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Shaping the future.

Aareal Bank Group – Interim Report
1 January to 30 September 2017

Aareal Bank Group

Key Indicators

	1 Jan-30 Sep 2017	1 Jan-30 Sep 2016
Results		
Operating profit (€ mn)	262	281
Consolidated net income (€ mn)	165	193
Consolidated net income allocated to ordinary shareholders (€ mn)[1]	147	166
Cost/income ratio (%)[2]	41.1	41.6
Earnings per ordinary share (€)[1]	2.46	2.78
RoE before taxes (%)[1][3]	12.6	13.5
RoE after taxes (%)[1][3]	7.8	9.0

	30 Sep 2017	31 Dec 2016
Statement of financial position		
Property finance (€ mn)[4]	25,564	27,928
of which: international (€ mn)	21,967	23,423
Equity (€ mn)	2,884	3,129
Total assets (€ mn)	43,267	47,708
Regulatory indicators		
Risk-weighted assets (€ mn)	12,685	14,540
Common Equity Tier 1 ratio (CET1 ratio) (%)	17.7	16.2
Tier 1 ratio (T1 ratio) (%)	19.9	19.9
Total capital ratio (TC ratio) (%)	27.1	27.5
Common Equity Tier 1 ratio (CET1 ratio) (%) – fully phased-in –	17.3	15.7
Employees	2,768	2,728

	30 Sep 2017	31 Dec 2016
Fitch Ratings		
Deposit rating long-term	A- (outlook: stable)	A- (outlook: stable)
Issuer default rating long-term	BBB+ (outlook: stable)	BBB+ (outlook: stable)
short-term	F2	F2
Mortgage Pfandbrief rating	AAA (outlook: stable)	AAA (outlook: stable)
Public-Sector Pfandbrief rating	AAA (outlook: stable)	AAA (outlook: stable)
Moody's[5]		
Bank deposit rating long-term	A3 (outlook: stable)	A3 (outlook: stable)
Issuer rating long-term	Baa1	Baa1
short-term	P-2	P-2
Mortgage Pfandbrief rating	Aaa	Aaa
Sustainability[6]		
MSCI	AA	AA
oekom	prime (C)	prime (C)
Sustainalytics	71	71

[1] The allocation of earnings is based on the assumption that net interest payable on the AT1 bond is recognised on an accrual basis.
[2] Structured Property Financing segment only
[3] On an annualised basis
[4] Excluding € 0.9 billion in private client business (31 December 2016: € 1.1 billion) and € 0.6 billion in local authority lending business by former Westdeutsche ImmobilienBank AG (former WestImmo) (31 December 2016: € 0.6 billion)
[5] First published on 12 January 2017
[6] Please refer to our Sustainability Report for more details.

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

Contents

Letter from the Management Board

Dear shareholders,
business associates and staff members,

The market environment for Aareal Bank Group remained challenging during the third quarter of the 2017 financial year, characterised by various uncertainty factors and strong competition. Global economic growth proved robust during the first three quarters of the year, and global market sentiment clearly improved. However, a series of geopolitical events had a dampening effect.

Nevertheless, overall economic development remained sound, and thereby stabilised financial and capital markets. Although the European Central Bank (ECB) continued its expansive monetary money policy during the course of the year, it reduced the monthly purchase volume – within the scope of its asset-buying programme – from € 80 billion to € 60 billion, effective since April 2017. At the end of October, the ECB announced that it would extend its bond-purchasing programme by at least nine months from January 2018, further reducing the monthly volume to € 30 billion from that time. The US Federal Reserve (Fed) hiked the target corridor for its Fed Funds rate already for the second time this year, by 25 basis points respectively, to reach between 1.00 % and 1.25 % as at the end of the third quarter. Despite the turnaround of US monetary policy and the strong economic environment, interest rates remained low, especially in those markets which are important to Aareal Bank.

The banking sector's market environment remained challenging The continuous increase in regulatory requirements, combined with upcoming amendments to banking supervision led to uncertainty. Major challenges include the persistent low-interest rate environment and a set of new rules and regulations on banking supervision, including new requirements on risk management and banking IT. The business environment for commercial property financing was still characterised by high competitive pressure in many markets. Global transaction volumes remained at a high level, but the development was heterogeneous: volumes increased on some European markets, but declined in North America and Asia. Since the beginning of the year, margins were under pressure in most European markets as well as in the US, where they remained on a higher level compared to Europe. Aareal Bank particularly benefited from this trend, thanks to its flexible allocation of new business and expansion into higher-margin markets such as North America, which is in line with its strategy.

During the third quarter of the 2017 financial year, Aareal Bank Group maintained strong momentum from the first half of the year. In an environment that continued to be demanding, the Group generated consolidated operating profit of € 82 million (Q3 2016: € 74 million), and is thus well on track for achieving its targets for the full year 2017. Net interest income for the third quarter was down to € 164 million, in line with expectations (Q3 2016: € 175 million). Positive non-recurring effects from high early loan repayments were offset by charges – also as expected – from the continued scheduled reduction of the credit portfolio, and by currency translation effects. Consolidated net income attributable to ordinary shareholders amounted to € 47 million in the third quarter of 2017.

In the Structured Property Financing segment, Aareal Bank Group generated operating profit of € 89 million during the third quarter of 2017, thus € 4 million above the same quarter of the previous year – a good result, particularly in light of the persistently difficult environment. At € 26 million, allowance for credit losses was clearly lower year-on-year, and within expectations. Regarding total allowance for credit losses, we affirm the forecast range of € 75 million to € 100 million for the full financial year, which is lower compared to the previous year. Aareal Bank generated € 1.9 billion in new business in its Structured Property Financing segment during the third quarter of 2017 (Q3 2016: € 1.6 billion). This brought new business origination for the first nine months of the year to € 5.7 billion, which is about on par with end-September 2016. Thanks to its flexible allocation of new business, and with a clear focus on attractive markets such as the US, Aareal Bank Group was able to keep gross margins on new business stable – despite tough competition and in contrast to original expectations. The target for new business in the Structured Property Financing segment for the full year 2017 remains unchanged, at between € 7 billion and € 8 billion.

In the Consulting/Services segment, which – in line with our "Aareal 2020" programme for the future – is set to evolve into a key growth driver for Aareal Bank Group, the Bank's Housing Industry division further strengthened its market position. Aareal Bank was able to acquire new customers in its payment services and deposit-taking businesses, while the customer base in the energy and waste disposal industries was also further expanded. Our IT subsidiary Aareon AG also continued to steer a steady, successful course, with solid earnings development and another increase in sales revenues to € 51 million (Q3 2016: € 49 million). Driven by the good performance of the entire segment, Aareal Bank Group's consolidated net commission income developed favourably, rising to € 48 million in the third quarter of 2017 (Q3 2017: € 44 million).

Aareon continued to consistently pursue its core growth initiatives throughout the third quarter of the year, representing an integral part of "Aareal 2020". For instance, recent demand for Aareon's newly-developed digital solutions, such as the Mareon service portal for the German housing industry, has grown significantly. The increase in demand is not limited to the German market, as shown by recently signed contracts for the development of country-specific digital solutions for the French and Dutch markets. The Bank's Housing Industry division has responded to the digitalisation megatrend, through investments into the "Aareal Portal" corporate clients platform in particular. The pilot phase for this platform, which optimises and speeds up mutual communications processes, has commenced.

In the segment's banking business, the volume of client deposits from the housing industry remained at a high level, averaging € 9.7 billion during the quarter under review (Q3 2016: €9.5 billion) – a testament to the continued trust that clients place in Aareal Bank. Nevertheless, results from the deposit-taking business continued to be burdened by interest rates at historically low levels in the current year, leading to a segment operating loss of € 7 million before taxes for the third quarter – an improvement of € 4 million against the same period of the previous year (Q3 2016: € -11 million).

Not least due to the ECB's persistent low-interest rate policy, we must assume – for the time being – that segment results will continue to be burdened. Yet the importance of deposit-taking goes way 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.

Aareal Bank Group has remained very solidly funded throughout the first nine months of 2017. It maintained its inventory of long-term funding at a high level, raising € 2.1 billion on the capital markets during this period, including a total volume of € 1.7 billion placed via Pfandbriefe. As at 30 September 2017, the Bank's Tier I ratio was 19.9 per cent, which is comfortable on an international level. Assuming full implementation of Basel III, the fully phased-in Common Equity Tier I (CET I) ratio would be 17.3 per cent. This means that Aareal Bank continues to have a very solid capital base.

Based on the successful business performance between January and September 2017, we remain confident that we will achieve our targets set for 2017, and therefore maintain our full-year forecast. We continue to anticipate being able to generate consolidated operating profit of between € 310 million and € 350 million in the current financial year. This would translate into earnings per share of between € 2.85 and € 3.30. We anticipate RoE for the current year in a range between 11 per cent and 12.5 per cent. We affirm our medium-term target for return on equity of around 12 per cent before taxes.

Aareal Bank Group anticipates that the uncertainty factors and the overall market environment will not fundamentally change during the remainder of the year. This includes, in particular, continued intense competition as well as rapidly tightening regulatory requirements. Against this background, we will be focusing, until the end of the year, on continuing to pursue the strategic direction we have embarked upon. Thanks to our perfectly healthy operative business and financial strength, we are in a position to take the right strategic decisions to ensure a sustainably successful future for our Company – making the requisite investments as well as bearing the burdens associated with the changes from a position of strength. We will consistently pursue its "Aareal 2020" programme for the future. This programme comprises numerous initiatives for further developing business in its two segments, especially with respect to ongoing digitalisation and the expansion of business into new markets and neighbouring industries, as well as the expansion of syndication activities. A further key element of the programme is the optimisation of internal structures and processes, which – as already announced – will be continued next year, and will also involve personnel measures.

Dear shareholders, business associates and staff members, as you can see, Aareal Bank Group will do everything to successfully implement a focused and consistent business strategy – even under challenging overall market and geopolitical conditions. We look forward to your continued support along this path.

For the Management Board

Yours sincerely,

Hermann J. Merkens
Chairman

Interim Group Management Report

Report on the Economic Position

Macro-economic environment

The developed economies reported synchronised and robust growth in the first three quarters of the year. On the other hand, numerous political uncertainty factors had a dampening effect.

Economy

Global economic output demonstrated solid growth in the first three quarters, with a synchronous increase observed in the industrial nations. There was a noticeable increase in global trade up to the end of the third quarter. Global economic sentiment indicators reached high levels.

The euro zone achieved robust growth in the first three quarters of the year; growth momentum in private consumption decreased slightly whilst investment and export activities increased. Elevated political uncertainty in the run-up to elections in France and the Netherlands eased significantly after the respective events, even though the formation of the Dutch government was not completed by the end of the third quarter of 2017. Germany benefited from the increase in world trade; the ifo business climate index reached an all-time high in July. Economic growth was in line with the euro zone average. Economic output in France climbed significantly in the course of the year. Spain continued its strong growth path up to the third quarter. Growth in Italy was up sharply on the previous year, albeit below the euro zone average. In addition, the Italian banking sector continued to provide problems during the year, with two regional institutions entering resolution in the second quarter. Prior to this development, Fitch Ratings had downgraded Italian government bonds from BBB+ to BBB.

Growth in numerous non-euro zone EU nations surpassed the average growth rate of their euro zone neighbours. Growth in Sweden strengthened as the year progressed, whereas Denmark posted significantly higher growth figures than in the same period of the previous year. Growth in Poland was also materially higher in the first three quarters of the year.

The exit of the UK from the EU, which was formally requested on 29 March 2017, continued to impact on politics and the economy there, along with the early parliamentary elections on 8 June 2017. Several terrorist attacks added to the uncertainty. Contrary to the governing Conservative party's hopes, the election did not produce a strong mandate for the forthcoming Brexit negotiations with the EU, thus increasing the uncertainty surrounding the planned exit. Weak private consumption and a weak expansion of the services sector curbed economic growth during the first three quarters of the year. Moody's responded to this by downgrading the UK's creditworthiness from Aa1 to Aa2.

The two hurricanes "Harvey" and "Irma" led to slightly lower-than-expected third quarter growth in the US. Growth in the first three quarters was sustained by investment and private consumption, and was higher than the comparable prior-year period.

Growth in China was stable in the first three quarters. Due to strong private debt and falling growth prospects, rating agency Moody's downgraded China's creditworthiness from A1 to A3 at the end of May, also changing the outlook from "stable" to "negative".

Unemployment rates declined slightly during the first three quarters of the year, both in the euro zone and in the EU. Unemployment was also stable to slightly lower when looking at individual countries. Within the EU, Germany and the Czech Republic continued to post the lowest unemployment rates, whilst unemployment remained at just under 20% in Spain, despite slight decreases. Unemployment in the UK fell to its lowest level in 42 years. The already very low unemployment rate in the US continued to decline at the start of the year but remained stable, at a low level, during the course of the year.

Financial and capital markets, monetary policy and inflation

Geopolitical events towards the end of the third quarter led to a temporary increase in volatility on the financial and capital markets, having been very low in the year to date. However, the robust economic environment had an overall stabilising effect. The focus in the third quarter was on exchange rate fluctuations and rising volatility on the currency markets.

The European Central Bank (ECB) maintained its expansionary policy in the first three quarters of 2017. However, as already announced in December 2016, it reduced the monthly purchase volume within the scope of its asset-buying programme by € 20 billion, to € 60 billion since April 2017. Sweden's Riksbank further expanded its monetary policy during the same period, increasing the planned government bond purchase volume by SEK 15 billion for the second half of the year. Due to the pending Brexit negotiations, the Bank of England (BoE) adhered to its cautious attitude, keeping its monetary policy stance unchanged.

The US Federal Reserve (Fed) raised its key interest rate corridor twice during the course of 2017 – most recently in June – by 25 basis points, respectively. Thus, at the end of the third quarter, the Fed Funds corridor was between 1.00 % and 1.25 %. It also confirmed at the end of September that it will start to gradually reduce its total assets from October onwards, in small steps initially. The reduction is expected to pick up pace over time, according to a fixed schedule. The Fed is therefore the first of the important central banks worldwide to start reducing its balance sheet. However, it gave no indication of the extent of the reduction.

Long-term interest rates[1] showed a mixed picture in the first six months of 2017 across the different currency areas important for Aareal Bank. Whilst they were stable for the US dollar at the beginning of the year, they fell again slightly until the third quarter, coming in just below the 2016 year-end level. For the pound sterling, they were slightly above the 2016 year-end level at the end of the third quarter. A slight but steady rise could be observed in the euro zone.

