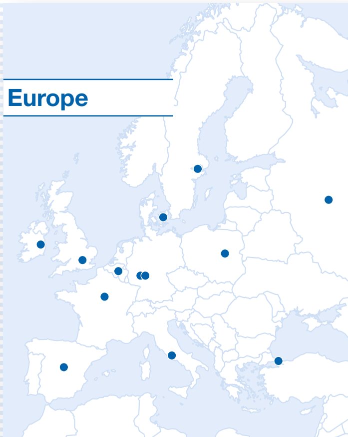
as at 30 June 2014

Financial Calendar

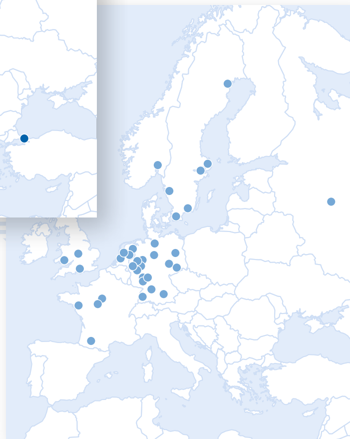
11 November 2014	Presentation of interim report as at 30 September 2014
May 2015	Annual General Meeting – Kurhaus, Wiesbaden

Locations

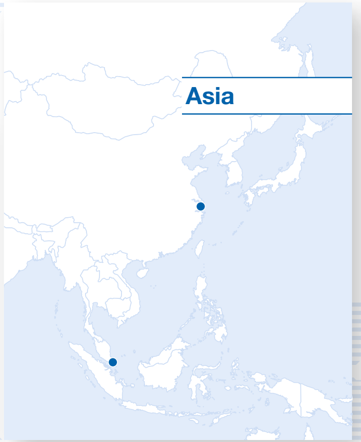
Structured Property Financing



Structured Property Financing



Consulting / Dienstleistungen



Structured Property Financing

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

Aareal Bank, Housing Unit: Berlin, Essen, Hamburg, Leipzig, Munich, Stuttgart, Wiesbaden | **Aareon AG:** Berlin, Coventry, Dortmund, Emmen, Enschede, Essen, Gorinchem, Hamburg, Hilversum, Hückelhoven, Karlskrona, Leipzig, Lund, Mainz, Meudon-la-Forêt, Mölndal, Munich, Nantes, Norrtälje, Orléans, Oslo, Piteå, Southampton, Stockholm, Stuttgart, Swansea, Toulouse | **Deutsche Bau- und Grundstücks-AG:** Berlin, Bonn, Dresden, Frankfurt/Main, Freiburg, Hannover, Leipzig, Moscow, Munich, Wuppertal | **Aareal First Financial Solutions AG:** Mainz

as at 30 June 2014

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