AAREAL BANK GROUP – INTERIM REPORT
1 JANUARY TO 30 JUNE 2021

new perspectives

Aareal

YOUR COMPETITIVE ADVANTAGE.

Key Indicators

	1 Jan-30 Jun 2021	1 Jan-30 Jun 2020
Results		
Operating profit (€ mn)	73	13
Consolidated net income (€ mn)	33	16
Consolidated net income allocated to ordinary shareholders (€ mn)[1]	24	7
Cost/income ratio (%)[2]	45.3	51.7
Earnings per ordinary share (€)[1]	0.40	0.11
RoE before taxes (%)[1)3]	4.9	0.0
RoE after taxes (%)[1)3]	1.9	0.5

	30 Jun 2021	31 Dec 2020
Statement of Financial Position		
Property finance (€ mn)[4]	27,854	27,181
Equity (€ mn)	2,992	2,967
Total assets (€ mn)	46,644	45,478
Regulatory Indicators[5]		
Risk-weighted assets (€ mn)	11,981	12,138
Common Equity Tier 1 ratio (CET1 ratio) (%)	19.2	18.8
Tier 1 ratio (T1 ratio) (%)	21.7	21.3
Total capital ratio (TC ratio) (%)	25.4	28.0
Common Equity Tier 1 ratio (CET1 ratio) (%) – Basel IV (phase-in) –[6]	17.2	17.3
Employees	3,036	2,982

	30 Jun 2021	31 Dec 2020
Moody's		
Issuer rating	A3	A3
Bank deposit rating	A3	A3
Outlook	negative	negative
Mortgage Pfandbrief Rating	Aaa	Aaa
Fitch Ratings		
Issuer default rating	BBB+	BBB+
Senior Preferred	A-	A-
Senior Non Preferred	BBB+	BBB+
Deposit ratings	A-	A-
Outlook	negative	negative
Sustainability Ratings[7]		
MSCI	AA	AA
ISS-ESG	prime (C+)	prime (C+)
CDP	Awareness Level C	Awareness Level C

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; in line with common practice in the banking sector, bank levy and contributions to the deposit guarantee scheme are not included; the previous year's figure was adjusted accordingly.
3) On an annualised basis
4) Excluding € 0.3 billion in private client business (31 December 2020: € 0.3 billion) and € 0.3 billion in local authority lending business by the former Westdeutsche ImmobilienBank AG (WestImmo) (31 December 2020: € 0.3 billion)
5) 31 December 2020: less a proposed dividend payout of € 1.50 per share in 2021 and incorporating the pro-rata accrual of net interest payable on the AT1 bond. The 2021 dividend payment of € 1.50 for 2020 would need to be made in two steps. In compliance with the requirements published by the European Central Bank (ECB) on 15 December 2020, the distributable amount is calculated at € 0.40 per share. A proposal on the allocation of profits was approved at the ordinary Annual General Meeting in May 2021. Following the announcement issued by the ECB on 23 July 2021, and depending on further economic developments, regulatory requirements, the Bank's capital position and its risk situation, in the absence of material adverse developments the Bank plans to convene an extraordinary Annual General Meeting, to be held during the fourth quarter of 2021, to decide on the intended remaining payout of € 1.10 per share, amending the resolution dated 18 May 2021 on the appropriation of profits.
30 June 2021: less the remaining proposed dividend distribution of € 1.10 per share in 2021 and inclusive of the interim dividend for 2021 less any pro rata dividends in accordance with the dividend policy and pro rata accrual of the net interest on the AT1 bond.
The SREP recommendations concerning the NPL inventory and the ECB's NPL guidelines for exposures newly classified as NPLs were taken into account.
6) Underlying RWA estimate, incorporating the higher figure determined using the revised AIRBA or the revised CRSA (phase-in), based on the final Basel Committee framework dated 7 December 2017. The calculation of the material impact upon Aareal Bank is subject to the outstanding EU implementation as well as the implementation of additional regulatory requirements such as the EBA requirements.
7) Please refer to our website (www.aareal-bank.com/en/responsibility/reporting-on-our-progress/) for more details.

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

Contents

Interim Group Management Report

Report on the Economic Position

Macro-economic environment

Developments surrounding the Covid-19 pandemic kept a tight hold on the global economy in the first half of 2021. High new infection levels and another wave of infections led many countries to maintain or reintroduce their measures to prevent infections, especially at the start of the year. Monetary policy and fiscal support measures were extended with the objective of supporting the economy and accelerating the economic recovery. Simultaneously, it was evident that many companies in the manufacturing industry have learned how to deal with the pandemic. For instance, in many countries the economic impact of the extensive containment measures in response to new waves of infection was less severe that in the first wave in the spring of 2020. As case numbers fell thanks to the availability of vaccines, the global economy showed growing signs of a persistent recovery in the course of the first half-year.

Economy

With numerous countries having once again tightened measures to prevent infections at the end of 2020 due to another wave of Covid-19 infections, economic output slowed down at the start of 2021. This especially impacted contact-intensive sectors such as business services, while companies in the manufacturing industry proved considerably more robust. Although the development of various vaccines fostered hopes of a gradual easing of the containment measures and drove up the purchasing managers' sentiment indicators, the provision and inoculation of the vaccines varied from country to country – and progress was very slow in some cases. The progressing vaccination campaigns during the first half of 2021 allowed the measures to prevent infections to be gradually reduced in many countries, leading to a notable increase in economic activity. In most European countries, this development lagged the US and Asian countries that had already achieved positive economic growth in the first quarter of 2021, or the second half of 2020.

In the euro zone, first quarter real gross domestic product fell by 0.3 % quarter-on-quarter. The easing of restrictions led to increased investments and consumption in the second quarter, resulting in a 1.8 % rise in gross domestic product. Although supply problems slowed down activity in certain sectors of the industry, economic development gained momentum overall. Total economic output in the first half of 2021 was up by 5.7 % on the same period of the previous year. Among the largest countries in the euro zone, France recorded the greatest increase in economic output with 8.7 %, followed by Italy with 7.1 % and Spain with 6.7 %. At 3.0 % in the first half of the year, growth in Germany was less pronounced.

The EU governments supported companies and employees in the first half of 2021 with fiscal aid measures that varied in terms of scale and structure. In addition to liquidity and capital aid for companies, income support, debt and contract relief was provided in some countries. Back in 2020, EU member states had already agreed on a € 750 billion plan[1)] to finance economic recovery. The limited recovery fund started raising funds in June 2021 by issuing bonds on the capital market. The funds generated will be provided to EU member states between now and 2026.

The recovery reported in some countries within the European Union that are not members of the euro zone was milder than was seen on average in the euro zone member states. Sweden, for example, achieved economic growth of 4.8 % year-on-year in the first half of 2021, and Poland 4.1 %.

The UK recorded a strong increase in economic output in the first half of the year. At the end of the first six months, gross domestic product was 6.5 % higher than in the same period of the previous year. The positive development was attributable to the decline in new Covid-19 infections since the start of the year – even though figures have increased again recently – and to a rapid vaccination

1) At 2018 prices.

progress by international standards. This supported the lifting of measures taken to prevent infections, that were however extended in the course of the emergence and spread of the Covid-19 Delta variant.

Economic output in the US rose by 6.5 % year-on-year by the middle of the year. This was due in particular to the rapid progress with Covid-19 vaccinations, and earlier withdrawal of the measures taken to prevent infections compared to Europe. Despite the slowdown in the pace of employment growth and occasional capacity squeezes in the industry, economic development increasingly picked up speed in the first half year, supported by fiscal stimulus. The rise in private consumption played an essential part in this development. In Canada, gross domestic product at the end of the first half year was up by 6.7 % on the same period of the previous year.

China already brought the pandemic under control ahead of the rest of the world, which is why it achieved double-digit economic growth in the first half of 2021. Exports, which are important for China, increased again in the course of the global economic recovery. Economic output in Australia in the first half of 2021 was up 5.2 % on the same period of the previous year. The recovery in private consumption and higher investments played an essential part in this development.

The labour markets in many countries continued to be influenced by state aid programmes. Although job numbers increased in the first half of 2021 in the sectors benefiting from the easing of measures taken to prevent infections, employment in many countries remained below pre-crisis levels. The unemployment rate in the euro zone was 8.2 % at the end of the first half of 2021, in line with the 2020 year-end level. At 5.9 % in the US at the end of the first half of 2021, it was down from the figure of 6.8 % at the end of 2020.

Financial and capital markets, monetary policy and inflation

The Covid-19 pandemic remained the dominant topic on the financial markets as well. To support the economy, and so as not to slow down the incipient recovery, the most important central banks continued to pursue a very expansive monetary policy during the first half of 2021. Their targeted goal was not to jeopardise the fragile economic development through higher volatility on the capital markets and higher interest rates.

In the first half of 2021, the European Central Bank (ECB) continued to follow the path of a very accommodating monetary policy embarked upon in 2020, in order to promote favourable financing conditions for the real economy in times of heightened uncertainty and support the economic recovery. The main refinancing rate and deposit rate remained at 0 % and -0.5 % respectively in the two-tier system based on the deposit volume. The ECB also continued to provide the banks with liquidity through targeted long-term refinancing operations (TLTRO 3), to support bank lending to companies and private households. Provided that banks participating in these refinancing operations realise positive net lending to non-financial enterprises and private individuals in the euro zone within a specified reference period, this represents an attractive refinancing option. The net purchases under the Pandemic Emergency Purchase Programme (PEPP) for bonds issued by public and private borrowers, which totalled € 1.85 trillion, will continue to run at least until March 2022 – and in any case until the ECB Council believes the Covid-19 pandemic phase has passed. The ECB will reinvest maturing principal payments from securities purchased under the PEPP at least until the end of 2023. The net purchases under the Asset Purchase Programme (APP) will be continued with a monthly volume of € 20 billion.

The US Federal Reserve (Fed) also continued to adhere to its expansive monetary policy in the first half of 2021. The Fed Funds corridor therefore remained unchanged at 0 %-0.25 %. The Fed introduced another stimulus in the form of its purchase programme for government bonds and mortgage-backed securities, without defining a target volume. This measure was designed to free up liquidity in the banking system, so as to support lending to households and the corporate sector. According to the Fed, the monetary policy course will be maintained until the target of full employment and an inflation rate of more than 2 per cent over the long-term is reached. Some of the economic subsidy programmes started by the Fed in 2020 were discontinued during the first half of the year.

The Bank of England kept its bank rate unchanged at 0.1 % in the first half of 2021 and the target value for the programme for purchasing government and corporate bonds at GBP 895 billion.

Short-term interest rates[1] in the euro area at the end of the first half of 2021 were almost unchanged from the end of 2020. The same applied to the pound sterling, the Swedish krona, the Australian dollar and the Canadian dollar. Short-term interest rates in US dollar declined slightly. Long-term interest rates[2] rose in all of the currency areas that are relevant to Aareal Bank. Government bonds with a ten-year maturity also painted a uniform picture, with prices rising during the first half of 2021.