Short-term maturities[2] also saw a mixed picture towards the end of the first half of the year compared to year-end 2016. There was evidence of a marked increase over the end of 2016 in the US dollar. Short-term interest rates in the euro zone were stable on a slightly negative level during the course of the year. Pound sterling short-term interest rates however decreased slightly.

The development of global long-term government bond yields remained inconsistent up to the end of the third quarter. The decline in the US was continuous, with yield levels only slightly lower compared with year-end 2016. On the other hand, yields within the euro zone increased slightly during the same period. Volatility in the UK was a little higher than in the euro zone; yields at the end of the third quarter were up slightly on the year-end 2016 level.

The euro exchange rates against various counterparties that are important to Aareal Bank were more volatile during the third quarter than in the first half of 2017. The euro has made consistent and strong gains in value over the US dollar since the second quarter. It also strengthened considerably vis-à-vis the Canadian dollar during the course of the year. The pound sterling was almost constant to the euro in the first half of the year but then incurred a significant loss in value during the third quarter.

Inflation increased markedly in the course of the year in many economies over the previous year and reached a preliminary high in many markets during the first half of the year. In the euro zone, it remained on average below the ECB's target during the first three quarters; it then weakened to 1.3 % in the third quarter. Inflation in the UK has increased significantly over the course of the year, to reach

[1] Based on the 10-year swap rate
[2] Calculated on the basis of 3-month Euribor or the corresponding LIBOR or other comparable rates for other currencies

2.8 % in the third quarter. This was mainly due to the weaker pound sterling. In the US, inflation reached 2.0 % in the third quarter of 2017; the upside price pressure therefore weakened slightly in the course of the year. Third quarter inflation in China was 1.6 %, which represents a slight increase compared with the first half year.

The Pfandbrief market was once again heavily influenced in 2017 by the ECB, and by developments related to quantitative easing measures. Persistently low interest rates and low credit spreads on Pfandbriefe determined the ability to place Pfandbriefe this year, too. Notwithstanding the discernible decline in the volume of privately placed Pfandbrief issues, issuing activity of Pfandbrief transactions in benchmark format was only marginally lower than in the previous year. However, positive net issuance was ascertained again this year: by September, issuance had already exceeded maturities by nearly € 5 billion.

Regulatory environment

The environment in which banks are operating continues to be defined by highly dynamic regulatory requirements, as well as by changes in banking supervision. Especially when considering the extensive work the Basel Committee is undertaking to complete the already-implemented Basel III regime, it is still not possible to fully assess the impact. In addition, the amendment to the Minimum Requirements for Risk Management (MaRisk) – including the new German Banking Supervisory Requirements for IT (BAIT), the EU Commission's proposals to revise supervisory regimes (CRR, CRD IV, BRRD and SRMR) as well as the EBA consultation paper "Guidelines on PD estimation, LGD estimation and the treatment of defaulted exposures", will all lead to further regulatory changes.

The ECB's Supervisory Review and Evaluation Process (SREP) ensures a common approach on the supervisory review of banks, within the framework of Pillar 2. The SREP is built around a business model analysis, an assessment of governance, as well as of the capital and liquidity risks. The results of the individual areas are aggregated in a score value, from which the ECB derives supervisory measures on holding additional capital and/or additional liquidity requirements. The ECB converted the SREP requirements from a pure CET 1 ratio to a total SREP ratio (Total SREP Capital Requirement – "TSCR") with effect from 1 January 2017. This has been 9.75 % since 1 January 2017, comprising the total capital ratio of 8 % for Pillar 1 and a (Pillar 2) capital requirement of 1.75 % from the ECB's Supervisory Review and Evaluation Process (SREP). In addition, the Bank is required to hold a (phased-in) capital conservation buffer of 1.25 %, plus a countercyclical capital buffer of 0.03 %. Aareal Bank's pure SREP-driven CET 1 requirement has been 7.53 % since 1 January 2017, comprising 4.5 % for Pillar 1, the Pillar 2 capital buffer requirement of 1.75 % (as mentioned above), as well as the capital conservation buffer (1.25 %) and the countercyclical buffer (0.03 %). No further liquidity requirements were imposed upon Aareal Bank.

Sector-specific and business developments

Structured Property Financing segment

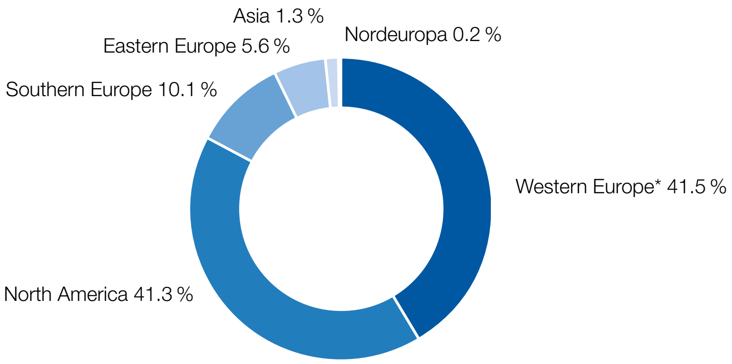
The development of the volume of commercial property transactions was inconsistent across the different regions in the third quarter of 2017. Transaction activity in some European markets rose again over the previous year. In contrast, volumes in North America and Asia declined.

Financing of existing commercial property continued to be subject to considerable competitive pressure in many markets. While margins were under pressure in most European markets and the US during the first three quarters, they remained on a higher level in the US when compared to Europe. Pricing levels on the US market are also influenced by the market for commercial mortgage-backed securities (CMBS). The volume in this segment increased slightly during the third quarter but remained on a low level.

In a highly competitive business environment that remains characterised by uncertainty, Aareal Bank succeeded in generating € 5.7 billion of new

New business 1 January - 30 September 2017

by region (%) Total volume: € 5.7 bn



* Incl. Germany

business in the first three quarters. This figure is down only slightly on the corresponding figure for the previous year (€ 6.0 billion). At € 3.8 billion, the volume of newly-originated loans was up slightly on the previous year (€ 3.6 billion), so that the share of newly-originated loans in aggregate new business for the first three quarters of 2017 came to 67.6 % (9 m 2016: 57.3 %). New business of € 1.9 billion (Q3 2016: € 1.6 billion) was generated in the quarter under review, with newly-originated loans accounting for € 1.1 billion or 58.4 % thereof (Q3 2016: € 0.6 billion or 35.2 %).

At 57.4 % (9 m 2016: 68.2 %), Europe accounted for the largest share of new business in the first three quarters of the year, followed by North America with 41.3 % (9 m 2016: 28.8 %), and Asia with 1.3 % (9 m 2016: 3.0 %). This increase in the North American share over the previous year is in line with the targets of our "Aareal 2020" programme for the future.

Europe

The volume transacted in commercial property in Europe was stable in the first three quarters of 2017. Overall, the level remained high, and transaction activity could be described as lively. Transaction volumes rose in Germany, the Netherlands and Spain, whilst declining significantly in France and Poland. In the UK, a few large transactions concluded with Asian investors led to an increase in the volume transacted in the second and third quarter.

Compared to year-end 2016, yields for newly-acquired, first-class commercial properties declined in the course of 2017 to date in many European economic centres; in part, this was due to the shortage of available top-quality properties. Yields in the UK declined marginally in some sub-markets, having risen slightly during the same quarter of the previous year, following the Brexit vote on 23 June 2016. The underlying yield development trend applied to office, retail and logistics properties alike.

Rents for first-class office, retail and logistics properties in the European economic centres were largely stable to date in 2017 compared to the end of 2016. In contrast, rents even rose in a few markets, e.g. in the markets for first-class office properties in Berlin and Stockholm. Rents for first-class retail properties increased slightly in some markets, such as in Milan. Only a few European economic centres witnessed declining rents in the premium segment, for example in a few retail locations in Germany.

The hotel markets in the European economic centres presented a positive picture during the first three quarters of 2017. Occupancy ratios rose in most markets; markedly so in certain markets such as Brussels, Milan, Paris, and Prague. The indicator of average revenues per available room (important for hotel markets) also recorded an increase in most markets. Developments in Brussels and Paris should be highlighted, as these markets continued to recover very well, having been burdened by terrorist attacks in the past years. In London, occupancy figures also rose noticeably, and average revenues per available room picked up significantly.

Aareal Bank succeeded in originating € 1.2 billion of new business in Europe during the third quarter (Q3 2016: € 1.1 billion), therefore amounting to € 3.3 billion overall during the first three quarters of 2017 (9 m 2016: € 4.1 billion). Western Europe accounted for the highest share, followed by

Southern and Eastern Europe, and a marginal share in Northern Europe.

North America

The volume transacted in the North American commercial property markets was noticeably lower than in the first three quarters of 2016. Nevertheless it was high, and the market was very liquid.

The first three quarters of 2017 were characterised by a largely constant yield development. On a national average, investment yields in the US hardly moved – compared to the year-end 2016 – for office and retail properties. On the other hand, retail properties reported scattered increases in California's metropolitan areas.

Rents increased marginally on a national average in the US, compared to the final quarter of 2016, for the types of property mentioned. This development also applied for many of the leading regional markets in the US.

In the first three quarters of the year, occupancy ratios for hotel properties rose slightly on a national average in the US, compared to the previous year. Average revenue per available hotel room on the other hand climbed at a slightly stronger rate. Both indicators showed modest growth in Canada too.

Aareal Bank originated new business of € 0.7 billion in North America during the third quarter (Q3 2016: € 0.5 billion), bringing aggregate new business in North America to € 2.4 billion for the first three quarters of the year (9 m 2016: € 1.7 billion). This business was generated in the US and Canada.

Asia

The volume transacted in commercial property during the first three quarters of 2017 in the Asia-Pacific region fell significantly compared with the previous year's figure.

Investment yields for newly-acquired, high-quality commercial property remained largely stable in Beijing and Shanghai, whilst rents for first-class office and retail properties in these two metropolitan areas hardly moved. Rents for office properties outside of the first-class segment in Beijing were down marginally.

A positive development of average revenues per available hotel room prevailed on the hotel markets of Beijing and Shanghai in the period under review.

Aareal Bank Group concluded only minor new business in Asia during the first three quarters of the year (9 m 2016: € 0.2 billion).

Consulting/Services segment

Housing Industry division

The development of the housing and commercial property industries in Germany proved stable during the third quarter of 2017, too. The key issues for the industry are implementing the transition of the energy sector (the "Energiewende") for buildings, as well as new construction.

The positive development seen in the course of the year continued on the housing market, despite the slowdown in price momentum and even greater regional differences. Rents offered were approximately 3.1 % higher in the third quarter than at the start of the year. While vacancies are increasing in rural areas, housing shortages are appearing in some urban areas despite higher levels of building permits and new construction activity.

The vacancy ratio reported by members of the Federation of German Housing Enterprises (GdW) also varies regionally. Vacancies in the East German states showed slightly declining rates+, to 8.2 %, while remaining constant at 1.9 % in the West German states.

The Bank's Housing Industry division has responded to the digitalisation megatrend, a development that has also noticeably affected the housing industry, through investments into the "Aareal Portal" corporate clients platform in particular. The pilot phase for this platform, which optimises and speeds up mutual communications processes, has commenced. In addition, the Bank is constantly reviewing innovative fintech start-ups with a view towards potential scope for cooperations, in order to gradually supplement its range of services in connection with existing payments products.

The Bank's Housing Industry division further strengthened its market position during the first three quarters of 2017, bringing in more business partners from the housing industry – managing more than 244,000 residential units between them – for the payments and deposit-taking businesses. Moreover, it intensified existing business relationships. We also continuously expanded our client base in the energy and waste disposal industries, especially through interface products facilitating cross-sector collaboration amongst our client groups. Examples include accounting documentation and invoicing of energy supplies.

At present, more than 3,200 housing industry clients throughout Germany are using the process-optimising products and banking services of Aareal Bank Group. The high volume of deposits from the housing industry – averaging € 9.7 billion in the third quarter of 2017 (€ 9.6 billion in Q2 2017) – is in line with the "Aareal 2020" programme for the future. Besides the increase in current account deposits, the share of rent deposits and reserves in accordance with the German Residential Property Act in particular also increased. Deposits averaged € 9.8 billion during the 2017 period under review (9 m 2016: € 9.4 billion). All in all, this reflects the strong trust that clients place in Aareal Bank.

Aareon

Aareon's contribution to consolidated operating profit amounted to € 21 million during the period under review (Q3 2016: € 21 million).

Germany

In Germany, Aareon distributes the Wodis Sigma ERP solutions, SAP® solutions, and Blue Eagle. Numerous additional customers opted for Wodis Sigma up to the end of the third quarter. Among these, there are still many previous GES customers who opted to change to Wodis Sigma within the framework of Aareon's migration campaign. As expected, the favoured version is the one that uses Wodis Sigma as a service from the exclusive Aareon Cloud. Aareon is still implementing a large number of migration projects, which are developing on schedule. Capacity utilisation in the Aareon consulting business thus remains on a high level.

The topic of digitalisation is becoming increasingly more important in the German housing industry. With the digital ecosystem Aareon Smart World, Aareon is offering an integrated portfolio of solutions that networks the stakeholders. In this context, Aareon is reporting high demand for digital solutions, such as the Mareon service portal, Aareon Archiv kompakt, Aareon CRM, and Mobile Solutions. Demand also benefits from the migration business with the ERP solutions. In addition, Aareon cooperates with PropTech companies, in order to expand the integrated offer of Aareon Smart World for its clients.

Within the area of add-on products, Aareon was able to considerably extend its outsourcing business in Germany, in particular. Sales at the BauSecura insurance business were running at the same level as the previous year during the quarter under review. Amid business expansion for the energy utilities industry, Aareon has stepped up its marketing activities. A solution for the process digitalisation in the case of house moves for this target group is in the scheduled pilot phase.

International Business

Aareon offers country-specific ERP solutions on an international level and continues to grow in this area. The acquisition of Dutch Kalshoven Groep B.V., effective 1 April 2017, made a significant contribution to growth in the business with ERP products. Stronger maintenance business generated sustainable growth in France. Despite intensive competition, three customers were won in the UK for QL.net. In Sweden, subsidiary Aareon Sverige AB (formerly Incit AB) won the contract for the Lerum municipality, whilst a client rolled out production with the ERP solution Incit Xpand and the digital tenant portal.

Further contracts with digital solutions were signed and the sales volume in International Business exceeded that of the previous year. Whilst sales growth in France is particularly strong due to regulatory requirements of Aareon clients, in the UK it has remained below the previous year's level. Together with Aareon UK, Aareon Nederland has prepared the market launch of the Trace & Treasury solution in the UK (already well-established in the Netherlands) during the last months, and a first client was acquired – as was the case for the Dutch Facilitator solution in the Scandinavian market.

The full acquisition of the Dutch subsidiary SG2ALL B.V. in 2016, and the increased business with third-party products in the UK, led to higher sales revenues in the area of add-on products.

Preparations in view of the introduction of the new EU General Data Protection Regulation (GDPR, effective as of 2018) are progressing as scheduled.

Financial Position and Financial Performance

Financial performance

Group

Consolidated operating profit amounted to € 262 million during the first nine months of the financial year (9 m 2016: € 281 million).

Net interest income totalled € 486 million, an expected reduction from the previous year (9 m 2016: € 532 million). This was largely due to the scheduled reduction of the former WestImmo and Corealcredit portfolios, high early repayments, as well as a lack of suitable investment opportunities for our liquidity reserves, given the persistent low interest rate levels, and exchange rate fluctuations.

Allowance for credit losses amounted to € 53 million (9 m 2016: € 64 million) and was thus in line with our expectations. It mainly comprised net additions to specific allowance for credit losses of € 51 million.

Net commission income increased to € 145 million (9 m 2016: € 137 million), which was mainly due to higher sales revenue at Aareon.

The aggregate of net trading income/expenses and the net result on hedge accounting of € 8 million (9 m 2016: € 25 million) resulted largely from the measurement and close-out of derivatives used to hedge interest rate and currency risks.

At € 388 million (9m 2016: € 417 million), administrative expenses were reduced as expected,

Consolidated net income of Aareal Bank Group

€ mn	1 Jan-30 Sep 2017	1 Jan-30 Sep 2016
Net interest income	486	532
Allowance for credit losses	53	64
Net interest income after allowance for credit losses	**433**	**468**
Net commission income	145	137
Net result on hedge accounting	-5	4
Net trading income/expenses	13	21
Result from non-trading assets	0	66
Results from investments accounted for using the equity method	–	0
Administrative expenses	388	417
Net other operating income/expenses	64	2
Operating profit	**262**	**281**
Income taxes	97	88
Consolidated net income	**165**	**193**
Consolidated net income attributable to non-controlling interests	6	15
Consolidated net income attributable to shareholders of Aareal Bank AG	159	178

in spite of provisions recognised for planned personnel measures resulting from the optimisation of processes and structures, within the scope of the "Aareal 2020" programme for the future. The decline was due in particular to lower integration costs and lower running costs for former WestImmo, as well as lower project expenditure.

Net other operating income of € 64 million (9 m 2016: € 2 million) mainly resulted from net reversals of provisions (€ 50 million) in connection with the final agreement on contractual issues with a third party, which were still pending when Aareal Bank Group acquired former Corealcredit, and the release of tax assessment notes. Aareal Bank Group disclosed a corresponding income tax expense of € 26 million.

Overall, this resulted in consolidated operating profit of € 262 million for the first nine months (9 m 2016: € 281 million). Taking into consideration tax expenses of € 97 million and non-controlling interest income of € 6 million, consolidated net income attributable to shareholders of Aareal Bank AG amounted to € 159 million (9m 2016: € 178 million). Assuming the pro rata temporis accrual of net interest payments on the AT1 bond, consolidated net income allocated to ordinary shareholders stood at € 147 million (9 m 2016: € 166 million). Earnings per ordinary share amounted to € 2.46 (9m 2016: € 2.78) and annualised return on equity (RoE) before taxes to 12.6 % (9 m 2016: 13.5 %).

Structured Property Financing segment

Operating profit in the Structured Property Financing segment amounted to € 281 million during the first nine months of the financial year (9 m 2016: € 309 million).

Segment net interest income of € 494 million showed an expected decline from the previous year (9 m 2016: € 542 million). This was largely due to the scheduled reduction of the former WestImmo and Corealcredit portfolios, high early repayments, as well as a lack of suitable investment opportunities for our liquidity reserves, given the persistent low interest rate levels, and exchange rate fluctuations.

Allowance for credit losses amounted to € 53 million (9 m 2016: € 64 million) and was thus in line with our expectations. It mainly comprised net additions to specific allowance for credit losses of € 51 million.

Structured Property Financing segment result

€ mn	1 Jan-30 Sep 2017	1 Jan-30 Sep 2016
Net interest income	494	542
Allowance for credit losses	53	64
Net interest income after allowance for credit losses	**441**	**478**
Net commission income	4	5
Net result on hedge accounting	-5	4
Net trading income/expenses	13	21
Result from non-trading assets	0	66
Results from investments accounted for using the equity method	–	–
Administrative expenses	234	266
Net other operating income/expenses	62	1
Operating profit	**281**	**309**
Income taxes	104	98
Segment result	**177**	**211**

At € 234 million (9 m 2016: € 266 million), segment administrative expenses were reduced as expected, in spite of provisions recognised for planned personnel measures resulting from the optimisation of processes and structures, within the scope of the "Aareal 2020" programme for the future. The decline was due in particular to lower integration and lower running costs for the former WestImmo, as well as lower project expenditure.

Net other operating income of € 62 million (9 m 2016: € 1 million) mainly resulted from net reversals of provisions (€ 50 million) in connection with the final agreement on contractual issues with a third party, which were still pending when Aareal Bank Group acquired former Corealcredit, and the release of tax assessment notes. Aareal Bank Group disclosed a corresponding income tax expense of € 26 million.

Overall, operating profit for the Structured Property Financing segment was € 281 million (9 m 2016: € 309 million). Taking tax expenses of € 104 million into consideration (9 m 2016: € 98 million), the segment result was € 177 million (9 m 2016: € 211 million).

Consulting/Services segment

Sales revenue generated in the Consulting/Services segment developed positively during the first nine months 2017, totalling € 162 million (9 m 2016: € 148 million), driven particularly by Aareon's higher sales revenues. The persistent low interest rate environment continued to burden margins from the deposit-taking business that are reported in sales revenues.

Other items were roughly unchanged from the previous year's levels.

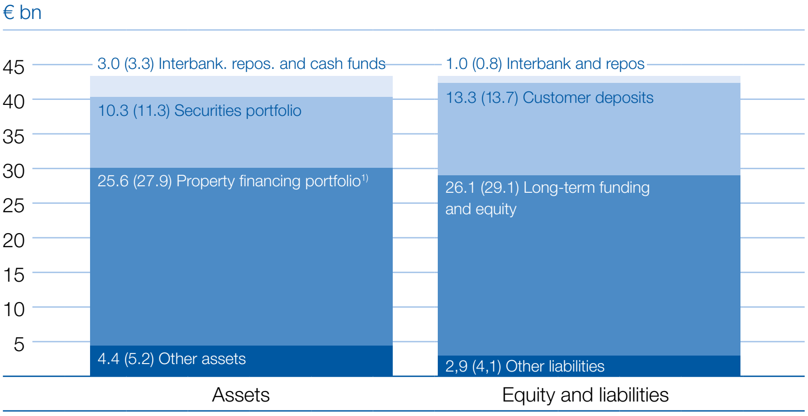
Overall, segment operating profit in the first nine months of 2017 was € -19 million (9 m 2016: € -28 million). Aareon's contribution was € 21 million (9 m 2016: € 21 million).

After taking taxes into consideration, the segment result for the first nine months of the year amounted to € -12 million (9 m 2016: € -18 million).

Consulting/Services segment result

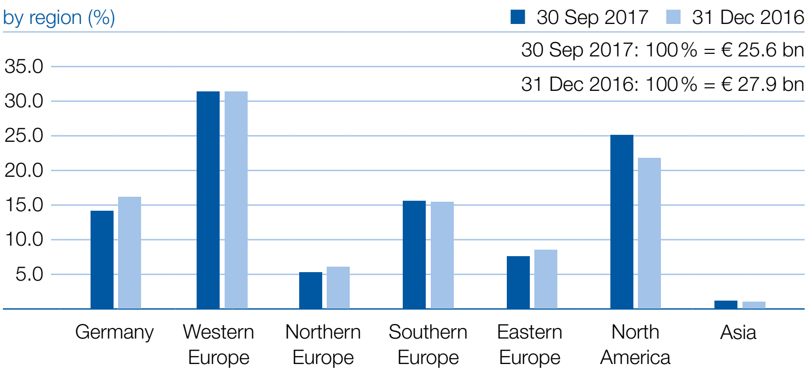
€ mn	1 Jan-30 Sep 2017	1 Jan-30 Sep 2016
Sales revenue	162	148
Own work capitalised	3	4
Changes in inventory	0	0
Other operating income	3	3
Cost of materials purchased	26	24
Staff expenses	109	107
Depreciation, amortisation and impairment losses	9	9
Results from investments accounted for using the equity method	–	0
Other operating expenses	43	43
Interest and similar income/expenses	0	0
Operating profit	**-19**	**-28**
Income taxes	-7	-10
Segment result	**-12**	**-18**

Statement of financial position – structure as at 30 Sep 2017 (31 Dec 2016)

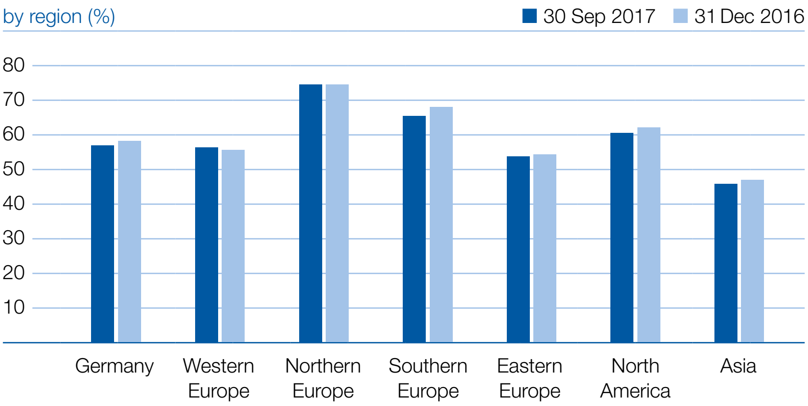


1) Excluding € 0.9 billion in private client business (31 December 2016: € 1.1 billion) and € 0.6 billion in local authority lending business by former WestImmo (31 December 2016: € 0.6 billion)

Property financing volume2) (amounts drawn)



Average LTV of property financing2)



2) Excluding former WestImmo's private client business and local authority lending business
Note that the loan-to-value ratios are calculated on the basis of market values, including supplementary collateral with sustainable value.

Financial position

Aareal Bank Group's consolidated total assets amounted to € 43.3 billion as at 30 September 2017, after € 47.7 billion as at 31 December 2016.

Property financing portfolio

The volume of Aareal Bank Group's property financing portfolio stood at € 25.6 billion as at 30 September 2017, down by 8.5 percentage points from the year-end level 2016 (€ 27.9 billion). This was particularly attributable to the planned portfolio reduction at former WestImmo and Corealcredit, high early repayments, and exchange rate fluctuations. The international share of the portfolio increased to 85.9 % (31 December 2016: 83.9 %).

At the reporting date (30 September 2017), Aareal Bank Group's property financing portfolio was composed as shown in the charts beside, compared with year-end 2016.

Portfolio allocation by region and continent changed only selectively compared with the end of the previous year. Whilst the portfolio share of exposures in North America rose by 3.4 percentage points, in line with the "Aareal 2020" programme for the future, it declined in Germany (by approximately 2.1 percentage points). It remained stable, or declined only marginally for all other regions.

The breakdown of the portfolio by property type did not change significantly during the reporting period. The share of hotel property increased by 2.1 percentage points compared to year-end 2016, whilst the share of office property was reduced by 2.8 percentage points. The share of financings for residential, logistics, and retail property as well as other financings in the overall portfolio remained almost unchanged compared to the year-end 2016.

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

Securities portfolio

As at 30 September 2017, the nominal volume of the securities portfolio[1] declined to € 8.6 billion (31 December 2016: € 9.3 billion), as scheduled, reflecting a high level of maturities and low new investments. The securities portfolio comprises three asset classes: public-sector borrowers, covered bonds and Pfandbriefe, as well as bank bonds. 99 %[2] of the overall portfolio is denominated in euro. 98 %[2] of the portfolio has an investment grade rating[3]. More than 75 % of the portfolio fulfils the requirements of "High Quality Liquid Assets" (as defined in the Liquidity Coverage Ratio (LCR)).

Financial position

Funding and equity

Funding

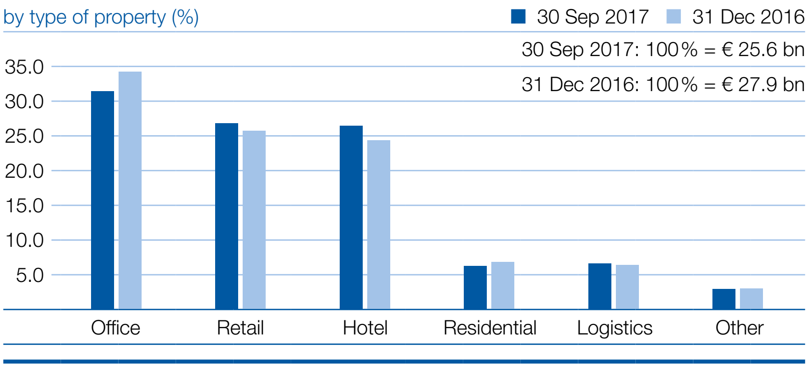
Aareal Bank Group has remained very solidly funded throughout the first nine months of the 2017 financial year. Total long-term refinancing as at 30 September 2017 amounted to € 23.5 billion (31 December 2016: € 26.5 billion), comprising Pfandbrief issues as well as senior unsecured and subordinated issues. As at the reporting date, Aareal Bank also had € 9.3 billion at its disposal in deposits generated from the business with the housing industry (31 December 2016: € 8.4 billion). Institutional money market investors' deposits amounted to € 4.0 billion (31 December 2016: € 4.5 billion).

The Liquidity Coverage Ratio (LCR) exceeded 150 % on the reporting days of the period under review.