The euro initially lost significant value vis-a-vis the US dollar during the first half of the year, with the devaluation reaching its peak at the end of March. Following an appreciation phase, the euro lost ground again in June. At the end of the first half year, the exchange rate was USD 1.19 to the euro and therefore below the rate of 31 December 2020 (USD 1.23 to the euro). The euro weakened against the Canadian dollar over the same period, from CAD 1.57 to the euro to CAD 1.47. The euro fell initially against the pound sterling in the first quarter, followed by a relatively stable performance. The exchange rate fell from GBP 0.90 to the euro at the start of the year to GBP 0.86. The euro remained virtually unchanged relative to the Swedish krona, and appreciated from SEK 10.06 to the euro to SEK 10.15. During the same period, the euro remained almost unchanged to the Australian dollar and was trading at AUD 1.58 at the end of the first half of 2021.

Euro zone inflation rose to 1.8 % at the end of the first half of 2021. This was mainly attributable to basis effects due to the curbing of economic activity in the wake of the Covid-19 pandemic in 2020, as well as to the momentum in oil price development. Inflation in the UK rose to 2.0 % at the end of the first half year, while rising to 4.8 % in the US. The more pronounced increase in the US is due to the easing of measures taken to prevent infections, which supported investment volume and private consumption. The increased demand met with capacity bottlenecks in some industries, leading to price surges for goods and services.

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. This includes, in particular, the implementation of the final draft of the Basel III framework into EU law (known as “Basel IV”), which was endorsed by the Basel Committee’s Group of Governors and Heads of Supervision (GHOS). Furthermore, the EU Commission’s revision of supervisory regimes (CRR II, CRD V, BRRD II and SRMR II) at EU level as well as the EBA documents (Guidelines on PD and LGD estimation, treatment of defaulted exposures, and determination of downturn LGD), brought about further regulatory changes. The provisions put forward by the ECB, EBA and the EU Commission on the treatment of non-performing loans must also be taken into account. With regard to Covid-19, the IASB and relevant regulatory authorities such as the EBA, the ECB and ESMA formulated recommendations for implementation in the processes and for risk quantification, which we have taken into consideration accordingly.

Moreover, both national and European regulators are imposing various new requirements – including in connection with IT/information security risks, or regarding the prevention of money laundering/terrorist financing and tax evasion. Furthermore, politics and the banking supervision deem it necessary to establish sustainability more strongly with society, and as a regulatory requirement within

[1] Calculated on the basis of 3-month Euribor, LIBOR or other comparable rates for other currencies
[2] Calculated on the basis of swaps in the respective currencies

the economy. As such, the EU's Technical Expert Group on Sustainable Finance published the "Taxonomy Technical Report", and BaFin issued its "Guidance Notice on Dealing with Sustainability Risks" at the end of 2019. The ECB also published its guide on climate-related and environmental risks, setting out its expectations relating to risk management and disclosure.

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 buffers. In the past year, ECB took a pragmatic SREP approach, which was mainly focused on the assessment of Covid-19-related risks. As a result, the score values and the requirements for additional capital and liquidity buffers remained unchanged except in justified individual cases. As a result, there were no changes for Aareal Bank. Yet this year's SREP – which has not been concluded as yet, and which will once again be based on the original systematic approach – as well as this year's EBA/ECB stress test may lead to adjustments and/or changes to scores or requirements for additional equity and liquidity buffers.

Sector-specific and business developments

Structured Property Financing segment

The commercial property markets were burdened in the first half of 2021 by the continued high levels of uncertainty about the duration of the Covid-19 pandemic and its long-term consequences. In this environment, global transaction volumes increased compared to the corresponding prior-year period. However, there were differences between the regions: whilst volumes in North America and the Asia/Pacific region increased by 20 % and 15 %, respectively, Europe saw a 10 % decline.

There were regional differences between property types as well: In Europe, demand for logistics properties in particular remained strong in the first half of 2021. Transaction volumes here increased over the first half of 2020, whilst volumes remained stable for hotels and declined for office and retail properties. Volumes in North America increased for all property types. In the Asia/Pacific region, transaction volumes declined for office and hotel properties, whereas they increased for retail and logistics properties.

Lenders focused their interest on residential, logistics, foodstore properties, as well as on office properties in preferred locations. Greater demand was seen for hotel financing, which focused on the area of premium hotels. Competition in commercial property financing remained intense overall, which was reflected in falling margins in part since the start of the year. The high level of investor interest in the logistics sector ensured that the margins for office and logistics properties converged and were at the same level in some markets at the end of the first half year. The loan-to-value ratios remained largely stable in the first half year.

Aareal Bank generated new business of € 3.3 billion[1)] in the first half of 2021 (H1 2020: € 2.7 billion). Following a subdued first quarter, the volume of newly-originated loans increased, especially in April and June. This was due to the relaxation of the contact and travel restrictions referred to above, as well as to the general increase in activity on the transaction markets. Newly-originated loans totalled € 2.2 billion during the first half of the year (H1 2020: € 2.1 billion). The first "green" loan was granted in June by way of a hotel financing concluded in Australia.

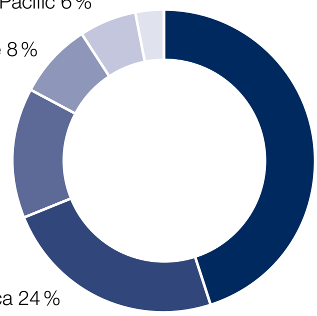
At around 70 %, the highest proportion of the financing volume was in Europe (H1 2020: 57 %), followed by North America at 24 % (H1 2020: 39 %). The Asia/Pacific region accounted for a share of 6 % (H1 2020: 4 %).

[1)] New business, excluding former WestImmo's private client business and local authority lending business.

New business[1] 1 January – 30 June 2021

by region (%)

Total volume: € 3.3 bn



* Including Germany

[1] New business, excluding former WestImmo's private client business and local authority lending business.

In terms of property types, retail properties – which were broadly diversified by sub-category as well as by country – dominated new business with a share of around 33 %, followed by office properties with 22 % and logistics properties with a share of 21 %. Hotel properties accounted for a share of 19 %, while residential properties made up 5 % of the total volume of new business. In terms of newly-originated loans, logistics properties dominated with around 32 %, followed by retail properties with 26 % and office properties with a share of 19 %. Hotel properties accounted for a share of 15 %, while residential properties made up 8 % of the business.

Europe

Transaction volumes in Europe fell by around 10 % year-on-year in the first half of 2021, which shows that uncertainty continued to influence investor behaviour. This impacted many large European countries, with only the UK and Spain bucking this trend. The demand for logistics properties remained pronounced, so that transaction volumes here increased compared to the first half of 2020, while declining in the office and retail segments. Transaction volumes for hotels were stable. The majority of cross-border investors were on the buy side, whilst REIT structures tended to be sellers. Institutional and private investors had balanced positions.

Office properties stagnated with regard to rental development in the prime segment, as well as to the performance of average rents in the first half of 2021. Rents rose noticeably in some sub-markets, such as London or Paris, whereas rental levels across Europe were unchanged on average from year-end 2020. Rental developments for retail properties fell on average, although these varied depending on the retail segment. Rents for high street properties and shopping centres fell but remained stable for supermarkets, as well as for specialist stores and local supply centres, as these were affected to a lesser extent by the infection control measures that were temporarily in place. Rents for logistics properties benefited from the ongoing strong demand in the entire segment and could continue the positive development of the last few years.

Prime yields for office properties changed only marginally during the first half of the year and remained low. While yields for office properties in secondary locations were more volatile, no clear pattern emerged. However, they remained stable on average. Yields[2] for logistics properties fell

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

throughout Europe due to the strong demand and converged further towards office property yields. This impacted on all sub-types in this property segment. Yields declined by up to 60 basis points in the most important markets since the start of the year. The development on the retail property market varied with the property types. Prime yields for high-street properties remained stable on average, while rising by 10 to 20 basis points in places for shopping centres. They even increased by around 65 basis points on average in the UK. Increases in yields were more pronounced in secondary locations. Yields in the supermarket and local supplier segment fell by around 15 basis points on average since the start of the year, with the focus mainly on Western Europe.

For hotel properties, occupancy and revenue per available room have increased since the start of the year, when measures taken to protect against the spread of the infection were eased, even though the level reached at the end of the first half-year was nowhere near the same extent as before the crisis.

The Bank generated new business of € 2.3 billion in the first half of 2021 (H1 2020: € 1.6 billion). The largest share was transacted in Western Europe, followed by Southern and Eastern Europe. Northern Europe's share was comparatively minor.

North America

Transaction volumes in North America were up by around 20 % in the first half of 2021 compared with the corresponding period of the previous year. Following a muted start to the year, both transaction volumes as well as the number of transactions picked up in the course of the first half-year. Cross-border and private investors assumed a balanced position, whilst institutional investors were mostly buyers and REIT structures mostly sellers.

Rents offered for first class and secondary office properties in US metropolitan areas were stable on average in the first half of 2021. Developments did, however, vary from market to market. Rents in San Francisco and New York have fallen since the start of the year, thus continuing the trend of the last quarters, whereas rental levels remained stable in many other metropolitan areas, such as Atlanta or Los Angeles. Shopping mall rents in the US also painted a mixed picture, with rents stagnating in the majority of the markets, such as in Dallas, but increasing, for example, in New York and Chicago. Local suppliers and retailers stocking everyday consumer goods proved once again robust.

Yields on prime and secondary office properties have remained almost unchanged since the start of the year, owing to the availability of liquidity and the readiness to provide financing in the market. Yields on retail properties were also stable for all sub-types, changing only marginally since the start of the year.

Hotel occupancy and revenue in North America have improved significantly since February. Occupancy ratios and revenues per available room in the luxury & upper upscale category in the US have almost doubled since the start of the year, while the growth in Canada was even more pronounced.

In North America, the Bank originated new business of € 0.8 billion (H1 2020: € 1.0 billion), almost all of which was attributable to the US.

Asia/Pacific

Transaction volumes for commercial property in the Asia/Pacific region were roughly 15 % higher in the first half of 2021 than in the same period of the previous year. Volumes declined by 20 % in Australia, whilst an 11 % increase was recorded in China. Cross-border and institutional investors were on the buy side for the most part, while REIT structures and private investors were predominantly sellers.

The development of prime rents for office properties stagnated in the first half of 2021 in the important sub-markets of Australia, as well as in the Chinese metropolitan areas of Beijing and Shanghai. Prime rents for logistics properties remained stable in Australia. In China and Australia, rents for retail properties remained unchanged from the start of the year, with only Perth and Melbourne reporting rent declines.