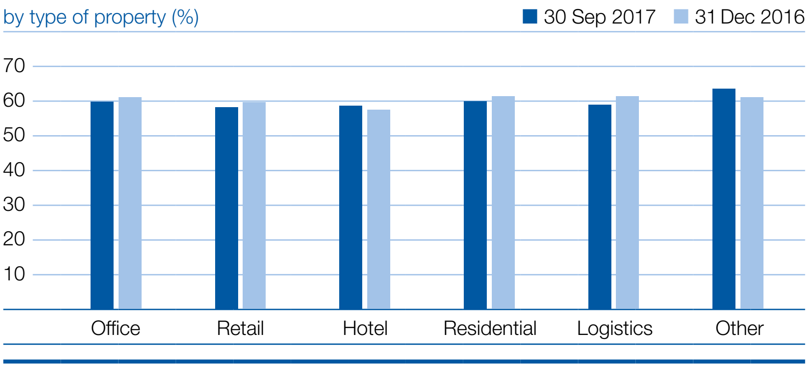
Aareal Bank Group raised € 2.1 billion on the capital market during the first nine months of 2017. The total figure included two non-euro Mortgage Pfandbrief issues worth mentioning in particular, with issuing volumes of US$ 625 million and £ 250 million, respectively – the majority of which was sold to international investors.

[1] As at 30 September 2017, the securities portfolio was carried at € 10.3 billion (31 December 2016: € 11.3 billion).
[2] Details based on the nominal volume
[3] The rating details are based on the composite ratings

Property financing volume[4] (amounts drawn)

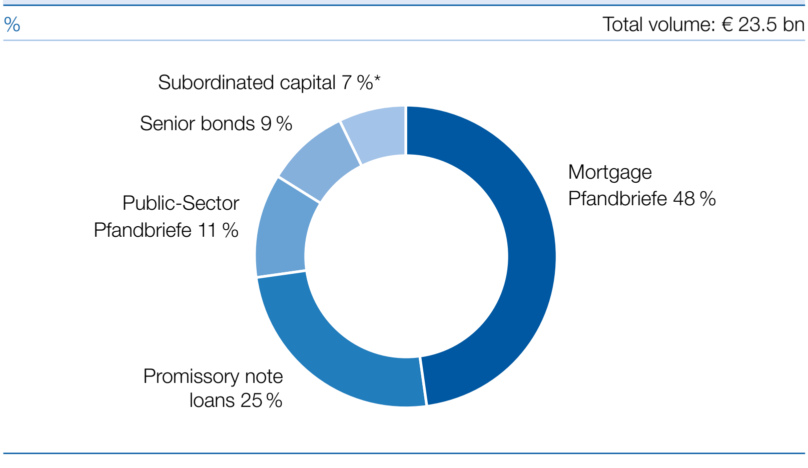


Average LTV of property financing[4]



[4] Excluding former WestImmo's private client business and local authority lending business
Note that the loan-to-value ratios are calculated on the basis of market values, including supplementary collateral with sustainable value.

Capital market funding mix as at 31 September 2017



* Incl. AT1 bond

The total issuance volume of € 2.1 billion comprised € 1.7 billion in Mortgage Pfandbriefe, and € 0.4 billion in uncovered issues.

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

Equity

Aareal Bank Group's total equity as disclosed in the statement of financial position amounted to € 2,884 million as at 30 September 2017 (31 December 2016: € 3,129 million), comprising € 300 million for the Additional Tier 1 (AT 1) bond. Due to the repayment of the Capital Funding Trust in the first quarter of the year, non-controlling interests were reduced to € 1 million (31 December 2016: € 242 million).

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).

Regulatory capital

	30 Sep 2017	31 Dec 2016
€ mn		
Common Equity Tier 1 (CET1)	2,245	2,351
Tier 1 (T1)	2,523	2,896
Total capital (TC)	3,443	3,994
%		
Common Equity Tier 1 ratio (CET1 ratio)	17.7	16.2
Tier 1 ratio (T1 ratio)	19.9	19.9
Total capital ratio (TC ratio)	27.1	27.5

Analysis of risk-weighted assets (RWA)

30 September 2017

	EAD	Risk-weighted assets (RWA)			Regulatory capital requirements
		AIRBA	CRSA	Total	
€ mn					
Credit risks	**44,780**	**9,084**	**1,707**	**10,791**	**863**
Companies	27,527	6,905	863	7,768	621
Institutions	2,901	423	14	437	35
Public-sector entities	12,404	0	20	20	2
Other	1,948	1,756	810	2,566	205
Market price risks				**241**	**19**
Credit Valuation Adjustment				**220**	**18**
Operational risks				**1,433**	**115**
Total	**44,780**	**9,084**	**1,707**	**12,685**	**1,015**

31 December 2016

€ mn	EAD	Risk-weighted assets (RWA) AIRBA	CRSA	Total	Regulatory capital requirements
Credit risks	**48,844**	**9,729**	**2,665**	**12,394**	**991**
Companies	30,094	7,737	1,741	9,478	758
Institutions	3,819	346	85	431	34
Public-sector entities	12,795	0	22	22	2
Other	2,136	1,646	817	2,463	197
Market price risks				**122**	**10**
Credit Valuation Adjustment				**254**	**20**
Operational risks				**1,770**	**142**
Total	**48,844**	**9,729**	**2,665**	**14,540**	**1,163**

Risk Report

Aareal Bank Group Risk Management

The Annual Report 2016 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 duly acknowledged by the Supervisory Board, provides the conceptual framework for Aareal Bank Group's risk management. Taking this as a basis, and strictly considering 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, adopted by the Management Board, and duly acknowledged by 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 Group 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 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 Capital Requirements Regulation

Risk-bearing capacity of Aareal Bank Group as at 30 September 2017
– Going-concern approach –

€ mn	30 Sep 2017	31 Dec 2016
Own funds for risk cover potential	2,623	2,598
less 7.75 % (31 Dec 2016: 8 %) of RWA (Tier 1 capital (T1))	870	1,477
Freely available funds	**1,753**	**1,121**
Utilisation of freely available funds		
Credit risks	260	317
Market risks	166	207
Operational risks	86	106
Investment risks	21	24
Other risks	174	–
Total utilisation	**707**	**654**
Utilisation as a percentage of freely available funds	**40 %**	**58 %**

(CRR). Freely available funds increased significantly during the period under review. Firstly, this was due to portfolio planning; secondly, Aareal Bank further refined its procedures, defining Tier 1 (T1) capital (as defined by the CRR) at a level of 7.75 % of forecast risk-weighted assets (RWA) as a deductible, in accordance with regulatory requirements. Other risks such as migration or FX lending risk are no longer deducted as a buffer, but included as risk exposure. Only free own funds exceeding this level are applied as potential risk cover, of which a further 10 % is deducted. This deduction is not applied to risk limits, but retained for risk types that cannot be quantified (for example, business risks).

We adopt a 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 Tier 1 ratio of 7.75 % of RWA, 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 following table summarises the Group's overall risk-bearing capacity as at 30 September 2017.

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

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

Aareal Bank employs various risk classification procedures for the initial, regular, or event-driven assessment of counterparty credit 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 outside the Sales units.

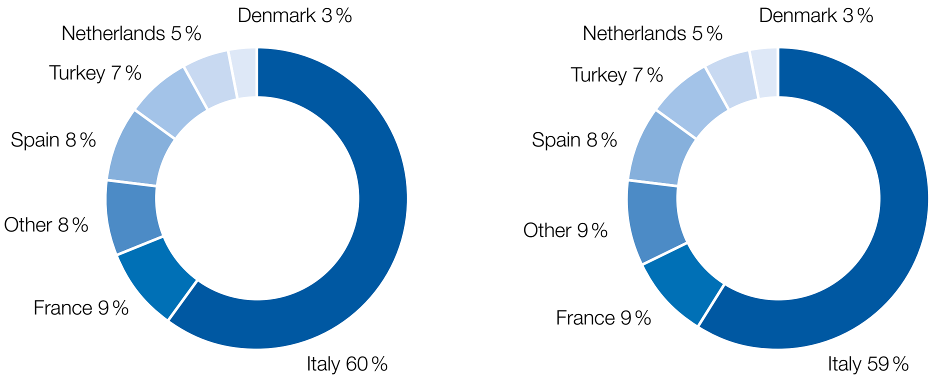
Methods used to measure, control and monitor concentration and diversification effects on a portfolio level include two different credit risk models. Based on these models, the Bank's decision-makers are regularly informed of the performance and risk content of property financing exposures, and of business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

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.

Individually impaired property financing[1)]

by country (%) 30 Sep 2017: 100 % = € 1.3 bn | 31 Dec 2016: 100 % = € 1.4 bn



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

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 and manage” strategy in managing its credit portfolio – with the primary objective of holding loans extended on its balance sheet until maturity; at the same time, targeted measures – such as syndication – are deployed for actively managing the portfolio and the risks involved.

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 by the Bank's senior management. The Risk Controlling division is responsible for the continuous monitoring of country limits and limit utilisation, and for periodical reporting.

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. Commodities are irrelevant for the Bank's business. Hence, the primary market price risk exposures are related to the relevant risk parameters of 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 numerous 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 Group's consolidated 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.

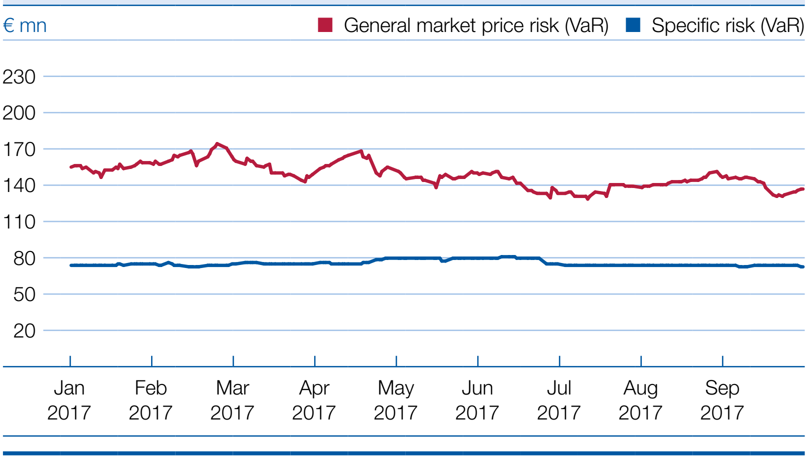
When interpreting the VaR figures stated below, it should be taken into account that these refer to the overall portfolio (thus including all non-trading positions as defined in IFRSs). Hence, the analysis provided represents a very extensive disclosure of market price risks by industry standards.

€ mn	MAX	MIN	Mean	Limit
Year-to-date (full previous year) **95 %, 250-day holding period**				
Aareal Bank Group – general market price risk	173.6 (305.0)	127.7 (161.1)	147.5 (224.5)	– (–)
Group VaR (interest rates)	127.6 (211.6)	85.8 (103.0)	102.0 (149.5)	– (–)
Group VaR (FX)	98.8 (185.9)	68.9 (102.2)	83.9 (135.5)	– (–)
VaR (investment fund and equities)	4.8 (5.8)	3.2 (3.5)	4.0 (4.6)	20.0 (20.0)
Aggregate VaR in the trading book	0.0 (0.0)	0.0 (0.0)	0.0 (0.0)	5.0 (5.0)
Group VaR (specific risks)	79.8 (85.9)	71.5 (62.8)	74.6 (73.3)	– (–)
Group funding risk	26.2 (23.0)	7.6 (17.2)	17.5 (19.4)	– (–)
Aggregate VaR – Aareal Bank Group	204.6 (311.5)	159.6 (174.0)	182.9 (237.5)	390.0 (390.0)

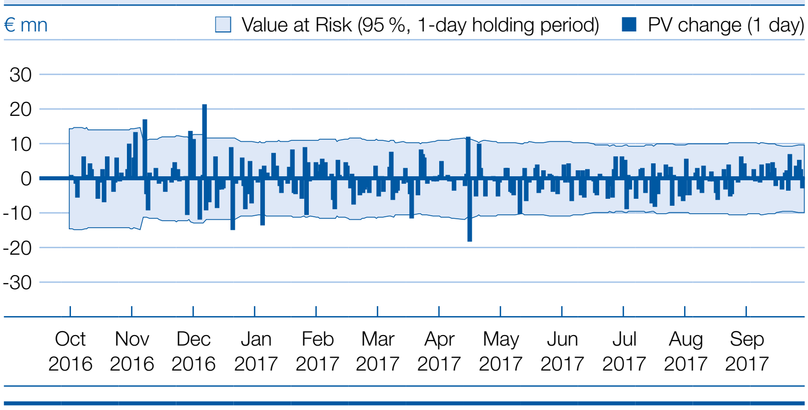
To ensure that Aareal Bank's figures are comparable to those published by other institutions, the risk parameters shown below were determined for a one-day holding period:

€ mn	MAX	MIN	Mean	Limit
Year-to-date (full previous year) 95 %, 1-day holding period				
Aareal Bank Group – general market price risk	11.0 (19.3)	8.1 (10.2)	9.3 (14.2)	– (–)
Group VaR (interest rates)	8.1 (13.4)	5.4 (6.5)	6.4 (9.5)	– (–)
Group VaR (FX)	6.3 (11.8)	4.4 (6.5)	5.3 (8.6)	– (–)
VaR (investment fund and equities)	0.3 (0.4)	0.2 (0.2)	0.3 (0.3)	1.3 (1.3)
Aggregate VaR in the trading book	0.0 (0.0)	0.0 (0.0)	0.0 (0.0)	0.3 (0.3)
Group VaR (specific risks)	5.0 (5.4)	4.5 (4.0)	4.7 (4.6)	– (–)
Group funding risk	1.7 (1.5)	0.5 (1.1)	1.1 (1.2)	– (–)
Aggregate VaR – Aareal Bank Group	12.9 (19.7)	10.1 (11.0)	11.6 (15.0)	24.7 (24.7)

General market price risk and specific risk during 2017



Present values and 1-day VaR during the course of 2016/2017



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 remained unchanged during the quarter under review; no limit breaches were detected.

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). Four 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 during the quarter under review.

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. Risk Controlling prepares a daily liquidity report submitted to responsible members of the Management Board. In addition, the entire Management Board is informed on a monthly basis, within the scope of an extensive risk report.

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. Further details are provided in the comments on the Bank's liquidity in the section on "Refinancing and Equity".

Operational risks

The Bank defines operational risk as the threat of losses caused by inappropriate internal procedures, human resources and systems (or their failure), or through external events. This definition also includes legal risks. To the extent that they are caused by operational risks, model, strategic and reputational risks are also taken into consideration within this type of risk. Systemic risks (or their impact on operational risks) are not affected by this.

Aareal Bank's legal department 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 quarterly 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 quarterly basis. Moreover, information about legal risks is included in operational risk reporting. 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 2016 Annual Report contains a detailed description of controlling tools employed by the Bank to manage operational risk, plus the relevant responsibilities.

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

In the Report on Expected Developments, Aareal Bank presents the macro-economic environment as well as sector-specific and business developments, including Group targets, considering the resulting opportunities.

Macro-economic environment

Developments for the economy, as well as for financial and capital markets, are exposed to diverse risks and threats – which also have an impact on the commercial property markets. The economic forecast as at the end of September 2017 is characterised by significant uncertainty, such as geopolitical risks and protectionist economic policies. Furthermore, falling commodity prices and weak growth in China could burden the economy.

The low interest rate environment continues to be a risk factor in many markets, as it harbours risks for financial stability of a systemic dimension, should it persist for a longer period. Low interest rates can lead to a misallocation of investment capital, possibly resulting in asset-price bubbles. Moreover, market participants are encouraged to take on higher levels of risk. Sudden changes in interest rates may trigger a revaluation and changes in investor behaviour, potentially leading to a collapse in asset prices. A longer-lasting period of low interest rates complicates an exit from such an environment, heightening the risks for the financial and capital markets. Low interest rates may also entice a scaling back of reform and consolidation efforts in various sectors.

A sharp increase in interest rates entails considerable risk: an excessively quick and sharp rise can hamper investments, and may have negative implications for asset prices. Emerging economies in particular will have to face capital outflows, and may have to raise their own interest rates. Although financial market players are expecting interest rates to rise further in the US, the extent – and possible resulting financial market volatility – is still an unknown factor. Turmoil in the financial and capital markets may still hurt the global economy.

Political uncertainty in the US holds the risk of negative developments, which may – should they affect relevant economic sectors – lead to recession. Furthermore, in the wake of the change of government in the US, many economic players had anticipated growth due to lower taxes and reduced regulatory requirements. However, these expectations may not fully materialise. Therefore, corrections could occur on those financial and capital markets where the aforementioned expectations have led to currency or price increases.

A major risk factor in Europe is the impact of the UK's exit from the EU (Brexit). Despite the minimal economic impact visible until now, we continue to see a high level of economic risk for the UK, as well as for the EU. The exit of further countries from the EU cannot be ruled out; in this context, political uncertainty in Spain also needs to be mentioned. A separation of the Autonomous Community of Catalonia from the Kingdom of Spain might have negative economic consequences, which are as yet difficult to assess. The difficult political situation in Turkey, which burdens the Turkish economy, poses an additional risk.

The sovereign debt crisis might still raise its head again in Europe: the problem of high levels of indebtedness continues to exist. Diverging monetary policy between the US and the euro zone, as well as political reorientation, could also heighten that risk.

In China, there is continued danger that the sharp increase in levels of private debt could lead to a pronounced market correction. Despite a slight easing of price pressure on the residential property market, the danger of a far-reaching market correction still exists.

Economy

Despite the high number of existing uncertainty factors and burdens, economic momentum is expected to be slightly stronger than in the previous year. The growth rate of real global economic output is expected to slightly exceed the levels seen during 2016. However, risks and uncertainty factors, were they to materialise to a substantial extent, could mute the economic development, or even cause recessive tendencies in various regions.

In the euro zone, economic development is expected to remain stable during the course of the year. Sentiment indicators are signalling a strengthening of industrial production and export. It is however uncertain whether private consumption will be as strong as last year, due to increased inflation. Not least due to the robust growth in the first half of the year, we anticipate a slightly higher growth rate for 2017 compared to the previous year, despite structural problems in some euro zone countries having a dampening effect. In line with our projections for the region as a whole, most of the euro zone countries relevant to Aareal Bank should show moderate to good economic development. Real GDP growth is anticipated to be lowest in Belgium and Italy, with a slightly higher growth rate expected in France. Prospects for Germany are comparable to the euro zone average, whereas growth perspectives for Austria, Finland, the Netherlands and Spain are relatively favourable by comparison.

In 2017, the economic development of the EU as a whole is anticipated to be similar to that of the euro zone countries. Growth is expected to remain high in Sweden, albeit significantly less so than in the previous two years. For the UK, we expect economic growth in line with last year's levels. For Denmark, we anticipate slightly accelerated economic growth. The Polish economy should continue its strong growth in the current year.

Economic growth in Turkey is expected to be slightly higher this year, compared to 2016; even though, historically, it is on a relatively low level. Due to the political situation, the outlook is clouded by a high degree of uncertainty. Slightly positive growth can be expected for Russia in this year – following several years of recession. The modest increase in oil prices provides support, while the ongoing political conflicts and a lack of structural reforms continue to have a dampening effect.

As seen in the previous year, the US economy is expected to receive support from private consumption (which benefits from increases in wages and employment) this year. Corporate investments should contribute slightly more than in 2016. Even though natural disasters during the third quarter of 2017 will initially burden growth to some extent, the robust economy is likely to absorb the anticipated interest rate hikes; uncertainty remains with regard to the course of economic policy. In Canada, the negative effect of lower investments in the oil industry should diminish. Moderately rising external demand is increasingly providing support. However, private consumption is expected to be weakened by rising interest rates and rising inflation. Overall, we expect a moderate increase in real economic growth for Canada, compared to last year's figure.

In China, this year's growth will be on a par with the previous year's levels. Curbing factors are the slowdown in the housing boom, the targeted reduction of over-capacity, especially in heavy industry, and the transition to an overall lower investment ratio. We are still witnessing uncertainty with regard to the increase of macro-economic debt. In addition, the Chinese economic cycle could slow down.

Against a background of a positive economic development, we expect most labour markets across the euro zone as well as in other European countries to register slowly decreasing or virtually stagnating unemployment rates for 2017. In the US, unemployment should remain at a cyclical low.

Financial and capital markets, monetary policy and inflation

The risks and uncertainty factors we have listed so far also apply to the financial and capital markets this year. This includes, in particular, political events, but also any of the aforementioned risks which could, were they to materialise to a substantial extent, cause turbulence on the financial and capital markets. In the current environment, we assume volatility will remain moderate overall. We continue to expect that financial and capital markets will remain receptive towards securities issues and refinancings.

The extremely expansive monetary policy pursued in the euro zone will remain intact this year. This is underscored by the ECB's decision (taken in 2016) to expand the scope of its asset-buying programme, and this year's decision to extend the duration of the programme until at least September 2018, together with further measures. The ECB will cut the monthly volume of purchases by half from January 2018 onwards. Various other European central banks, such as the Swedish Riksbank, are also likely to abide by their expansive fiscal policy during 2017. In the US however, a further interest rate move is anticipated for this year, whilst we believe that the Bank of England is likely to refrain from any interest rate adjustments beyond the 25 bp hike in November this year. Also, it will likely adhere to its cautious attitude regarding the exit from the EU.

In the US, further slowly rising interest rates are on the horizon for 2017, in light of further key interest rate hikes. Although this may place upside pressure on interest levels in the euro zone and other EU countries, European interest rate levels are expected to remain very low during the remainder of the year given the ECB's extremely loose monetary policy stance.

Inflation will increase noticeably in the euro zone and the other EU member states this year – in particular due to slightly stronger oil prices and improved employment rates. However, in the euro zone, we expect an inflation rate clearly below 2 % to prevail for the full year 2017. For the US, we expect the annual average of inflation to be slightly higher than in the euro zone, and we are assuming a value of just over zero per cent for Japan. The Chinese rate of inflation is expected to close in on 2 %, a moderate price increase.

Regulatory environment

The trend towards a tighter regulatory framework in the banking business is set to persist during the coming years. Numerous initiatives, such as the revision of the Credit Risk Standard Approach (CRSA), the Internal Ratings-based Approaches (IRBA) and the basic approaches for operational risk and the capital floor rules are currently under discussion. EBA has also finalised its Guidelines on the collection of information related to the Internal Capital Adequacy Assessment Process (ICAAP) and the Internal Liquidity Adequacy Assessment Process (ILAAP). In addition, the Single Supervisory Mechanism (SSM) has developed expectations regarding the structure of ICAAP and ILAAP based on a multi-year plan.

The ECB will also review the internal model of Pillar I (Target Review of Internal Models) in 2017, whose exact impact on banks – and the consequences – cannot be fully assessed at present.

Regulators have yet to come up with final details for some of these additional regulatory requirements; hence, various technical standards, guidelines and regulations still have to be finalised. In addition, EBA published a consultation paper in November 2016 on "Guidelines on PD estimation, LGD estimation and the treatment of defaulted exposures". The EU Commission made proposals to revise supervisory regimes (CRR, CRD IV, BRRD and SRMR) that implement – in particular – international banking supervision rules of the Basel Committee and the FSB (Financial Stability Board) in Europe.

To facilitate the timely implementation, we have already continued to pursue the individual issues in numerous projects – devoting considerable resources to this task.

Moreover, the increasing volatility of requirements presents an additional challenge for institutions: besides the new requirements mentioned by way of example, this volatility is particularly a function of the concrete specifications for instruments implemented by the ECB and/or the national supervisory authorities. For instance, the capital buffers to be set on a national level (the anticyclical buffer and the buffer for systemic risks), or the annual results of the Supervisory Review and Evaluation Process (SREP) for individual banks, can only be planned to a certain extent. Moreover, these instruments may lead to changes in a bank's individual capital requirements, at short notice.

Sector-specific and business developments

Structured Property Financing segment

Commercial property will continue to be a sought-after asset class in many markets until the end of 2017. Thus, global transaction volumes should remain on a high level, albeit slightly lower overall when compared to the particularly high levels seen in the two previous years. Transaction volumes may decline significantly in individual markets, such as France and Poland, whilst increasing further in others, e.g. in Germany and Spain. Given the shortage of available first-class properties on offer, and rising total revenue requirements, investor interest in properties outside the top segment will likely increase compared to previous years. Investor demand is thus expected to continue to support performance this year. Nonetheless, commercial property markets are also exposed to major risks and threats. An excessively sharp interest rate hike – originating from the US – may have a negative effect on performance. Moreover, other uncertainty factors and risks in the macro-economic environment are also relevant for commercial property markets.

Several factors will impact the market value[1] of commercial property during the remainder of the year. Whilst the stable economy and low interest rate environment will support property values, political uncertainty and a potentially significant interest rate increase can reduce values. Whilst expansive monetary policy supports the upward trend in market values, which has now been intact for a very long time, market cycles have not been invalidated. This means that cyclical downturns are possible as well.

We therefore anticipate a largely stable development in the market values of commercial property in many markets this year. However, the combination of the existing low interest rate environment and adjustments to the (often very low) returns on investment, given potential sharp interest rate hikes, pose the risk of a correction to the market values of commercial property.

We expect a stable development of market values in most European countries in 2017, including Germany, France, Italy, the Netherlands and Poland. Deviating from this, we expect a slightly positive development owing to the good economic situation in Denmark and Spain. The situation in the UK is subject to uncertainty because of the Brexit vote. Market values could fall in some sub-markets, although we anticipate a stable development overall. There is political uncertainty in Turkey, which is likely to have a negative impact on the market values of commercial property.

Following the sharp decline in property values in Russia in recent years, we believe these will stabilise in the current year due to the slight economic recovery.

In the US, values are expected to show a slightly positive performance overall, on account of the relatively good economic prospects. Increasing interest rates pose certain risks for this development. We expect a stable performance in Canada.

In China, market values for commercial property are expected to remain stable.

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

The trends described above are expected to apply to office, retail and logistics properties.

We expect a slightly positive development in 2017 on the hotel markets of Europe's most significant economic centres. Paris should see a notable increase in occupancy ratios and average revenues per available room, after terrorist attacks had caused figures to decline last year. Average revenues per available room are likely to increase slightly in the other big European cities, such as London and Madrid. The difficult political situation in Turkey will continue to have negative implications for the hotel markets.

We believe a slight improvement on average in revenues per available room is likely in the US, with stable or slightly lower occupancy ratios. However, this development might be dampened slightly by natural disasters in the affected regions of the US. We expect slight increases to both indicators in Canada, not least thanks to the 150th anniversary celebrations of the foundation of the Canadian Confederation.

In Asia, we anticipate occupancy ratios and average revenues per available room to remain stable throughout 2017 in the hotel markets of many metropolitan areas.

The intense competition in commercial property financing is also likely to persist in many markets during the current year, so that we assume that lenders will be willing to lower margins. We anticipate a stable development in loan-to-value ratios across the various regions. Banks are expected to continue adhering to their preference for financing first-class properties in top locations. Investors' readiness to finance properties outside top locations will increase.

We have incorporated various market aspects, amongst other factors, in our assessment of anticipated new business volumes for the current year. For the Structured Property Financing segment, we are targeting new business of between € 7 billion and € 8 billion for the 2017 financial year. Aareal Bank Group's property financing portfolio should amount to between € 25 billion and € 28 billion at the end of 2017, subject to currency fluctuations.

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

Consulting/Services segment

Housing Industry division

We expect developments within the German housing industry and commercial property sector to remain stable until the end of the year. Companies in this sector are expected to continue pursuing sustainable portfolio optimisation.

GdW member companies plan to increase investments by close to 17% this year, to more than € 16 billion. Driven by strong demand for newly-built properties, companies plan to boost their new construction investments in particular, by approximately 23 %. Overall, GdW member companies are expected to complete around 28,300 residential units by the end of this year – up by just under 42 % year-on-year.

Thanks to the stable environment for the German economy, the German housing market is expected to continue its positive development in the fourth quarter. Migration trends towards prospering economic areas will slow down in the future, which is expected to translate into lower growth rates for residential property prices.

We see good opportunities during the remainder of 2017 to acquire new clients and to intensify business relationships with our existing client base. This also applies to our payments services for utilities and the waste disposal industry. In addition, in line with our "Aareal 2020" programme for the future, we are investing into the expansion of the "Housing Industry Ecosystem", the cross-sector development of interface products, and the expansion to adjacent ecosystems. We will also examine cooperations with fintech and proptech companies.