Yields for prime office and retail properties were stable overall compared to year-end 2020. Yields for logistics properties in Australia fell by between 25 and 60 basis points.

Hotels in the Asia/Pacific region recovered significantly in part in the first half year, thanks to strong domestic demand for travel and comprehensive support measures provided by the government to the tourism sector. Individual markets, such as Sydney and Melbourne, lagged behind, as travel and overnight stays in Australia were halted by renewed lockdown measures and contact restrictions. Markets that depend heavily on international demand for travel generally recovered at a slower pace.

The Bank originated new business of € 0.2 billion in the Asia/Pacific region in the first half of 2021 (H1 2020: € 0.1 billion).

Banking & Digital Solutions segment

The residential and commercial property sectors are proving to be stable market segments, even in light of the Covid-19 pandemic. Despite individual rent deferrals, no significant decline in rental income has been witnessed on the housing market so far. Rental arrears of, for example, companies organised in the Federal Association of German Housing and Real Estate Companies (GdW) rose by only 3 % during 2020. In general, steady rental income generated from a high occupancy status continues to guarantee a secure foundation. New-build rents once again rose by 4.1 % at the beginning of the year, compared with the beginning of 2020.

The influx of the under-30s towards the conurbations was offset by a counter-movement by the over-30s, who are gravitating increasingly to rural areas. The pandemic measures have even driven this trend, as the high cost of housing in the cities was temporarily no longer outweighed by cultural offerings. This not only benefits the surrounding area. Even the more remote areas recorded growth.

The national trend for building permits is positive; just short of 30,000 building permits were granted from January to April 2021, and therefore 13.8 % more than in the corresponding prior-year period. Overall, however, completions lagged significantly behind approval status. Nearly 800,000 new-build housing projects were deemed as approved in 2020 but not implemented.

We once again strengthened our range of property industry services in the current year and, together with our Aareal First Financial Solutions subsidiary, extended the range of digital solutions for the housing industry and its clients.

With the Aareal Exchange & Payment Platform (AEPP), we offer a solution that enables companies to integrate alternative payment methods in the automatic administrative processes. AEPP also opens up the opportunity to implement new customer services and to invoice efficiently. PayPal and credit cards were integrated as additional payment methods during the period under review.

With Aareal Meter, we have developed a product together with pixolus GmbH that, based on mobile scanning of energy meters, automates and speeds up clients' meter reading processes and hence the reporting date-based service charge invoicing.

Aareal Connected Payments acts as a new invoicing solution to support e-mobility: here, Aareal Bank cooperates with smartlab, a platform provider operating a network of charging points.

In collaboration with plusForta, the Group's own specialist for tenant deposit guarantees, we have extended our total offering in rental security deposits to include Aareal Aval, as an integrated alternative for tenant deposit guarantees in our clients' ERP systems.

The digital solutions also include the participation in the objego GmbH start-up, a joint venture with ista Deutschland GmbH, offering software to private landlords with up to 250 units, allowing them to manage their rented apartments in an efficient and straightforward manner.

At present, around 4,000 corporate clients throughout Germany are using our process-optimising products and banking services. The segment's volume of deposits averaged at € 11.9 billion in the first half of 2021 (H1 2020: € 10.7 billion) and thus exceeded our expectations slightly. All in all, this reflects the strong trust our clients continue to place in Aareal Bank. Additionally, despite accounting for expected effects from recent court rulings on general terms and conditions clauses, we were able to increase net commission income in the Banking & Digital Solutions segment as planned to € 13 million (H1 2020: € 12 million).

Aareon segment

Aareon is a provider of ERP software and digital solutions for the European property sector and its partners in Europe. It pursues an international growth strategy based on expanding the operating business, the Value Creation Programme that was developed last year and the inorganic growth through mergers & acquisitions. Key factors to its success are clear client focus, expanding and further developing the digital solutions, further strengthening of the ERP systems through new product generations and exploring new relevant markets and related sectors associated with the property industry. In the course of Aareon's forward-looking orientation and further intensification of research and development, the focus will be on digital solutions.

The Covid-19 pandemic defined the first half of 2021, too. Aareon continued to support its clients, as it has done since the pandemic started in 2020 – with special product and service offerings, as well as numerous webinars, enabling them to continue their business operations in digital form. Client events were held online. The digital industry event Aareon Live in Germany was held in June, with more than 1,000 participants.

In the first half of 2021, Aareon increased its sales revenue to € 133 million (H1 2020: € 126 million) and its adjusted EBITDA[1)] to € 29 million (H1 2020: € 26 million), whereby the first quarter of 2020 had hardly been affected by the Covid-19 pandemic. Aareon expanded its software-as-a-service (SaaS) business. The acquisitions of Arthur Online, Twing and Fixflo (Tactile) also played a role here, so that the share of recurring revenues continued to rise (to 68% in the past twelve months, previous quarter: 67%). As planned in the Value Creation Programme, a marketing campaign was launched in Germany in June to increase this share further. Revenue from digital solutions rose by 11% compared with the first half of 2020 (or to 17% excluding consulting). The consulting business remained low due to Covid-19 and could not be offset entirely by the digital green consulting.

Sales revenue from the ERP business in the DACH region was unchanged from the first half of 2020. The sales revenues generated with Wodis Sigma and the new Wodis Yuneo product generation were increased. In addition, sales revenues with Aareon Cloud Services and the BauSecura insurance business were higher. Sales revenue from SAP® ERP and Blue Eagle software solutions, as well as with RELion, were down slightly compared with the first half of 2020. This was due to the lower consulting revenue.

Sales revenue from the international ERP business exceeded that of the first half of 2020, due above all to Aareon France and Aareon Nederland. In the Netherlands, the transformation of the business model to an SaaS operation continued. Sales revenues generated with the Dutch REMS ERP solution for the commercial property business increased year-on-year. The new release of Prem'Habitat, which was launched in 2020 in France, was in demand. International consulting revenues were also down from the first half of 2020 due to the Covid-19 pandemic, despite the growing demand for green consulting.

Digitalisation is becoming increasingly important for the property industry. The Covid-19 pandemic also accelerates the process, which will have an impact in the medium term in particular. A growing

[1)] "Earnings before interest, taxes, depreciation and amortisation" before new products, Value Creation Programme (VCP), ventures, M&A activities and non-recurring effects.

number of clients are enhancing their ERP systems with the addition of integrated digital solutions, thus developing their own digital ecosystem, so that business volumes with digital solutions continued to rise in the first half of 2021.

Demand was strong in the first half of the year in the DACH region and in the international business for the WRM (Workforce Relationship Management) and CRM (Customer Relationship Management) solutions. With the marketing launch of the Digital Agency, Aareon offers its clients in Germany a platform that reflects the entire tenant life cycle from start to finish. The marketing of the AI-based virtual assistant Neela (CRM solution), which already started in 2020, continued in the first half of 2021. In a first stage, Neela was introduced as a chatbot. In BRM (Building Relationship Management), Aareon started the marketing of PrediMa – a solution for digitalised preventive maintenance – in Germany in April.

With a view to potential inorganic growth, Aareon's management already conducted comprehensive research in 2020 on potential acquisition targets and identified opportunities. In December 2020, Aareon announced the acquisition of 100% of the shares in Arthur Online Ltd., London (Arthur). Arthur offers a cloud-based software solution for property management, which brings together property managers, property owners, tenants and contractors on a single platform. The company was acquired with effect from 29 January 2021. Further acquisitions followed in May: With the 100% acquisition of Twinq B.V., Oosterhout, a provider of software for managing property in the Netherlands, Aareon is developing the market segment for residential property management. With the total acquisition of the UK company Tactile Ltd. (Fixflo), London, Aareon has extended its product range in the UK to include software for property servicing and maintenance. In addition, at the beginning of July, Aareon announced the acquisition of RentPro Ltd. and Curo Software Ltd., two companies based in Warrenpoint, operating under the name Tilt Property Software (Tilt). Tilt offers software for small and medium-sized property managers in the UK. These latest acquisitions have further extended Aareon's market position in the respective countries.

Financial Position and Financial Performance

Financial performance

Group

Consolidated operating profit in the first half of 2021 came to € 73 million and was thus significantly above the previous year (€ 13 million) and in line with expectations – despite a non-recurring tax effect. Consolidated net income amounted to € 33 million (H1 2020: € 16 million). Results were burdened by the consideration of new findings on the tax treatment of a legacy fund investment which was sold in 2012. As a result, the expected tax rate for the current year has increased to approximately 55%, and € 11 million in interest on tax back payments needed to be recognised in net other operating income/expenses.

At € 280 million, net interest income was significantly higher than in the previous year (€ 245 million), as expected. This was largely due to the higher loan portfolio over the previous year and the interest benefit of € 12 million received as part of the ECB's Targeted Longer-Term Refinancing Operations (TLTRO 3).

As expected, loss allowance of € 40 million was significantly below the previous year's figure (€ 106 million), which was particularly influenced by Covid-19. Stage 3 loss allowance mainly increased due to three new loan defaults. Moreover, we used a reversal of loss allowance for a defaulted loan to conclude the accelerated de-risking in Italy; on aggregate, this required additional loss allowance of € 13 million.

Net commission income increased as planned to € 118 million (H1 2020: € 111 million), both in the Banking & Digital Solutions segment and at Aareon.

Consolidated net income of Aareal Bank Group

€ mn	1 Jan-30 Jun 2021	1 Jan-30 Jun 2020
Net interest income	280	245
Loss allowance	40	106
Net commission income	118	111
Net derecognition gain or loss	8	16
Net gain or loss from financial instruments (fvpl)	-4	-7
Net gain or loss from hedge accounting	-2	2
Net gain or loss from investments accounted for using the equity method	-1	0
Administrative expenses	268	238
Net other operating income/expenses	-18	-10
Operating profit	**73**	**13**
Income taxes	40	-3
Consolidated net income	**33**	**16**
Consolidated net income attributable to non-controlling interests	2	1
Consolidated net income attributable to shareholders of Aareal Bank AG	31	15

The net derecognition gain of € 8 million (H1 2020: € 16 million) resulted from market-driven effects of early loan repayments, which also more than compensated for de-risking measures of € 3 million in the securities portfolio. The previous year's figure included non-recurring income from repurchases in the Treasury business within the scope of market support.

The net loss from financial instruments (fvpl) and from hedge accounting in the aggregate amount of € -6 million (H1 2020: € -5 million) was largely due to credit-risk-induced valuation losses on defaulted property loans which are reflected in net gain or loss from financial instruments (fvpl).

Administrative expenses rose to € 268 million (H1 2020: € 238 million). As expected, this is due on the one hand to business expansion and investments into new products, Aareon's Value Creation Programme (VCP), ventures and M&A activities as well as to lower cost savings made during the Covid-19 pandemic, compared to the previous year. On the other hand, compared with the previous year and in relation to the planning, higher provisions were recognised overall for the annual bank levy and contributions to the deposit guarantee scheme, due to a deposit protection event (Greensill) and other effects.

Net other operating income/expenses of € -18 million (H1 2020: € -10 million) was burdened by € 11 million in interest on tax back payments, as well as lower results from properties held by the Bank, as a result of Covid-19. The previous year's result included a Covid-19-related impairment of a property held by the Bank.

Overall, this resulted in consolidated operating profit of € 73 million (H1 2020: € 13 million). Taking into consideration tax expenses of € 40 million and non-controlling interest income of € 2 million, consolidated net income attributable to shareholders of Aareal Bank AG amounted to € 31 million (H1 2020: € 15 million). Given said non-recurring tax effect, income taxes rose above the tax rate expected for the current year. The capitalisation of deferred taxes had a positive impact on the previous year's income tax expenses. Earnings per ordinary share amounted to € 0.40 (H1 2020: € 0.11), and RoE after taxes to 1.9 % (H1 2020: 0.5 %).

Structured Property Financing segment

Operating profit in the Structured Property Financing segment amounted to € 72 million in the first half of 2021 (H1 2020: € 6 million).

At € 260 million, net interest income was significantly higher than in the previous year (€ 226 million), as expected. This was largely due to the higher loan portfolio over the previous year and the interest benefit of € 12 million received as part of the ECB's Targeted Longer-Term Refinancing Operations (TLTRO 3).

As expected, loss allowance of € 40 million was significantly below the previous year's figure (€ 106 million), which was particularly influenced by Covid-19. Stage 3 loss allowance mainly increased due to three new loan defaults. Moreover, we used a reversal of loss allowance for a defaulted loan to conclude the accelerated de-risking in Italy; on aggregate, this required additional loss allowance of € 13 million.

The net derecognition gain of € 8 million (H1 2020: € 16 million) resulted from market-driven effects of early loan repayments, which also more than offset de-risking measures of € 3 million in the securities portfolio. The previous year's figure included non-recurring income from repurchases in the Treasury business within the scope of market support.

The net loss from financial instruments (fvpl) and from hedge accounting in the aggregate amount of € -6 million (H1 2020: € -5 million) was largely due to credit-risk-induced valuation losses on defaulted property loans which are reflected in net gain or loss from financial instruments (fvpl).

Administrative expenses rose to € 134 million (H1 2020: € 117 million). As expected, this is due on the one hand to lower cost savings compared to the previous year's cost savings made during the Covid-19 pandemic. On the other hand, compared with the previous year and in relation to the planning, higher provisions were recognised overall for the annual bank levy and contributions to the deposit guarantee scheme, due to a deposit protection event (Greensill) and other effects.

Net other operating income/expenses of € -20 million (H1 2020: € -11 million) was burdened by € 11 million in interest on tax back payments, as well as lower results from properties held by the Bank, as a result of Covid-19. The previous year's result included a Covid-19-related write-down of a property held by the Bank.

Structured Property Financing segment result

€ mn	1 Jan-30 Jun 2021	1 Jan-30 Jun 2020
Net interest income	260	226
Loss allowance	40	106
Net commission income	4	3
Net derecognition gain or loss	8	16
Net gain or loss from financial instruments (fvpl)	-4	-7
Net gain or loss from hedge accounting	-2	2
Administrative expenses	134	117
Net other operating income/expenses	-20	-11
Operating profit	**72**	**6**
Income taxes	40	-5
Segment result	**32**	**11**

Overall, operating profit for the Structured Property Financing segment was € 72 million (H1 2020: € 6 million). Taking into consideration income taxes of € 40 million (H1 2020: € -5 million), the segment result amounted to € 32 million (H1 2020: € 11 million). Given said non-recurring tax effect, income taxes rose above the tax rate expected for the current year. The capitalisation of deferred taxes had a positive impact on the previous year's income tax expenses.

Banking & Digital Solutions segment

Net interest income in the Banking & Digital Solutions segment amounted to € 22 million (H1 2020: € 20 million). Net interest income continues to be burdened by the negative margin from the deposit-taking business due to the persistently low level of interest rates.

Despite accounting for expected effects from recent court rulings on general terms and conditions clauses, net commission income was increased, as planned, to € 13 million (H1 2020: € 12 million).

Compared with the previous year and in relation to the planning, administrative expenses increased slightly to € 36 million (H1 2020: € 35 million) as a result of higher overall provisions recognised for the annual bank levy and contributions to the deposit guarantee scheme due to a deposit protection event (Greensill) and other effects.

Overall, segment operating profit for the first half of 2021 was € -2 million (H1 2020: € -3 million). Taking income taxes into consideration, the segment result for the first half of the year amounted to € -1 million (H1 2020: € -2 million).

Aareon segment

Net commission income increased as planned to € 107 million (H1 2020: € 102 million) despite the Covid-19 pandemic.

Administrative expenses increased as expected to € 104 million (H1 2020: € 92 million) due to business expansion and investments into new products, Aareon's Value Creation Programme (VCP), ventures and M&A activities.

Overall, segment operating profit for the first half of 2021 was € 3 million (H1 2020: € 10 million). Taking income taxes into consideration, the segment result for the first half of the year amounted to € 2 million (H1 2020: € 7 million).

Banking & Digital Solutions segment result

€ mn	1 Jan-30 Jun 2021	1 Jan-30 Jun 2020
Net interest income	22	20
Net commission income	13	12
Net gain or loss from financial instruments (fvpl)	–	0
Administrative expenses	36	35
Net other operating income/expenses	0	0
Operating profit	**-2**	**-3**
Income taxes	-1	-1
Segment result	**-1**	**-2**

Aareon segment result

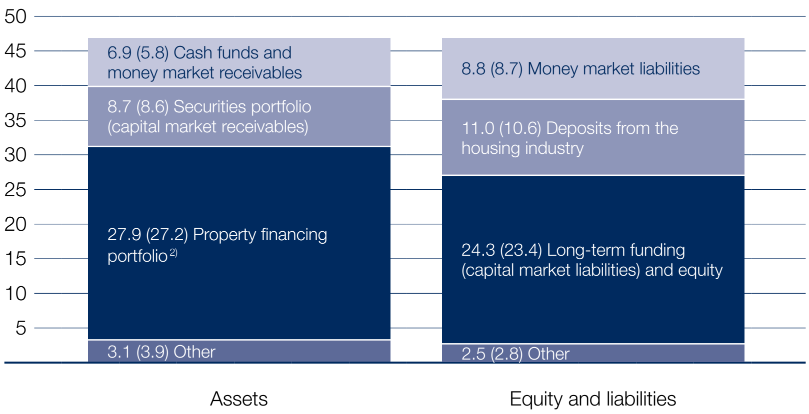
€ mn	1 Jan-30 Jun 2021	1 Jan-30 Jun 2020
Net interest income	-2	-1
Loss allowance	0	0
Net commission income	107	102
Net gain or loss from financial instruments (fvpl)	–	0
Net gain or loss from investments accounted for using the equity method	0	0
Administrative expenses	104	92
Net other operating income/expenses	2	1
Operating profit	**3**	**10**
Income taxes	1	3
Segment result	**2**	**7**

Financial position

Consolidated total assets of Aareal Bank Group increased to € 46.6 billion as at 30 June 2021 (31 December 2020: € 45.5 billion), reflecting the use of further targeted longer-term refinancing operations (TLTROs): this led to increases in cash funds and money-market liabilities.

Balance sheet structure as at 30 June 2021 (31 December 2020)

€ bn



[2] Excluding € 0.3 billion in private client business (31 December 2020: € 0.3 billion) and € 0.3 billion in local authority lending business by the former Westdeutsche ImmobilienBank AG (WestImmo) (31 December 2020: € 0.3 billion), and excluding loss allowance

Property financing portfolio

The volume of Aareal Bank Group's property financing portfolio[1] stood at € 27.9 billion as at 30 June 2021, up as planned from the year-end level 2020 (€ 27.2 billion).

At the reporting date (30 June 2021), Aareal Bank Group's property financing portfolio was composed as shown in the following charts, compared to year-end 2020.

Portfolio allocation by region and continent did not change significantly during the period under review. Whilst the portfolio share of exposures in Western Europe rose by around 1.4 percentage points, it declined in North America by around 1.2 percentage points, remaining relatively stable for all other regions.

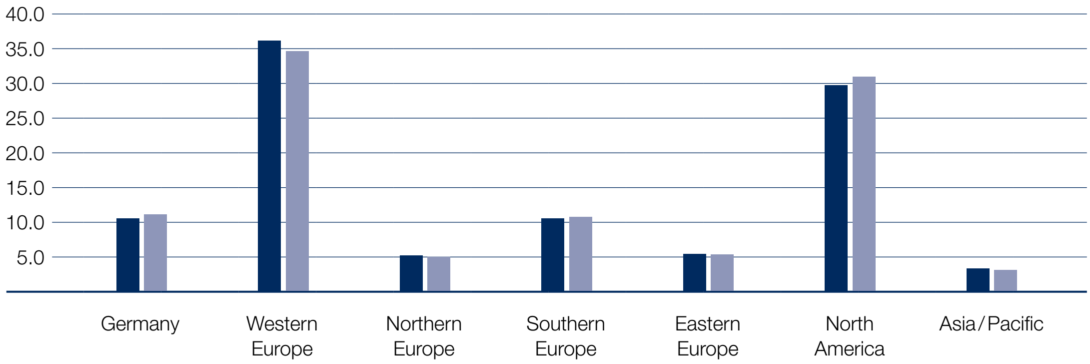
The breakdown of the portfolio by property type did not change significantly during the reporting period. The share of hotel property increased by approximately 1.1 percentage points compared to year-end 2020, whilst the share of office property fell by around 2 percentage points. The share of retail and logistics properties as well as other

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

Property financing volume[1)] (amounts drawn)

by region (%)

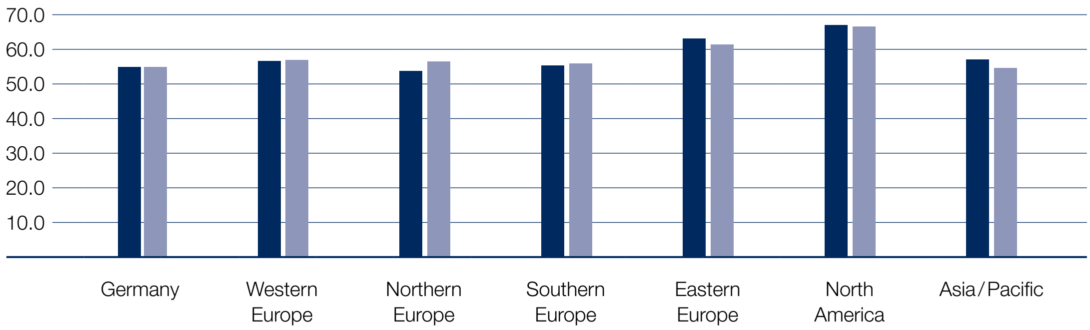
■ 30 Jun 2021 (100 % = € 27.9 bn) ■ 31 Dec 2020 (100 % = € 27.2 bn)