We expect the volume of deposits to remain on a high level. The persistent low interest rate environment, which is relevant for the results from our deposit-taking business, will continue to place a significant burden 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

Aareon will continue to pursue its growth strategy during the remainder of 2017 – based on its strategic programme, which is an integral part of Aareal Bank Group's "Aareal 2020" programme for the future. Aareon's consolidated sales revenues are expected to rise slightly, accompanied by a roughly unchanged contribution to Group results. The expansion of the digital solutions of the Aareon Smart World portfolio of products, strengthening the ERP business and tapping new areas of business will be the key growth factors. Investing in the expansion of Aareon Smart World, as well as in measures to further enhance performance and efficiency and to integrate Kalshoven Groep, will slightly increase costs in the 2017 financial year.

Aareon anticipates its advisory business to expand in Germany as the migration of GES clients to the Wodis Sigma ERP solution proceeds as planned. We also believe that sales revenues with digital solutions will continue to grow in 2017: the topic has gained considerably in importance for the housing industry, alongside burgeoning customer interest. Despite significant investments to enhance performance and efficiency, costs in Germany are expected to remain stable in 2017, thanks to savings.

Aareon anticipates maintenance revenues to rise in the Netherlands and in France. Growth will be stimulated by the ongoing market penetration of digital solutions, together with regulatory requirements for digital invoicing and continued success with Platinum maintenance agreements in France. The maintenance business was further strengthened by the acquisitions of Kalshoven Groep B.V. (effective 1 April 2017) and SG2ALL B.V. (31 December 2016). In the UK, Aareon expects sales revenues to remain at the previous year's level, due to intense competition. Sales revenues in Sweden are also expected to be unchanged, reflecting delays in the implementation of projects.

In view of the aforementioned, Aareon expects a slight increase in sales revenues for the 2017 financial year, together with a contribution to consolidated operating profit of between € 34 million and € 35 million.

Group targets

For the 2017 financial year, we continue to see good opportunities to achieve consolidated operating profit in the expected range between € 310 million and € 350 million, including a positive non-recurring effect in the amount of € 50 million recognised in the second quarter, from a subsidiary's reversal of provisions against income. Earnings per share (EpS) are projected in a range between € 2.85 and € 3.30. RoE before taxes for the current year is anticipated between 11 % and 12.5 %; when adjusted for the non-recurring effect mentioned above, the range is between 9 % and 10.5 %. We affirm our medium-term target RoE of around 12 % before taxes.

Consolidated net interest income for the current financial year is expected at between € 620 million and € 660 million, with allowance for credit losses in a range between € 75 million and € 100 million. Net commission income is projected to be between € 195 million and € 210 million. Administrative expenses are expected in a range between € 470 million and € 510 million.

In the Structured Property Financing segment, the credit portfolio is projected to stand at between € 25 billion and € 28 billion by the end of 2017, subject to currency fluctuations. We are targeting new business of between € 7 billion and € 8 billion in the current year. In the Consulting/Services segment, we expect our IT subsidiary Aareon to contribute between € 34 million and € 35 million to consolidated operating profit.

By the end of 2017, we expect the fully phased-in Common Equity Tier 1 (CET1) ratio to be moderately higher than at the end of the last financial year (31 December 2016: 15.7 % – fully phased-in). Further, we expect the Liquidity Coverage Ratio (LCR), which should be at least 100 %, to broadly remain at a very high level.

Consolidated Interim Financial Statements
Statement of Comprehensive Income

Income Statement

€ mn	Notes	1 Jan-30 Sep 2017	1 Jan-30 Sep 2016[1]
Interest income		562	644
Positive interest from financial liabilities		5	1
Interest expenses		73	108
Negative interest from financial assets		8	5
Net interest income	1	**486**	**532**
Allowance for credit losses	2	53	64
Net interest income after allowance for credit losses		**433**	**468**
Commission income		172	164
Commission expenses		27	27
Net commission income	3	**145**	**137**
Net result on hedge accounting	4	-5	4
Net trading income/expenses	5	13	21
Results from non-trading assets	6	0	66
Results from investments accounted for using the equity method		–	0
Administrative expenses	7	388	417
Net other operating income/expenses	8	64	2
Operating profit		**262**	**281**
Income taxes		97	88
Consolidated net income		**165**	**193**
Consolidated net income attributable to non-controlling interests		6	15
Consolidated net income attributable to shareholders of Aareal Bank AG		159	178
Earnings per share (EpS)			
Consolidated net income attributable to shareholders of Aareal Bank AG[2]		159	178
of which: allocated to ordinary shareholders		147	166
of which: allocated to AT1 investors		12	12
Earnings per ordinary share (in €)[3]		2.46	2.78
Earnings per AT1 unit (in €)[4]		0.12	0.12

[1] Previous year's figures were adjusted due to separate disclosure of negative interest

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

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

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

Statement of Comprehensive Income

Reconciliation from Consolidated Net Income to Total Comprehensive Income

€ mn	1 Jan-30 Sep 2017	1 Jan-30 Sep 2016
Consolidated net income	**165**	**193**
Items that will not be reclassified subsequently to profit or loss		
Changes in the reserve from defined benefit plans	**10**	**-56**
Remeasurements	14	-82
Taxes	-4	26
Items that are reclassified subsequently to profit or loss		
Changes in revaluation surplus	**-2**	**8**
Gains and losses on remeasuring AfS financial instruments	-3	10
Reclassifications to the income statement	–	1
Taxes	1	-3
Changes in hedging reserves	**-15**	**11**
Profit/loss from derivatives used to hedge future cash flows	-22	16
Reclassifications to the income statement	0	1
Taxes	7	-6
Changes in currency translation reserves	**-13**	**-6**
Profit/loss from translating foreign operations' financial statements	-13	-7
Reclassifications to the income statement	–	1
Taxes	–	–
Other comprehensive income	**-20**	**-43**
Total comprehensive income	**145**	**150**
Total comprehensive income attributable to non-controlling interests	6	15
Total comprehensive income attributable to shareholders of Aareal Bank AG	139	135

Statement of Comprehensive Income

Income Statement (Quarterly Development)

€ mn	Quarter 3 2017	Quarter 3 2016[1)]
Interest income	188	202
Positive interest from financial liabilities	2	1
Interest expenses	26	25
Negative interest from financial assets	0	3
Net interest income	**164**	**175**
Allowance for credit losses	26	33
Net interest income after allowance for credit losses	**138**	**142**
Commission income	57	52
Commission expenses	9	8
Net commission income	**48**	**44**
Net result on hedge accounting	1	3
Net trading income/expenses	10	4
Results from non-trading assets	0	5
Results from investments accounted for using the equity method	–	0
Administrative expenses	120	127
Net other operating income/expenses	5	3
Operating profit	**82**	**74**
Income taxes	31	23
Consolidated net income	**51**	**51**
Consolidated net income attributable to non-controlling interests	0	5
Consolidated net income attributable to shareholders of Aareal Bank AG	51	46

[1)] Previous year's figures were adjusted due to separate disclosure of negative interest

Statement of Comprehensive Income

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

€ mn	Quarter 3 2017	Quarter 3 2016
Consolidated net income	**51**	**51**
Items that will not be reclassified subsequently to profit or loss		
Changes in the reserve from defined benefit plans	**-1**	**-9**
Remeasurements	-2	-14
Taxes	1	5
Items that are reclassified subsequently to profit or loss		
Changes in revaluation surplus	**2**	**5**
Gains and losses on remeasuring AfS financial instruments	3	5
Reclassifications to the income statement	–	2
Taxes	-1	-2
Changes in hedging reserves	**4**	**2**
Profit/loss from derivatives used to hedge future cash flows	6	5
Reclassifications to the income statement	–	-1
Taxes	-2	2
Changes in currency translation reserves	**-5**	**-4**
Profit/loss from translating foreign operations' financial statements	-5	-4
Reclassifications to the income statement	–	–
Taxes	–	–
Other comprehensive income	**0**	**-6**
Total comprehensive income	**51**	**45**
Total comprehensive income attributable to non-controlling interests	0	5
Total comprehensive income attributable to shareholders of Aareal Bank AG	51	40

Statement of Financial Position

€ mn	Notes	30 Sep 2017	31 Dec 2016
Assets			
Cash funds		2,209	1,786
Loans and advances to banks	9	884	1,583
Loans and advances to customers	10	28,481	31,203
Allowance for credit losses	11	-552	-554
Positive market value of derivative hedging instruments		2,053	2,481
Trading assets	12	337	502
Non-trading assets	13	8,899	9,730
Investments accounted for using the equity method		7	0
Intangible assets	14	134	126
Property and equipment	15	251	252
Income tax assets		28	68
Deferred tax assets		172	134
Other assets	16	364	397
Total		**43,267**	**47,708**
Equity and liabilities			
Liabilities to banks	17	1,890	1,703
Liabilities to customers	18	26,898	29,077
Certificated liabilities	19	7,474	8,346
Negative market value of derivative hedging instruments		1,758	2,529
Trading liabilities	20	269	652
Provisions	21	580	680
Income tax liabilities		26	71
Deferred tax liabilities		28	28
Other liabilities	22	197	127
Subordinated capital	23	1,263	1,366
Equity	24, 25, 26		
Subscribed capital		180	180
Capital reserves		721	721
Retained earnings		1,750	1,734
AT1 bond		300	300
Other reserves		-68	-48
Non-controlling interests		1	242
Total equity		2,884	3,129
Total		**43,267**	**47,708**

Statement of Changes in Equity

€ mn	Subscribed capital	Capital reserves	Retained earnings	AT1 bond	Other reserves: Reserve from remeasurements of defined benefit plans	Other reserves: Revaluation surplus	Other reserves: Hedging reserves	Other reserves: Currency translation reserves	Total	Non-controlling interest[1]	Equity
Equity as at 1 Jan 2017	**180**	**721**	**1,734**	**300**	**-100**	**29**	**17**	**6**	**2,887**	**242**	**3,129**
Total comprehensive income for the period			159		10	-2	-15	-13	**139**	6	**145**
Payments to non-controlling interests										-6	**-6**
Dividends			-120						**-120**		**-120**
AT1 coupon			-16						**-16**		**-16**
Other changes			-7						**-7**	-241	**-248**
Equity as at 30 Sep 2017	**180**	**721**	**1,750**	**300**	**-90**	**27**	**2**	**-7**	**2,883**	**1**	**2,884**

[1] Reduction due to repayment of the Capital Funding Trust

€ mn	Subscribed capital	Capital reserves	Retained earnings	AT1 bond	Other reserves: Reserve from remeasurements of defined benefit plans	Other reserves: Revaluation surplus	Other reserves: Hedging reserves	Other reserves: Currency translation reserves	Total	Non-controlling interest	Equity
Equity as at 1 Jan 2016	**180**	**721**	**1,633**	**300**	**-80**	**28**	**13**	**7**	**2,802**	**242**	**3,044**
Total comprehensive income for the period			178		-56	8	11	-6	**135**	15	**150**
Payments to non-controlling interests										-15	**-15**
Dividends			-99						**-99**		**-99**
AT1 coupon			-16						**-16**		**-16**
Other changes											
Equity as at 30 Sep 2016	**180**	**721**	**1,696**	**300**	**-136**	**36**	**24**	**1**	**2,822**	**242**	**3,064**

Statement of Cash Flows (condensed)

€ mn	2017	2016
Cash and cash equivalents as at 1 January	**1,786**	**1,282**
Cash flow from operating activities	-155	1,094
Cash flow from investing activities	824	496
Cash flow from financing activities	-246	-109
Total cash flow	**423**	**1,481**
Effect of changes in exchange rates	0	0
Cash and cash equivalents as at 30 September	**2,209**	**2,763**

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 quarterly financial report for the period ended 30 September 2017 was prepared pursuant to the provisions of section 37w of the German Securities Trading Act (Wertpapierhandelsgesetz – "WpHG") in conjunction with section 37y no. 2 of the WpHG and was approved for publication by the Management Board on 8 November 2017. It comprises the present interim condensed consolidated financial statements, as well as an interim group management report.

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 315e (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.

Apart from the acquisition of Kalshoven Groep B.V. and the investment in Mount Street Group Limited, there were no other material changes to the basis of consolidation during the period under review. WestImmo has transferred its banking operations, together with the related loan and securities portfolios, to Aareal Bank by way of a split-off. The split-off became effective upon entry into WestImmo's Commercial Register as at 30 June 2017. Following the split-off, WestImmo has assumed the function of a loan servicing entity and has operated under the name of "Westdeutsche Immobilien Servicing AG" since that date.

Accounting policies

The accounting policies applied in the preparation of the consolidated financial statements 2016 were also applied in the preparation of these condensed interim consolidated financial statements, including the calculation of comparative figures. There were no new financial reporting standards (IASs/IFRSs) that were required to be applied for the first time.

As described in the 2016 Annual Report, IFRS 9 Financial Instruments introduces new rules for the accounting of financial instruments and has to be applied for the first time as at 1 January 2018. The transition results in various effects that have to be recognised in equity.

The first-time application of IFRS 9 will – according to our current assessment – result in positive equity effects from the reversal of the revaluation surplus in connection with the reclassification of IAS 39 financial instrument categories according to the new business models under IFRS 9; furthermore, we also expect negative equity effects from an increase in risk provisioning due to the new impairment rules. We do not expect any material effects on Aareal Bank Group's statement of financial position from the new rules on hedge accounting. The reclassification of financial instruments according to the business models under IFRS 9 may lead to additional equity effects. The structure and allocation of financial instruments to the business models is in the responsibility of the management, and will be determined as at 31 December 2017. Overall, we only expect minor transition effects on equity as disclosed in the consolidated statement of financial position. Furthermore, the transition effects are subject to additional criteria, such as market developments, the credit quality of our clients, and changes in inventory. Therefore, Aareal Bank Group is not able to precisely forecast the effects from the adoption of IFRS 9 before the date of first-time application (1 January 2018).

Notes to the Statement of Comprehensive Income

(1) Net interest income

€ mn	1 Jan-30 Sep 2017	1 Jan-30 Sep 2016[1]
Interest income from		
Property loans	507	571
Promissory note loans	5	6
Other lending and money market operations	40	45
Debt securities and other fixed-income securities	10	22
Current dividend income	0	0
Total interest income	**562**	**644**
Positive interest from financial liabilities	**5**	**1**
Interest expenses for		
Bonds issued	20	26
Registered Pfandbriefe	3	9
Promissory note loans	24	32
Subordinated capital	21	23
Money market transactions	5	17
Other interest expenses	0	1
Total interest expenses	**73**	**108**
Negative interest from financial assets	**8**	**5**
Total	**486**	**532**

[1] Previous year's figures were adjusted due to separate disclosure of negative interest.

At € 486 million, net interest income was lower than the previous year's figure of € 532 million. This was largely due to the scheduled reduction of the former WestImmo and Corealcredit portfolios, high early repayments, as well as a lack of suitable investment opportunities for our liquidity reserves, given the persistent low interest rate levels, and exchange rate fluctuations.

(2) Allowance for credit losses

€ mn	1 Jan-30 Sep 2017	1 Jan-30 Sep 2016
Additions	65	94
Reversals	13	27
Direct write-offs	17	14
Recoveries on loans and advances previously written off	16	17
Total	**53**	**64**

Allowance for credit losses amounted to € 53 million (9 m 2016: € 64 million) and was thus in line with our expectations. It mainly comprised net additions to specific allowance for credit losses of € 51 million. Please also refer to our explanations in Note (11).

(3) Net commission income

€ mn	1 Jan-30 Sep 2017	1 Jan-30 Sep 2016
Commission income from		
Consulting and other services	157	150
Trustee loans and administered loans	0	1
Securities transactions	–	–
Other lending and money market transactions	8	6
Other commission income	7	7
Total commission income	**172**	**164**
Commission expenses for		
Consulting and other services	24	22
Securities transactions	1	1
Other lending and money market transactions	0	1
Other commission expenses	2	3
Total commission expenses	**27**	**27**
Total	**145**	**137**

Net commission income increased to € 145 million (9 m 2016: € 137 million), which was mainly due to higher sales revenue at Aareon.

(4) Net result on hedge accounting

€ mn	1 Jan-30 Sep 2017	1 Jan-30 Sep 2016
Ineffective portion of fair value hedges	-1	2
Ineffective portion of cash flow hedges	-4	2
Ineffective portion of net investment hedges	0	–
Total	**-5**	**4**

(5) Net trading income/expenses

€ mn	1 Jan-30 Sep 2017	1 Jan-30 Sep 2016
Net income/expenses from positions held for trading	6	17
Currency translation	7	4
Total	**13**	**21**

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

(6) Results from non-trading assets

€ mn	1 Jan-30 Sep 2017	1 Jan-30 Sep 2016
Result from debt securities and other fixed-income securities	0	5
of which: Loans and receivables (LaR)	–	5
Held to maturity (HtM)	–	–
Available for sale (AfS)	0	0
Result from equities and other non-fixed income securities	0	0
of which: Available for sale (AfS)	0	0
Results from equity investments (AfS)	0	61
Total	**0**	**66**

(7) Administrative expenses

€ mn	1 Jan-30 Sep 2017	1 Jan-30 Sep 2016
Staff expenses	240	246
of which: Wages and salaries	198	202
Social security contributions	25	25
Pensions	17	19
Other administrative expenses	133	155
Depreciation, amortisation and impairment of property and equipment and intangible assets	15	16
Total	**388**	**417**

At € 388 million (9 m 2016: € 417 million), administrative expenses were reduced as expected, in spite of provisions recognised for personnel measures resulting from the optimisation of processes and structures, within the scope of the "Aareal 2020" programme for the future. The decline was due in particular to lower integration costs and lower running costs for former WestImmo, as well as lower project expenditure.

(8) Net other operating income/expenses

€ mn	1 Jan-30 Sep 2017	1 Jan-30 Sep 2016
Income from properties	49	30
Income from the reversal of provisions	72	1
Income from goods and services	0	1
Miscellaneous	12	14
Total other operating income	**133**	**46**
Expenses for properties	41	29
Expenses for services used	0	0
Expenses for other taxes	5	3
Miscellaneous	23	12
Total other operating expenses	**69**	**44**
Total	**64**	**2**

Net other operating income of € 64 million (9 m 2016: € 2 million) mainly resulted from net reversals of provisions (€ 50 million net, comprising income from the reversal of provisions and other expenses) in connection with the final agreement on contractual issues with a third party, which were still pending when Aareal Bank Group acquired former Corealcredit, and the release of tax assessment notes. Aareal Bank Group disclosed a corresponding income tax expense of € 26 million.

Notes to the Statement of Financial Position

(9) Loans and advances to banks

€ mn	30 Sep 2017	31 Dec 2016
Money market receivables	800	1.458
Promissory note loans	77	119
Other loans and advances	7	6
Total	**884**	**1,583**

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

(10) Loans and advances to customers

€ mn	30 Sep 2017	31 Dec 2016
Property loans[1]	25,539	26,833
Promissory note loans	1,335	1,442
Other loans and advances	1,607	2,928
Total	**28,481**	**31,203**

[1] Excluding € 0.9 billion in private client business (31 December 2016: € 1.1 billion) and € 0.6 billion in local authority lending business by former WestImmo (31 December 2016: € 0.6 billion), which are reported under "Other loans and advances".

Loans and advances to customers are generally allocated to the measurement category "Loans and receivables" (LaR). Property loans acquired or incurred principally for the purpose of selling or repurchasing them in the near term with a syndication covenant are allocated to the measurement category "Held for trading" (HfT).

(11) Allowance for credit losses

30 September 2017

€ 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	**435**	**119**	**554**	**5**	**559**
Additions	61	4	**65**	–	**65**
Utilisation	30	–	**30**	0	**30**
Reversals	10	–	**10**	3	**13**
Unwinding	22	–	**22**	–	**22**
Changes in the basis of consolidation	–	–	**–**	–	**–**
Currency adjustments	-4	-1	**-5**	0	**-5**
Allowance for credit losses as at 30 September	**430**	**122**	**552**	**2**	**554**

30 September 2016

€ 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	**412**	**116**	**528**	**14**	**542**
Additions	83	11	**94**	–	**94**
Utilisation	11	–	**11**	–	**11**
Reversals	24	–	**24**	3	**27**
Unwinding	23	–	**23**	–	**23**
Changes in the basis of consolidation	–	–	**–**	–	**–**
Currency adjustments	-1	0	**-1**	0	**-1**
Allowance for credit losses as at 30 September	**436**	**127**	**563**	**11**	**574**

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 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.

(12) Trading assets

€ mn	30 Sep 2017	31 Dec 2016
Positive market value of trading assets	337	502
Total	**337**	**502**

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

(13) Non-trading assets

€ mn	30 Sep 2017	31 Dec 2016
Debt securities and other fixed-income securities	8,897	9,728
of which: Loans and receivables (LaR)	2,815	3,259
Held to maturity (HtM)	402	522
Available for sale (AfS)	5,680	5,947
Equities and other non-fixed income securities	1	1
of which: Available for sale (AfS)	1	1
Interests in affiliated companies (AfS)	–	–
Other investments (AfS)	1	1
Total	**8,899**	**9,730**

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

(14) Intangible assets

€ mn	30 Sep 2017	31 Dec 2016
Goodwill	80	76
Proprietary software	23	22
Other intangible assets	31	28
Total	**134**	**126**

(15) Property and equipment

€ mn	30 Sep 2017	31 Dec 2016
Land and buildings and construction in progress	220	220
Office furniture and equipment	31	32
Total	**251**	**252**

(16) Other assets

€ mn	30 Sep 2017	31 Dec 2016
Properties	202	234
Trade receivables (LaR)	43	50
Miscellaneous	119	113
Total	**364**	**397**

(17) Liabilities to banks

€ mn	30 Sep 2017	31 Dec 2016
Money market liabilities	983	813
Promissory note loans	263	352
Registered mortgage Pfandbriefe	569	496
Registered public-sector Pfandbriefe	67	21
Other liabilities	8	21
Total	**1,890**	**1,703**

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

(18) Liabilities to customers

€ mn	30 Sep 2017	31 Dec 2016
Money market liabilities	13,285	13,696
Promissory note loans	5,556	6,369
Registered mortgage Pfandbriefe	5,415	6,066
Registered public-sector Pfandbriefe	2,642	2,945
Other liabilities	0	1
Total	**26,898**	**29,077**

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

(19) Certificated liabilities

€ mn	30 Sep 2017	31 Dec 2016
Bearer mortgage Pfandbriefe	5,355	5,956
Bearer public-sector Pfandbriefe	45	45
Other debt securities	2,074	2,345
Total	**7,474**	**8,346**

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

(20) Trading liabilities

€ mn	30 Sep 2017	31 Dec 2016
Negative market value of trading assets	269	652
Total	**269**	**652**

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

(21) Provisions

€ mn	30 Sep 2017	31 Dec 2016
Provisions for pensions and similar obligations	358	359
Other provisions and contingent liabilities	222	321
Total	**580**	**680**

Changes in the discount rate require a revaluation of the amount of obligations. This is recognised directly in Other comprehensive income, under Changes in the reserve from defined benefit plans. Other provisions include € 24 million recognised for planned personnel measures resulting from the optimisation of processes and structures, within the scope of the ”Aareal 2020” programme for the future.

(22) Other liabilities

€ mn	30 Sep 2017	31 Dec 2016
Liabilities from outstanding invoices	7	10
Deferred income	13	15
Liabilities from other taxes	15	17
Trade payables (LaC)	13	30
Other liabilities (LaC)	149	55
Total	**197**	**127**

(23) Subordinated capital

€ mn	30 Sep 2017	31 Dec 2016
Subordinated liabilities	1,059	1,122
Profit-participation certificates	12	50
Contributions by silent partners	192	194
Total	**1,263**	**1,366**

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

(24) Equity

€ mn	30 Sep 2017	31 Dec 2016
Subscribed capital	180	180
Capital reserves	721	721
Retained earnings	1,750	1,734
AT1 bond	300	300
Other reserves		
Reserve from remeasurements of defined benefit plans	-90	-100
Revaluation surplus	27	29
Hedging reserves	2	17
Currency translation reserves	-7	6
Non-controlling interests	1	242
Total	**2,884**	**3,129**

Due to the repayment of the Capital Funding Trust in the first quarter of the year, non-controlling interests were reduced to € 1 million (31 December 2016: € 242 million).

(25) Treasury shares

No treasury shares were held during the period under review.

(26) Distributions

The Annual General Meeting of Aareal Bank AG held on 31 May 2017 resolved that a partial amount of € 119,714,442.00 of Aareal Bank AG's net retained profit of € 122,214,442.00 for the financial year 2016, as reported under the German Commercial Code (HGB), be used to distribute a dividend of € 2.00 per notional no-par value share.

In addition, on 30 April 2017, the Management Board resolved on a distribution in relation to the AT1 instruments, pursuant to the terms and conditions of the notes.

Within Aareal Bank Group's consolidated statement of financial position, a dividend payment and a distribution on the AT1 bond reduce the retained earnings item within consolidated equity.

Notes to Financial Instruments

(27) 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 individual hierarchy levels is based on the inputs used for fair value measurement.

30 September 2017

€ mn	Fair value total	Fair value level 1	Fair value level 2	Fair value level 3
Loans and advances to customers held for trading	**171**	**–**	**–**	**171**
Positive market value of derivative hedging instruments	**2,053**	**–**	**2,053**	**–**
Assets held for trading	**337**	**–**	**337**	**–**
Trading derivatives	337	–	337	–
Non-trading assets available for sale	**5,681**	**5,651**	**30**	**–**
Fixed-income securities	5,680	5,650	30	–
Equities/funds	1	1	–	–
Negative market value of derivative hedging instruments	**1,758**	**–**	**1,758**	**–**
Liabilities held for trading	**269**	**–**	**269**	**–**
Trading derivatives	269	–	269	–

31 December 2016

€ mn	Fair value total	Fair value level 1	Fair value level 2	Fair value level 3
Loans and advances to customers held for trading	**–**	**–**	**–**	**–**
Positive market value of derivative hedging instruments	**2,481**	**–**	**2,481**	**–**
Assets held for trading	**502**	**–**	**502**	**–**
Trading derivatives	502	–	502	–
Non-trading assets available for sale	**5,948**	**5,918**	**30**	**–**
Fixed-income securities	5,947	5,917	30	–
Equities/funds	1	1	0	–
Negative market value of derivative hedging instruments	**2,529**	**–**	**2,529**	**–**
Liabilities held for trading	**652**	**–**	**652**	**–**
Trading derivatives	652	–	652	–

The fair value of financial instruments is allocated to Level I 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 I that are observable for the financial instrument, either directly or indirectly, are included in Level 2 of the fair value hierarchy. Fair values determined using valuation techniques where one or more material inputs are not based on observable market data are assigned to Level 3 of the fair value hierarchy. Financial instruments are measured using various valuation techniques.

The property finance portfolio included in loans and advances to customers of the "Held for trading" category is measured using the discounted cash flow method for the purpose of the determination of fair value. Discounting of future cash flows of a transaction is based on transaction-specific risk-adjusted interest rates. These are derived on the basis of a virtually risk-free market interest rate for each currency depending on the relevant term, taking into account add-ons for risks specific to the counterparty as well as credit costs. In the case of loans subject to fixed interest rates, the contractually agreed payments are used as future cash flows. The future cash flows for floating-rate loans are derived using the future forward interest rates, taking into account the relevant spread for customer-specific terms and conditions.

In 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 securities are used, or quoted prices on inactive markets for identical or similar securities, 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.

In the first nine months of 2017, there were no material 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 reporting 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.

The fair values of financial instruments recognised at fair value in the statement of financial position that are assigned to Level 3 of the fair value hierarchy amounted to € 171 million, representing additions during the period under review: The associated instruments are loans and advances to customers classified as held for trading where the add-ons for risks specific to the counterparty represent material inputs not observable on the market. An increase / decrease by 1 % would lead to a decrease / increase of the fair value by approximately € 5 million.