Average LTV of property financing[1)]

by region (%)

■ 30 Jun 2021 ■ 31 Dec 2020

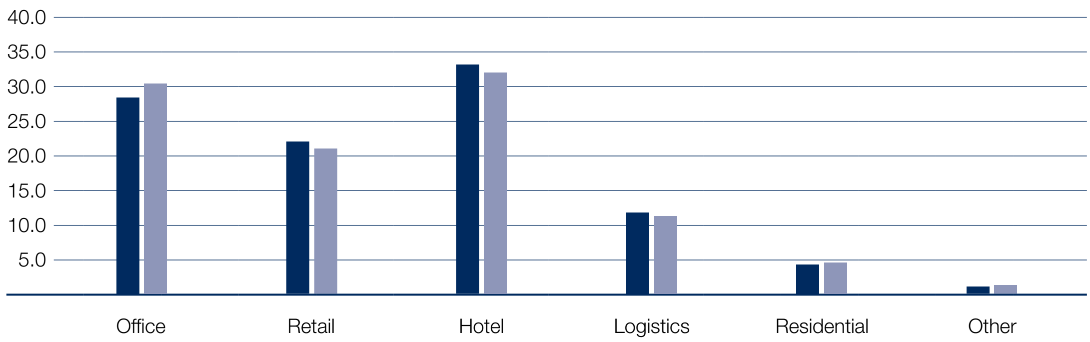


Note: the loan-to-value ratios are calculated on the basis of drawdowns and market values, including supplementary collateral with sustainable value, excluding defaulted property financings.

Property financing volume[1)] (amounts drawn)

by type of property (%)

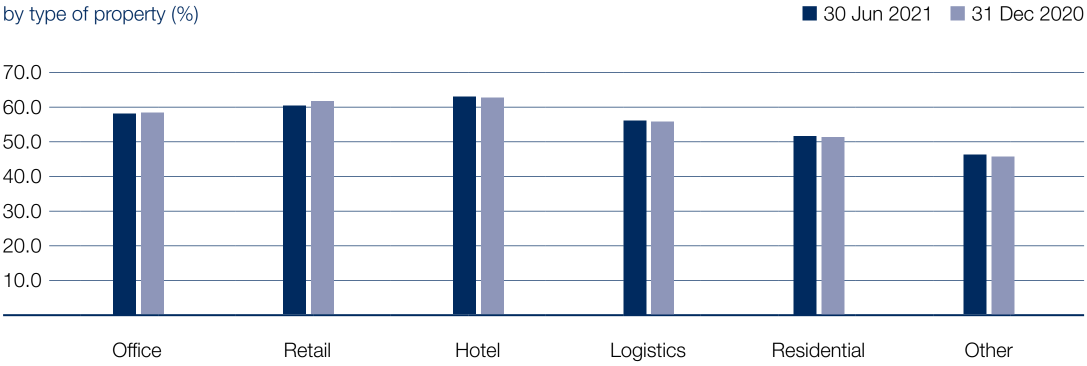
■ 30 Jun 2021 (100 % = € 27.9 bn) ■ 31 Dec 2020 (100 % = € 27.2 bn)



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

Average LTV of property financing[1)]

by type of property (%)



Note: the loan-to-value ratios are calculated on the basis of drawdowns and market values, including supplementary collateral with sustainable value, excluding defaulted property financings.

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

financings in the overall portfolio remained almost unchanged compared to the year-end 2020.

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.

Treasury portfolio

Aareal Bank holds a high-quality treasury portfolio.

Key aspects taken into account for portfolio management are good credit quality and the related value stability, as well as a high degree of liquidity, depending on the intended use.

As at 30 June 2021, the total nominal volume of the Treasury portfolio[2)] was € 7.6 billion (31 December 2020: € 7.3 billion).

The portfolio comprises the asset classes public-sector borrowers, covered bonds and bank bonds (financials), with the public-sector asset class accounting for the biggest portion of the portfolio (currently approximately 96 %).

The high creditworthiness requirements are also reflected in the rating breakdown in the portfolio. 99.9 % of the portfolio has an investment grade rating[3)], and 86 % of the positions have an AAA to AA- rating.

The portfolio currently comprises almost exclusively (98 %) securities denominated in euros and its average remaining term on the reporting date was 6.2 years.

Financial position

Funding and equity

Funding

Aareal Bank Group has remained very solidly funded throughout the first half of the 2021 financial year: total long-term refinancing as at 30 June 2021 amounted to € 19.1 billion in nominal terms (31 December 2020: € 19.1 billion), comprising Pfandbrief issues as well as senior unsecured and subordinated issues.

As at the reporting date, Aareal Bank also had € 11.0 billion at its disposal in deposits generated from the business with the housing industry (31 December 2020: € 10.6 billion). Money market liabilities, including targeted longer-term refinancing operations (TLTROs) of Deutsche Bundesbank, amounted to € 8.8 billion (31 December 2020: € 8.7 billion).

2) As at 30 June 2021, the securities portfolio was carried at € 8.7 billion (31 December 2020: € 8.6 billion).

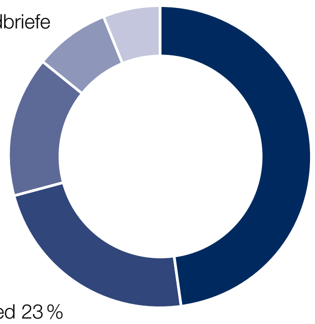
3) The rating details are based on the composite ratings.

Aareal Bank Group raised € 2.2 billion on the capital market during the first half of 2021. This included three Pfandbrief benchmark transactions: one for € 500 million, another for USD 750 million as well as a SONIA-linked one for GBP 500 million. Senior unsecured funding totalling € 0.4 billion was raised, almost exclusively in senior preferred bonds. In addition, TLTRO 3 borrowing was increased by € 1.0 billion to € 5.3 billion.

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.

Capital market funding mix as at 30 June 2021

% Total volume (nominal): € 19.1 bn



Equity

Aareal Bank Group's total equity as disclosed in the statement of financial position amounted to € 2,992 million as at 30 June 2021 (31. December 2020: € 2,967 million), comprising € 300 million for the Additional Tier 1 (AT 1) bond.

Please also refer to the Statement of Changes in Equity, and to our explanations in Note 22 of the consolidated interim financial statements for the first half of 2021.

Regulatory indicators[1)]

	30 Jun 2021[2)]	31 Dec 2020[3)]
€ mn		
Common Equity Tier 1 (CET 1)	2,298	2,286
Tier 1 (T1)	2,598	2,586
Total capital (TC)	3,048	3,395
%		
Common Equity Tier 1 ratio (CET 1 ratio)	19.2	18.8
Tier 1 ratio (T1 ratio)	21.7	21.3
Total capital ratio (TC ratio)	25.4	28.0
Common Equity Tier 1 ratio (CET 1 ratio) – Basel IV (phase-in) –[4)]	17.2	17.3

1) Aareal Bank AG utilises the rules set out in section 2a of the KWG in conjunction with Article 7 of the CRR, pursuant to which regulatory indicators of own funds may only be determined at Group level. In this respect, the following disclosures relate to Aareal Bank Group.

2) 30 June 2021: less the remaining proposed dividend distribution of € 1.10 per share in 2021 and inclusive of the interim profits for 2021 less any pro rata dividends in accordance with the dividend policy and pro rata accrual of the net interest payable on the AT1 bond. The SREP recommendations concerning the NPL inventory and the ECB's NPL guidelines for exposures newly classified as NPLs were taken into account.

3) 31 December 2020: less a proposed dividend payout of € 1.50 per share in 2021 and incorporating the pro rata accrual of net interest payable on the AT1 bond. The 2021 dividend payment of € 1.50 for 2020 would need to be made in two steps. In compliance with the requirements published by the European Central Bank (ECB) on 15 December 2020, the distributable amount is calculated at € 0.40 per share. A proposal on the allocation of profits was approved at the ordinary Annual General Meeting in May 2021. Following the announcement issued by the ECB on 23 July 2021, and depending on further economic developments, regulatory requirements, the Bank's capital position and its risk situation, in the absence of material adverse developments the Bank plans to convene an extraordinary Annual General Meeting, to be held during the fourth quarter of 2021, to decide on the intended remaining payout of € 1.10 per share, amending the resolution dated 18 May 2021 on the appropriation of profits.

4) Underlying RWA estimate, incorporating the higher figure determined using the revised AIRBA or the revised CRSA (phase-in), based on the final Basel Committee framework dated 7 December 2017. The calculation of the material impact upon Aareal Bank is subject to the outstanding EU implementation as well as the implementation of additional regulatory requirements such as the EBA requirements.

Analysis of risk-weighted assets (RWA)[1)]

€ mn	RWA amounts 30 Jun 2021	Total Capital requirements 30 Jun 2021	RWA amounts 31 Dec 2020	Total Capital requirements 31 Dec 2020
Credit risk (excluding Counterparty credit risk)	10,325	826	10,298	824
Counterparty credit risk	442	35	517	41
Market risk	83	7	87	7
Operational risk	1,131	90	1,236	99
Total	**11,981**	**958**	**12,138**	**971**

[1)] Calculations were performed in accordance with CRR II as at 30 June 2021 for the first time; results are presented in line with the new disclosure requirements. The previous year's figures were reclassified accordingly.

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).

Risk Report

Aareal Bank Group Risk Management

The Group Management Report 2020 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 the present Interim Report, we briefly reiterate the key elements of our risk management, also outlining material 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. Appropriate risk management and risk control processes are deployed to implement the risk strategies, and to ascertain the Bank's ability to bear risk. A monthly internal risk report is prepared for all material types of risk, and submitted to the Bank's Management Board and Supervisory Board.

Aareal Bank regularly reviews the appropriateness and effectiveness of its corporate governance systems (including risk governance systems). The regular review of the Risk Appetite Framework and the credit risk strategies carried out during the first quarter of 2021 did not indicate any material adjustments.

Aareal Bank also includes sustainability risks – so-called ESG risks (environmental, social and governance) – in its risk management. Fundamentally, Aareal Bank considers sustainability risks to include cross-species risks and risk drivers that are influenced directly or indirectly by environmental or social issues, or by monitoring processes. All material sustainability risks were able to be classified as a form of existing financial and non-financial risks. In line with this, they are managed implicitly as part of the risk types under which they are classified.

Risk-bearing capacity and risk limits

The Bank's ability to carry and sustain risk (as determined within the framework of the Internal Capital Adequacy Assessment Process (ICAAP)) is a core determining factor governing the structure of its risk management system. To ensure its uninterrupted risk-bearing capacity, Aareal Bank Group has adopted a dual management approach comprising two complementary perspectives: the normative and the economic perspective.

The normative perspective aims to ensure Aareal Bank Group's ability to fulfil all of its regulatory requirements over a multi-year period. This perspective thus accounts for all material risks which may impact upon relevant regulatory indicators over the multi-year planning period.

The normative ICAAP perspective is embedded into Aareal Bank Group's planning process, which – in particular – also includes capital planning. Group planning covers three planning years, it comprises both baseline and adverse scenarios. Results of Group planning are shown as a projected consolidated income statement for Aareal Bank Group. Planning also encompasses the balance sheet structure, as well as key regulatory indicators, plus additional internal management indicators.

Besides the planning process itself, intra-year computation adjustments to Aareal Bank Group's planning process also included the ongoing monitoring of management indicators as well as checking whether limits in the normative perspective were being complied with. Management indicators in the normative perspective (which are being monitored, and for which limits have been set) comprise various regulatory ratios.

We are using the ICAAP economic perspective, whose purpose is to safeguard Aareal Bank Group's economic substance and thus, in particular, to protect creditors against economic losses. We predominantly employ proprietary procedures and methods (agreed upon with regulators) in order to identify and quantify potential economic losses, and to determine the required capital backing.

Risk-bearing capacity of Aareal Bank Group (ICAAP – economic perspective)

€ mn	30 Jun 2021	31 Dec 2020
Tier 1 (T1) capital	2,598	2,586
Economic adjustments	-8	-61
Aggregate risk cover	**2,590**	**2,525**
Utilisation of aggregate risk cover		
Loan loss risks	682	637
Interest rate risk in the banking book (IRRBB)	67	68
Market risks	381	415
Operational risks	93	102
Investment risks	58	35
Property risks	76	76
Business and strategic risks	31	36
Total utilisation	**1,388**	**1,369**
Utilisation (% of aggregate risk cover)	**54 %**	**54 %**

The purpose of internal capital is to serve as a risk-bearing component under the economic perspective. Within Aareal Bank Group, the current regulatory Tier I capital serves as the basis for determining economic aggregate risk cover. Accordingly, available internal capital comprises Common Equity Tier I (CET1) capital, supplemented by Additional Tier I (AT1) capital. Tier 2 capital, as well as projected results to be incurred during the risk analysis horizon, are not taken into account.

Moreover, the value-oriented approach adopted under the economic perspective requires suitable adjustments to be made to regulatory Tier I capital, in order to bring aggregate risk cover into line with the economic assessment. Specifically, this may entail adjustments regarding conservative valuation, hidden encumbrances, or a management buffer.

Aareal Bank Group consistently applies a period of 250 trading days as a risk analysis horizon, as well as for the holding period as part of risk models under the economic perspective. To the extent that risks are measured on the basis of quantitative risk models, a uniform observation period of at least 250 trading days (or at least one year) is applied to the risk parameters used. The appropriateness of model assumptions is verified within the scope of independent validation of the corresponding risk models and parameters.

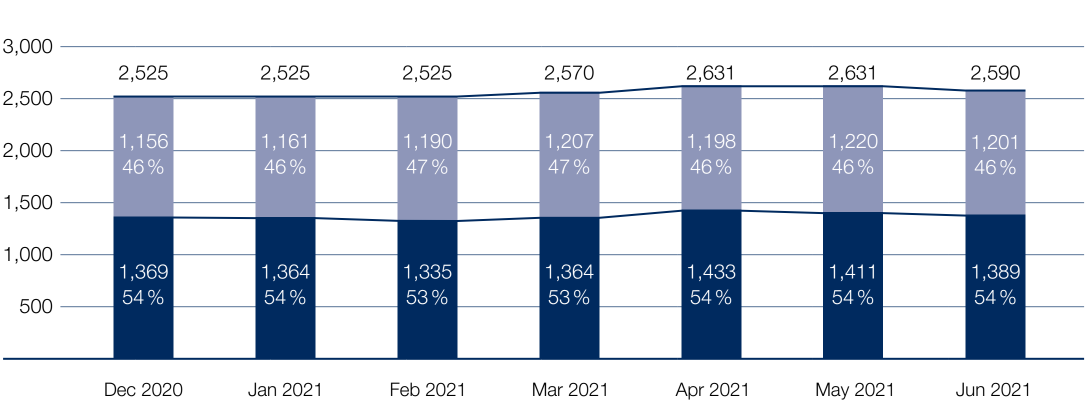
Looking at correlation effects between material types of risk within the framework of the economic ICAAP perspective, Aareal Bank Group has prudently opted for aggregation of risk levels; accordingly, no risk-mitigating correlation effects are being taken into account. Where we measure risks on the basis of quantitative risk models for the purposes of calculating risk-bearing capacity, these are based on a confidence interval of 99.9 %.

Limits for specific risk types are determined in such a manner that aggregate limits do not exceed economic aggregate risk cover, less a risk buffer designed to cover risks not explicitly covered by limits, and to also absorb other fluctuations of internal capital over time. Individual limits are set on the basis of existing risk exposures and historical levels of potential risks, and to an extent that is in line with the Bank's business and risk strategy. Specific limits have been set in a way that each limit is sufficient for utilisation in line with planned business development, as well as for common market fluctuations.

A detailed monthly report provides information regarding the utilisation of individual limits for the material types of risk, as well as on the overall limit utilisation. These are being monitored as part of daily reporting. No limit breaches were detected during the period under review.

Utilisation of aggregate risk cover

during the course of 2021, € mn



Utilisation of aggregate risk cover developed as follows during the period under review.

Since risk cover potential is an inadequate measure to assess the risk-bearing capacity in terms of monitoring the Bank's ability to meet its payment obligations (liquidity risk in the narrower sense), we have defined special tools within the framework of the Internal Liquidity Adequacy Assessment Process (ILAAP) for managing and monitoring this type of risk.

Loan loss risks

Definition

Aareal Bank defines loan loss risk as the risk of losses being incurred due to (i) a deterioration in a business partner's credit quality (migration risk); (ii) a business partner defaulting on contractual obligations; (iii) collateral being impaired; or (iv) 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

Regulatory requirements are 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 different risk classification procedures tailored to the requirements of the respective type of business for the initial, regular, or event-driven assessment of counterparty credit risk. Forward-looking as well as macro-economic information is taken into consideration for risk classification procedures, and in the valuation of collateral. The respective procedures and parameters are subject to permanent review and adjustment. Responsibility for development, quality assurance, and monitoring implementation of procedures, is outside the Sales units.

Against the background of the Covid-19 pandemic, special attention is currently paid to macro-economic forecasts. In the context of this ongoing review, we also rely on projections published by the ECB, apart from those issued by our usual data providers. Yet estimation uncertainties are currently much higher than usual, as the pandemic has provoked a situation unprecedented in recent history. Data and experience are therefore both lacking.

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.

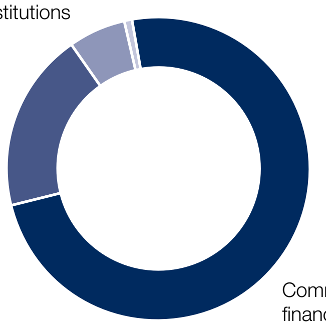
Within the process-oriented monitoring of individual exposures, the Bank uses various tools to monitor exposures on an ongoing basis: besides the tools already described, this includes rating reviews, the monitoring of payment arrears, and the regular, individual analysis of the largest exposures. The intensity of loan coverage is oriented upon the credit risk exposure.

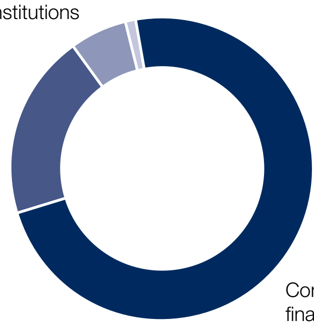
Against the background of the Covid-19 pandemic, Aareal Bank has established contact with national and international property financing clients subject to mandatory rating, and has amended contractual arrangements to clients' updated business plans to the extent necessary and possible. Given the lockdown, this primarily affected financings of hotels and shopping centres, as well as involving waivers

Breakdown of on-balance sheet and off-balance sheet business (gross carrying amounts)

by rating procedure, € bn

30 Jun 2021 | 31 Dec 2020





* Including the private client business of former WestImmo

of certain contractual agreements without impact on payments (covenants). Our clients and sponsors have provided a significant portion of the required liquidity from their own resources. Aareal Bank supported clients through deferrals of repayments totalling € 40 million as well as liquidity facilities of € 57 million. The gross carrying amount of the on-balance-sheet lending business under government moratoria amounted to € 29 million, whilst the gross carrying amount of on-balance sheet lending business subject to Covid-19-related forbearance measures amounted to € 7.2 billion. Measures related to Covid-19 – such as deferrals of repayments, or the provision of liquidity facilities – are being reported to the Management Board on a regular basis, and closely monitored.

On top of existing processes, additional measures were implemented for those portfolios particularly affected by the Covid-19 pandemic, such as retail, hotels, and student housing. These portfolios were subject to particular monitoring (regardless of whether liquidity facilities were provided), including ad-hoc valuation reviews of the financed properties, which were increasingly backed by external appraisals. The frequency for periodic monitoring and internal rating (which also comprise a detailed target/actual comparison of the business plan) was adjusted to a semi-annual cycle. The CRE Credit Risk Committee was closely involved in evaluating and assessing all credit or monitoring decisions. A separate reporting system was established for the affected portfolios, enabling follow-ups of individual exposures and providing credit-relevant information, in order to be able to derive suitable measures at portfolio level, at an early stage.

When accounting for these measures, we have taken the recommendations made by the IASB, and by relevant regulatory authorities such as the EBA, the ECB and ESMA, into consideration – with the objective of providing a realistic assessment of expected losses. Intensified handling triggers recognition of loss allowance, in the amount of lifetime expected credit loss for the financial instrument concerned (Stage 2). The same applies for financings for which a forbearance measure has been granted. The assumption that no significant decrease in credit quality has occurred is only made in exceptional cases when this is justified based on supportable information.