(28) 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 Sep 2017	Fair value 30 Sep 2017	Carrying amount 31 Dec 2016	Fair value 31 Dec 2016
Cash on hand and balances with central banks (LaR)	2,209	2,209	1,786	1,786
Loans and advances to banks (LaR)	884	887	1,583	1,590
Loans and advances to customers (LaR)	27,757	29,456	30,649	32,697
Non-trading assets (LaR)	2,815	2,724	3,259	3,144
Other assets (LaR)	82	81	85	84
Total loans and receivables	**33,747**	**35,357**	**37,362**	**39,301**
Loans and advances to customers held for trading	**171**	**171**	**–**	**–**
Non-trading assets held to maturity	**402**	**404**	**522**	**525**
Non-trading assets available for sale	**5,681**	**5,682**	**5,948**	**5,948**
Positive market value of derivative hedging instruments	**2,053**	**2,053**	**2,481**	**2,481**
Assets held for trading	**337**	**337**	**502**	**502**
Liabilities to banks (LaC)	1,890	1,907	1,703	1,719
Liabilities to customers (LaC)	26,898	27,039	29,077	29,040
Certificated liabilities (LaC)	7,474	7,536	8,346	8,361
Other liabilities (LaC)	170	169	97	96
Subordinated capital (LaC)	1,263	1,372	1,366	1,424
Total liabilities measured at amortised cost	**37,695**	**38,023**	**40,589**	**40,640**
Negative market value of derivative hedging instruments	**1,758**	**1,758**	**2,529**	**2,529**
Liabilities held for trading	**269**	**269**	**652**	**652**

(29) 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 or loss during the period under review. The day-one profit or loss is recognised as an item to be deducted from the carrying amount of the respective underlying derivative position:

€ mn	2017	2016
Balance as at 1 January	**12**	**27**
Additions from new transactions	1	0
Reversals through profit or loss in the period	7	12
Changes in basis of consolidation	–	–
Balance as at 30 September	**6**	**15**

(30) 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, the Bank opted for reclassification since there was no longer an active market for the securities concerned (in spite of their good quality), and due to the intention of holding 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 Sep 2017	Fair value 30 Sep 2017	Carrying amount 31 Dec 2016	Fair value 31 Dec 2016
from AfS to LaR	**2,627**	**2,529**	**3,044**	**2,921**
Asset-backed securities	–	–	–	–
Senior unsecured bank bonds	20	20	46	47
Covered bank bonds	112	113	237	239
Public-sector issuers	2,495	2,396	2,761	2,635
Total	**2,627**	**2,529**	**3,044**	**2,921**

If the Bank had not opted for reclassification, this would have had no effect on profit/loss before taxes for the first nine months of the current financial year (9 m 2016: loss of € 6 million), while a loss of € 18 million (9 m 2016: loss of € 41 million) would have been recognised in the revaluation surplus after taxes.

Segment Reporting

(31) Segment Results

	Structured Property Financing		Consulting/Services		Consolidation/Reconciliation		Aareal Bank Group	
	1 Jan - 30 Sep 2017	1 Jan - 30 Sep 2016	1 Jan - 30 Sep 2017	1 Jan - 30 Sep 2016	1 Jan - 30 Sep 2017	1 Jan - 30 Sep 2016	1 Jan - 30 Sep 2017	1 Jan - 30 Sep 2016
€ mn								
Net interest income	494	542	0	0	-8	-10	486	532
Allowance for credit losses	53	64					53	64
Net interest income after allowance for credit losses	**441**	**478**	**0**	**0**	**-8**	**-10**	**433**	**468**
Net commission income	4	5	136	124	5	8	145	137
Net result on hedge accounting	-5	4					-5	4
Net trading income/expenses	13	21		0			13	21
Results from non-trading assets	0	66					0	66
Results from investments accounted for using the equity method				0				0
Administrative expenses[1]	234	266	157	153	-3	-2	388	417
Net other operating income/expenses	62	1	2	1	0	0	64	2
Operating profit	**281**	**309**	**-19**	**-28**	**0**	**0**	**262**	**281**
Income taxes	104	98	-7	-10			97	88
Consolidated net income	**177**	**211**	**-12**	**-18**	**0**	**0**	**165**	**193**
Consolidated net income attributable to non-controlling interests	4	13	2	2			6	15
Consolidated net income attributable to shareholders of Aareal Bank AG	173	198	-14	-20	0	0	159	178
Allocated equity	1,772	1,587	155	133	592	741	2,519	2,461
Cost/income ratio (%)	41.1	41.6	114.2	122.2			55.2	54.7
RoE before taxes in %[2)3)]	19.6	23.5	-18.3	-30.3			12.6	13.5
Employees (average)	**895**	**1,042**	**1,849**	**1,776**			**2,744**	**2,818**
Segment assets	**33,184**	**40,869**	**10,083**	**9,665**			**43,267**	**50,534**

[1] € 24 million in provisions recognised for staff-related measures, resulting from the optimisation of processes and structures within the scope of the "Aareal 2020" programme for the future, was allocated to the Structured Property Financing segment in full.

[2] On an annualised basis

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

(32) Segment Reporting (Quarterly Development)

€ mn	Structured Property Financing		Consulting/Services		Consolidation/ Reconciliation		Aareal Bank Group	
	Quarter 3 2017	Quarter 3 2016	Quarter 3 2017	Quarter 3 2016	Quarter 3 2017	Quarter 3 2016	Quarter 3 2017	Quarter 3 2016
Net interest income	167	179	0	0	-3	-4	164	175
Allowance for credit losses	26	33					26	33
Net interest income after allowance for credit losses	**141**	**146**	**0**	**0**	**-3**	**-4**	**138**	**142**
Net commission income	1	2	45	39	2	3	48	44
Net result on hedge accounting	1	3					1	3
Net trading income/expenses	10	4					10	4
Results from non-trading assets	0	5					0	5
Results from investments accounted for using the equity method				0				0
Administrative expenses	68	77	53	51	-1	-1	120	127
Net other operating income/expenses	4	2	1	1	0	0	5	3
Operating profit	**89**	**85**	**-7**	**-11**	**0**	**0**	**82**	**74**
Income taxes	34	27	-3	-4			31	23
Consolidated net income	**55**	**58**	**-4**	**-7**	**0**	**0**	**51**	**51**
Consolidated net income attributable to non-controlling interests	0	5	0	0			0	5
Consolidated net income attributable to shareholders of Aareal Bank AG	55	53	-4	-7	0	0	51	46
Allocated equity	1,772	1,587	155	133	592	741	2,519	2,461
Cost/income ratio (%)	37.2	39.7	117.0	126.7			52.8	54.4
RoE before taxes (%) [1)2)]	18.8	18.8	-20.2	-34.0			12.0	10.3

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

(33) 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			Income statement classification – bank									
			Net interest income	Net commission income	Net trading income/expenses	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**
	9m 2017		0	136			157	2		**-19**	-7	**-12**
	9m 2016		0	124	0	0	153	1		**-28**	-10	**-18**
Income statement classification – industrial enterprise												
Sales revenue	9m 2017	162		162								
	9m 2016	148		148								
Own work capitalised	9m 2017	3					3					
	9m 2016	4					4					
Changes in inventory	9m 2017	0						0				
	9m 2016	0						0				
Other operating income	9m 2017	3						3				
	9m 2016	3			0			3				
Cost of materials purchased	9m 2017	26		26								
	9m 2016	24		24								
Staff expenses	9m 2017	109					109					
	9m 2016	107					107					
Depreciation, amortisation and impairment losses	9m 2017	9					9					
	9m 2016	9					9					
Results from investments accounted for using the equity method	9m 2017											
	9m 2016	0				0						
Other operating expenses	9m 2017	43					42	1				
	9m 2016	43					41	2				
Interest and similar income/expenses	9m 2017	0	0									
	9m 2016	0	0									
Operating profit	**9m 2017**	**-19**	**0**	**136**			**157**	**2**				
	9m 2016	**-28**	**0**	**124**	**0**	**0**	**153**	**1**				
Income taxes	9m 2017	-7									-7	
	9m 2016	-10									-10	
Segment result	**9m 2017**	**-12**										
	9m 2016	**-18**										

(34) Consulting/Services segment – Reconciliation of the Income Statement (Quarterly Development)

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)

			Income statement classification – bank									
€ mn			Net interest income	Net commission income	Net trading income/expenses	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**
	Q3/2017		0	45			53	1		**-7**	-3	**-4**
	Q3/2016		0	39		0	51	1		**-11**	-4	**-7**
Income statement classification – industrial enterprise												
Sales revenue	Q3/2017	53		53								
	Q3/2016	47		47								
Own work capitalised	Q3/2017	1					1					
	Q3/2016	1					1					
Changes in inventory	Q3/2017	0						0				
	Q3/2016	0						0				
Other operating income	Q3/2017	1						1				
	Q3/2016	2						2				
Cost of materials purchased	Q3/2017	8		8								
	Q3/2016	8		8								
Staff expenses	Q3/2017	38					38					
	Q3/2016	36					36					
Depreciation, amortisation and impairment losses	Q3/2017	3					3					
	Q3/2016	3					3					
Results from investments accounted for using the equity method	Q3/2017											
	Q3/2016	0				0						
Other operating expenses	Q3/2017	13					13	0				
	Q3/2016	14					13	1				
Interest and similar income/expenses	Q3/2017	0	0									
	Q3/2016	0	0									
Operating profit	**Q3/2017**	**-7**	**0**	**45**			**53**	**1**				
	Q3/2016	**-11**	**0**	**39**		**0**	**51**	**1**				
Income taxes	Q3/2017	-3									-3	
	Q3/2016	-4									-4	
Segment result	**Q3/2017**	**-4**										
	Q3/2016	**-7**										

Other Notes

(35) Contingent liabilities and loan commitments

€ mn	30 Sep 2017	31 Dec 2016
Contingent liabilities	136	114
Loan commitments	1,175	1,333
of which: irrevocable	701	901

(36) Employees

The number of Aareal Bank Group employees[1] at 30 September 2017 is shown below:

	30 Sep 2017	31 Dec 2016
Salaried employees	2,612	2,566
Executives	156	162
Total	**2,768**	**2,728**
of which: Part-time employees	534	503

The average number of Aareal Bank Group employees in 2017[2] is shown below:

	1 Jan-30 Sep 2017	1 Jan-31 Dec 2016
Salaried employees	2,585	2,633
Executives	159	164
Total	**2,744**	**2,797**
of which: Part-time employees	526	514

(37) Related party disclosures in accordance with IAS 24

No material transactions with related parties were entered into during the first nine months of the financial year 2017.

(38) Events after the interim reporting period

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

[1] This number does not include 244 employees of the hotel business (31 December 2016: 56).
[2] This number does not include 214 employees of the hotel business (1 January to 31 December 2016: 175).

Executive Bodies of Aareal Bank AG

Supervisory Board

Marija Korsch [1) 2) 3) 4) 5) 6)]
Chairman of the Supervisory Board
Former partner of Bankhaus Metzler seel.
Sohn & Co. Holding AG

Prof. Dr Stephan Schüller [1) 2) 3)]
Deputy Chairman of the Supervisory Board
Spokesman of the General Partners of
Bankhaus Lampe KG

York-Detlef Bülow [1) 2) 3) 7)]
Deputy Chairman of the Supervisory Board
Aareal Bank AG

Thomas Hawel [6) 7)]
Aareon Deutschland GmbH

Dieter Kirsch [2) 4) 5) 7)]
Aareal Bank AG

Richard Peters [1) 3) 6)]
President and Chairman of the Management Board
of Versorgungsanstalt des Bundes und der Länder

Dr Hans-Werner Rhein [1) 4) 5)]
German Lawyer (Rechtsanwalt)

Sylvia Seignette [4) 5)]
Former CEO for Germany and Austria,
Crédit Agricole CIB (formerly Calyon)

Elisabeth Stheeman [4) 5) 6)]
Senior Advisor, Bank of England, Prudential
Regulation Authority

Hans-Dietrich Voigtländer [2) 3) 6)]
Senior Partner at BDG Innovation +
Transformation GmbH & Co. KG

Prof. Dr Hermann Wagner [3) 4) 5)]
Chairman of the Audit Committee
German Chartered Accountant, Tax Consultant

Beate Wollmann [7)]
Aareon Deutschland GmbH

Management Board

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Chairman of the Management Board

Dagmar Knopek
Member of the Management Board

Christiane Kunisch-Wolff
Member of the Management Board

Thomas Ortmanns
Member of the Management Board

Christof Winkelmann
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) Member of the Technology and Innovation Committee;
7) Employee representative

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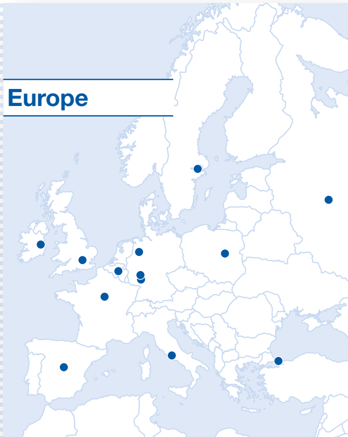
Financial Calendar

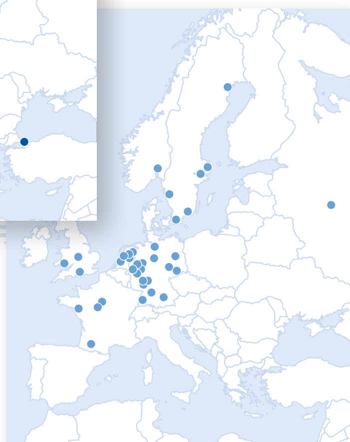
28 February 2018	Presentation of preliminary results for the 2017 financial year
28 March 2018	Publication of annual report as at 31 December 2017
9 May 2018	Publication of results as at 31 March 2018
23 May 2018	Annual General Meeting – Kurhaus, Wiesbaden
14 August 2018	Publication of results as at 30 June 2018
13 November 2018	Publication of results as at 30 September 2018

Locations

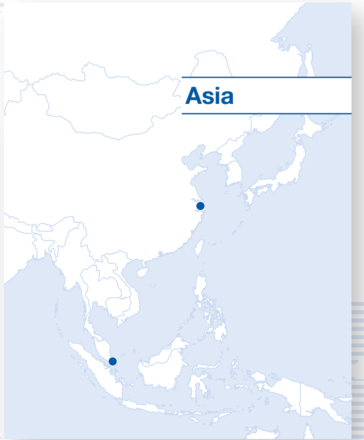
Structured Property Financing



Structured Property Financing



Consulting/Services



Structured Property Financing

Aareal Bank, Real Estate Structured Finance: Brussels, Dublin, Istanbul, London, Madrid, Moscow, New York, Paris, Rome, Shanghai, Singapore, Stockholm, Warsaw, Wiesbaden | **Aareal Estate AG:** Wiesbaden | **Aareal Valuation GmbH:** Wiesbaden | **Westdeutsche Immobilien Servicing AG:** Mainz, Münster

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

as at 30 September 2017

Imprint
Contents:
Aareal Bank AG, Group Corporate Communications
Design / Layout:
S/COMPANY · Die Markenagentur GmbH, Fulda, Germany

Corporate Responsibility Prime rated by oekom research

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