The following tables provide a breakdown of gross carrying amounts of on-balance sheet as well as off-balance sheet credit business, money-market business, and capital markets business, by rating

On-balance sheet commercial property finance business with mandatory rating

	30 Jun 2021					31 Dec 2020				
	Stage 1	Stage 2	Stage 3	fvpl[1)]	Total	Stage 1	Stage 2	Stage 3	fvpl[1)]	Total
€ mn										
Class 1										
Class 2	116				**116**	73				**73**
Class 3	204	4			**208**	249	4			**253**
Class 4	892				**892**	1,142				**1,142**
Class 5	3,797			160	**3,957**	3,684	9		249	**3,942**
Class 6	4,035	289		147	**4,471**	3,920	426		184	**4,530**
Class 7	3,495	521		50	**4,066**	2,991	297		253	**3,541**
Class 8	3,023	519		108	**3,650**	3,140	574		38	**3,752**
Class 9	1,975	1,044		12	**3,031**	2,565	1,271		14	**3,850**
Class 10	926	3,803		53	**4,782**	707	2,961		17	**3,685**
Class 11	248	729			**977**	453	514			**967**
Class 12	1	90			**91**	1	16			**17**
Classes 13-15										
Defaulted			1,613	91	**1,704**			1,547	95	**1,642**
Total	18,712	6,999	1,613	621	27,945	18,925	6,072	1,547	850	27,394

[1)] fvpl = at fair value through profit and loss (in accordance with IFRSs)

Off-balance sheet commercial property finance business with mandatory rating

	30 Jun 2021					31 Dec 2020				
	Stage 1	Stage 2	Stage 3	fvpl[1)]	Total	Stage 1	Stage 2	Stage 3	fvpl[1)]	Total
€ mn										
Classes 1-3										
Class 4	18				**18**	29				**29**
Class 5	183				**183**	69			10	**79**
Class 6	102				**102**	168				**168**
Class 7	64	0			**64**	87	0		14	**101**
Class 8	245	5			**250**	123	9			**132**
Class 9	172	0			**172**	158	41			**199**
Class 10	14	109			**123**	12	80			**92**
Class 11	28	14			**42**	30	11			**41**
Classes 12-15										
Defaulted			4		**4**			1	5	**6**
Total	826	128	4	–	958	676	141	1	29	847

[1)] fvpl = at fair value through profit and loss (in accordance with IFRSs); commitments for loan portions earmarked for syndication

On-balance sheet loans and advances to financial institutions

€ mn	30 Jun 2021					31 Dec 2020				
	Stage 1	Stage 2	Stage 3	fvpl[1]	Total	Stage 1	Stage 2	Stage 3	fvpl[1]	Total
Class 1	818				**818**	853				**853**
Class 2	277				**277**	213				**213**
Class 3	168				**168**	26				**26**
Class 4	136				**136**	108				**108**
Class 5	1				**1**	48				**48**
Class 6						26				**26**
Class 7	527				**527**	677				**677**
Class 8	354				**354**	320				**320**
Class 9	120				**120**					
Class 10	29				**29**	33				**33**
Classes 11-18										
Defaulted										
Total	**2,430**	**–**	**–**	**–**	**2,430**	**2,304**	**–**	**–**	**–**	**2,304**

[1] fvpl = at fair value through profit and loss (in accordance with IFRSs)

On-balance sheet loans and advances to sovereign states and local authorities

€ mn	30 Jun 2021					31 Dec 2020				
	Stage 1	Stage 2	Stage 3	fvpl[1]	Total	Stage 1	Stage 2	Stage 3	fvpl[1]	Total
Class 1	3,700				**3,700**	3,622				**3,622**
Class 2	1,614			27	**1,641**	1,674			26	**1,700**
Class 3	787			62	**849**	778			62	**840**
Class 4	72				**72**	76				**76**
Class 5	34				**34**	36				**36**
Class 6	134				**134**	177				**177**
Class 7	150				**150**	151				**151**
Class 8	0				**0**	1				**1**
Class 9	463	377			**840**	404	556			**960**
Classes 10-20										
Defaulted										
Total	**6,954**	**377**	**–**	**89**	**7,420**	**6,919**	**556**	**–**	**88**	**7,563**

[1] fvpl = at fair value through profit and loss (in accordance with IFRSs)

classes and loss allowance stages, in line with credit risk management at Group level. Compared to historical data, the impact of the Covid-19 pandemic has led to an increase in Stage 2 loss allowance; the higher level persists. Figures are based on Aareal Bank Group's internal default risk rating classes. The default definition follows the definition pursuant to Article 178 of the CRR, which is decisive for management purposes.

Monthly reporting covers the material aspects of credit risk; it is supplemented by detailed information – which also fully covers specific credit portfolio developments (broken down by country, property and product type, risk classes, and collateral categories, for example), in line with regulatory requirements – at least on a quarterly basis. Risk concentrations are being taken into account in particular.

Trading activities are 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 the majority of loans extended on its balance sheet until maturity; at the same time, targeted exit measures (including accelerated de-risking) 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, without any undue delay.

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.

Interest rate risk in the banking book

Definition

Interest rate risk in the banking book (IRRBB) is defined as the risk exposure of instruments held in the banking book which are sensitive to changes in interest rates, caused by yield curve shifts.

Specifically, for Aareal Bank this includes:

- risks arising from maturity transformation in the event of yield curve shifts (so-called gap risk), which, in turn, are broken down into:
  - risks from cash flows which are sensitive to interest rates, relative to the general yield curve (interest rate risk or repricing risk);
  - risks arising from the valuation of future cash flows, relative to the general yield curve (yield curve risk);
- risks from cash flows which are sensitive to interest rates, in terms of spreads to the general yield curve (basis risk);
- risks from explicit and implied options (option risk);
- risks arising from changing valuation of pension liabilities (pension risk);

- risks from fluctuations in the value of fund assets (fund risk); and

- risks from changes in Aareal Bank's specific funding spreads (funding risk).

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 exposure to interest rate risk in the banking book on a daily basis.

The VaR concept has been broadly accepted as the predominant method for measuring economic interest rate risk in the banking book. VaR quantifies risk as the maximum loss that will occur within a certain period of time, and given a defined probability.

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 99.9 % confidence interval under the economic perspective.

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 and deposits at notice which are factored into calculations for a period of up to ten 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 our goal to pursue a conservative approach adopted in our risk measurement processes.

Market risks

Definition

Market risks are broadly defined as the threat of losses due to changes in market parameters; this refers to market risks which are not assigned to the IRRBB. In particular, this also encompasses any type of spread risk exposure of instruments held in the banking book which are sensitive to changes in interest rates, and which are neither included in IRRBB nor in counterparty credit risk. Specifically, for Aareal Bank this includes:

- risks resulting from fluctuations of spot foreign exchange (FX) rates (spot FX risk);

- risks resulting from fluctuations of forward foreign exchange rates (forward FX risk); and

- risks from the regulatory review of the trading book (Financial Risk in the Trading Book – FRTB).

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 CRR. Given that no such trades were concluded during the period under review, trading book risks played a negligible role.

Commodities are irrelevant for the Bank's business. Exchange rate risks are largely eliminated through hedges.

Additional elements of market risk are:

- valuation risks due to changes in credit spreads (credit spread risk);

- specific price risks from the bond portfolio, wherein the bonds are mainly sovereign bonds (sovereign risk); and

- risks from adjustments to the credit valuation of OTC derivatives (CVA risk).

To differentiate spread risks (credit spread risk and sovereign risk) in terms of their credit risk exposure, reported market risk is adjusted accordingly.

Risk measurement and monitoring

Risk Controlling informs the members of the Management Board responsible for Treasury and risk monitoring about the risk position and market risk exposure on a daily basis.

The VaR concept has been broadly accepted as the predominant method for measuring economic market risk. VaR quantifies risk as the maximum loss that will occur within a certain period of time, and given a defined probability.

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[1] historical data pool maintained within the Bank. The loss potential is determined applying a 99.9 % confidence interval.

Backtesting

The quality of forecasts made using statistical models is checked through a monthly 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 99.9 %, only a small number of events are expected to break out of the VaR projection.

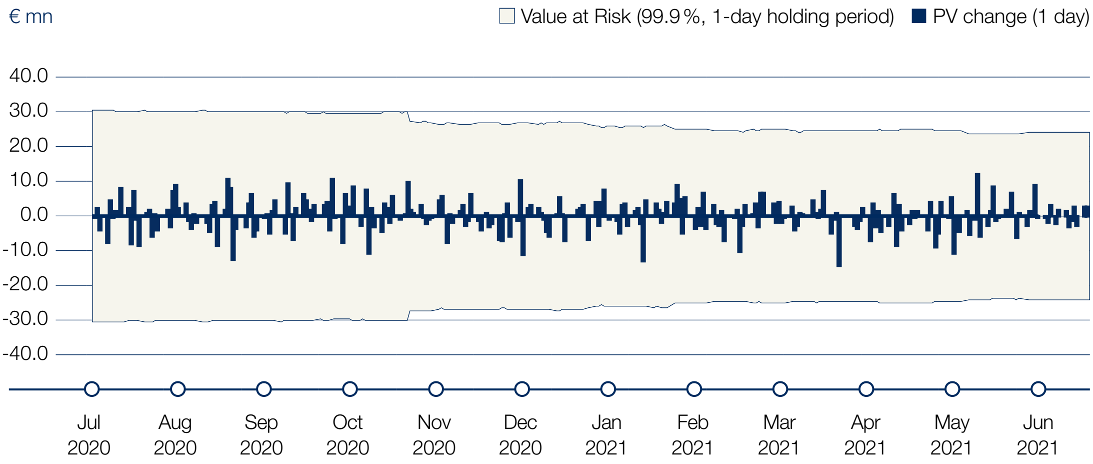
The backtesting exercise shown below comprises all risk positions subject to daily changes from the “Market risks” category.

No negative outliers were observed at Group level during the past 250 trading days, affirming the high forecasting quality of the VaR model we use.

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

Present values and 1-day VaR during the course of 2020/2021



[1] Historical data covering two years is used for the sub-risk type of credit spread risk.

also includes legal risks. To the extent that they are caused by operational risks, model 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 monitors any litigation the Bank is involved in (whether in court or out-of-court), and deals with any legal issues of fundamental importance.

Operational risk is quantified using the standardised approach. Supplementary operational risk management tools – in particular, the monitoring of indicators, analyses of loss events, scenario analyses and the self-assessment – do not indicate potential elevated risk nor did they indicate any material risk concentration.

Tools to control operational risk are supplemented by a system to manage and monitor outsourced activities and processes (outsourcing).

Investment risks

Aareal Bank defines 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.

All relevant Group entities are subject to regular audits, including a review and assessment of their risk situation within the framework of risk measurement and monitoring.

Property risks

We define property risk as the threat of unexpected losses arising from changes in the value of property held by the Bank, or by fully-consolidated subsidiaries.

Due to the special character of property risk (involving marketing risks, for example), special methods and procedures are employed to deal with investment risk. All relevant property holdings are subject to regular audits, including a review and assessment of their risk situation.

Business and strategic risks

Business and strategic risk is defined as the risk of unexpected losses, usually brought about by a decline in profits due to income falling short of expectations, whereby the shortfall cannot be compensated for by cost reductions. Strategic risk may emerge from changes in the competitive or regulatory environment, or due to unsuitable strategic positioning in the macro-economic environment.

In this context, we distinguish between investment risk and allocation risk, whereby allocation risk is already covered by various planning scenarios, and is thus incorporated in aggregate risk cover.

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.

As outlined in the Group Management Report 2020, liquidity risk is managed and monitored using a set of indicators, in accordance with both the normative and the economic perspective.

Report on Expected Developments and Opportunities

Macro-economic environment

The economy, financial markets and commercial property are all exposed to a number of different risks, although some of the downside risks started to dissipate or diminish by mid-2021. This is due, in part, to the improving diplomatic relations with the US since President Biden took office. There are, however, risks that could still have a negative impact. These include in particular the ongoing Covid-19 pandemic with its emerging viral mutations and associated economic restrictions. Doubts about the cohesion of the European project, increased government and private debt, geopolitical risks, and higher inflation pose other significant risks.

An ongoing Covid-19 pandemic due to high rates of new infections and viral mutations or a lack of vaccine success could slow or halt the recovery of the global economy. Extension or reintroduction of infection control measures could have adverse consequences on demand and the services sector in particular.

The political shift away from European cohesion poses a significant threat not only to the EU, but also to Europe, in the longer term. Nationalism among Central and Eastern European governments and the uncertainties surrounding the possible secession of the autonomous community of Catalonia from Spain must be mentioned in this context. The Covid-19 pandemic has also elevated the risk of a rise in populism in several countries. The reform backlog and structural economic problems in some euro zone countries present further uncertainties, risk and stress factors. While the EU's recovery package specifically seeks to support these countries, there is still the risk that the measures in place will not be enough to fully address structural problems at play and the negative impact of the Covid-19 pandemic.

Rising national debt, as a result of the massive fiscal support provided, but also as a consequence of the previous year's economic slump, is a global problem. While central banks continue to provide favourable refinancing conditions, risk premiums for highly indebted sovereigns could rise as bond-buying programmes come to an end. Non-financial corporate debt has expanded in many advanced economies, mainly due to an increase in bond issuance. An ongoing pandemic or other risks could be a reason for downgrading the rating of these bonds. In particular, ending special regulations and state aid poses a risk of higher insolvency rates for non-financial companies.

Despite some easing, the risk of disruption to free trade is still present and could intensify again in the future. In addition, further geopolitical risks such as cyberattacks, terrorism and political conflicts are likely to have a significant impact on markets and their participants.

Rising global demand from the conversion of pent-up savings into consumption and higher investment spending has already driven up prices. If this increased demand encounters capacity constraints further down the line, prices of some goods and services may rise more sharply, contributing to rising inflation. Stronger inflationary pressure is likely to lead to tighter monetary policy in the medium term.

Relating to macro-economic development, these factors are also significant for the financial and capital markets, and could trigger further disruption on these markets if they were to materialise to a considerable extent.

Economy

The increase in economic activity during the first half of the year and the sharp rise in private consumption support the assumption of strong real growth of the global economy for the full year 2021. Contact-intensive industries in particular should benefit from the impending recovery and there should be a shift in growth between manufacturing and services. However, pre-crisis levels will not be reached everywhere by the end of the year. Recovery is likely to be gradual and, in those regions hit hardest by the pandemic, it will take a long time. Uncertainties stem from the increase in the number of new infections and the emergence of new virus mutations, which in turn could slow down economic activity and delay the recovery by requiring additional infection control measures.

Real gross domestic product in the euro zone is expected to grow significantly for the full year 2021. Private consumption is expected to continue to increase and a substantial share of the savings accumulated by households will be spent over the next few months. In the second half of the year, funds from the EU recovery package will provide additional support. Since each member state has identified different investment priorities and is affected to varying degrees by the Covid-19 pandemic, the recovery of the EU member states will vary from country to country.

For the UK as well, strong economic recovery is expected for the full year 2021, which is likely to be even stronger than in the euro zone. Despite the recent spread of the Covid-19 delta variant, the lifting of infection control measures should help drive the consumer-led recovery. The trade agreement reached with the EU reduces uncertainties surrounding the movement of goods, even though it creates obstacles in the form of customs bureaucracy and regulatory barriers.

Similarly to the UK, we also expect strong full-year growth in the US. With the health situation increasingly normalising and the economy already gaining momentum in the first half of the year, large fiscal stimulus packages, recovering employment and rising optimism will all drive consumer growth. Imports are expected to grow faster than exports, leading to a widening of the current account deficit.

Looking at the Asia/Pacific region, our positive stance regarding full-year economic recovery and growth also applies to Australia and China.

Financial and capital markets, monetary policy and inflation

The risks and uncertainties referred to above are also significant for the financial and capital markets and could continue to create considerable disruption. However, we continue to assume that the funding markets will continue to offer favourable refinancing conditions.

In view of the existing uncertainties and in order not to interrupt the recovery that is underway, monetary and fiscal policy is expected to continue to be very expansive and interest rates to remain low in the second half of 2021. However, the persistent low interest rate environment might impair the effect of central banks' traditional policy.

Several factors are likely to push up inflation in the second half of the year. Firstly, energy prices are expected to rise further year-on-year, and secondly, some of the tax breaks associated with the pandemic will cease to apply. Combined with supply constraints across the industrial sector as a whole, the economic upswing is likely to be accompanied overall by marked price rises this year.

Regulatory environment

The Covid-19 pandemic impacted on the regulatory environment as well. Various regulatory initiatives were deferred and temporary relief resolved for financial institutions. Nonetheless, the trend towards a tighter regulatory framework is set to persist in the years ahead, too. For instance, the finalisation of the Basel III framework, adopted by the Basel Committee's Group of Governors and Heads of Supervision (GHOS), will bring about extensive changes to the approaches used for determining risk-weighted capital requirements (a concept known as "Basel IV"). In the course of the Covid-19 pandemic, the Basel Committee has deferred the date of application by one year to 1 January 2023. A second consultation on implementing Basel IV at European level, taking into account the experience gathered from the Covid-19 pandemic, is anticipated and likely to start during the second half of 2021.

The EBA guidelines on granting and monitoring loans will place further demands on a bank's internal governance (incl. in risk culture and strategy) and on the credit processes (incl. documentation, credit rating review) as well as the monitoring framework (e.g. ongoing monitoring of the credit terms).

These requirements at European level will be supplemented by an additional MaRisk amendment at national level, which will come into force in 2021.

Sector-specific and business developments

Structured Property Financing segment

Demand for commercial properties will vary in the second half of 2021, depending on the region and property type. In general, however, all property types stand to benefit from the assumed global economic growth. The Bank anticipates competition in the commercial property financing markets to remain intense, particularly in regions and for property types that were less adversely affected by the pandemic. While loan-to-value ratios for new business look set to remain stable, changes in the market environment could put direct pressure on margins, or result in higher loan-to-value ratios.

For commercial property, uncertainties persist due to the Covid-19 pandemic. This is an area in which developments surrounding the economic recovery will be decisive, especially given that some regions and property types have been more severely affected by the pandemic than others. This also applies to possible new infection control measures, which are likely to have different impacts depending on the country and property type. A potential renewed tightening of contact bans, travel restrictions and business closures of a temporary nature could have a significant negative impact on cash flows in the second half of the year, particularly for hotel and retail properties.

Moreover, other uncertainty factors and risks in the macro-economic environment are also relevant for commercial property markets. Various factors are expected to have an impact on how commercial property values develop in the second half of the year. While persistently low interest rates may support property values, political uncertainty, economic downturns and investor reticence as a result of emerging risks can all have an adverse impact on property values.

Over the next few years, we expect the market values of commercial property to remain stable, or to rise. Overall, commercial properties are likely to have already bottomed out in terms of value appreciation back in 2020. Considering the assumed recovery, most commercial properties should return to their pre-crisis values in the years to come. With a view to retail properties, we expect a slower recovery, as the structural change in buying behaviour is having a dampening effect on the outlook of value-driving rental revenues, depending on location and segment. Also subject to location and segment, we see hotel properties recovering to at least pre-crisis levels over the coming years, driven by increased travel activity. We expect a similar development with student housing, where demand from international students should recover over the next few years. As for office properties, we believe market values will rise over the next few years. However, value appreciation will be lower than in the pre-crisis period, as rental growth is expected to slow down. Logistics properties continue to be assessed positively, as we expect the trend of rising market values of these properties to prevail. Overall, however, the forecast is subject to greater uncertainty than usual on account of the Covid-19 pandemic, also against the background of the rapid spread of the highly contagious Delta variant, and any potential restrictions which might apply from the autumn of this year.

As a matter of principle, it is worth noting that estimation uncertainty – concerning the economy, markets, and the impact upon Aareal Bank – is currently much higher than usual, as the pandemic has provoked a situation unprecedented in recent history. Data and experience are therefore both lacking. Due to increased estimation uncertainties, there is also a “bad case” scenario in addition to our “swoosh” scenario. In the so-called “bad case”

%	2020	2021	2022	2023
“Swoosh” scenario				
Gross domestic product (year-on-year change in %)				
Euro zone	-7.1	4.5	4.6	2.1
USA	-3.5	7.7	4.5	1.9
UK	-10.3	7.7	6.2	2.1
Unemployment (%)				
Euro zone	8.0	8.4	8.5	8.0
US	8.1	5.2	4.0	3.6
UK	6.1	7.4	5.0	4.5
Portfolio-weighted property price development (2020 basis = 100%)		104.9	106.8	107.1
“Bad case” scenario				
Gross domestic product (year-on-year change in %)				
Euro zone	-7.1	-0.9	5.6	2.3
US	-3.5	0.0	4.2	1.7
UK	-10.3	-1.1	6.0	2.4
Unemployment (%)				
Euro zone	8.0	11.0	10.2	9.4
US	8.1	6.9	5.8	5.3
UK	6.1	10.8	9.2	7.8
Portfolio-weighted property price development (2020 basis = 100%)		97.6	99.8	99.9

scenario, loss allowance for the overall portfolio increases by approximately 20 basis points compared to our “swoosh” scenario in 2021. In line with current planning, these scenarios are based on the macro-economic factors shown in the table above.

In the Structured Property Financing segment, we aim to originate new business of between € 7 billion and € 8 billion for the 2021 financial year, so that Aareal Bank Group’s property financing portfolio is expected to be at approximately € 29 billion at the end of 2021, subject to exchange rate fluctuations. To manage our portfolio and risk exposure, we also use syndications.

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.

Banking & Digital Solutions segment

The German housing and commercial property industries are expected to continue showing solid development in 2021, in spite of the Covid-19 pandemic. Measures such as the short-time working furlough scheme and housing allowance relief as well as individual assistance agreements among housing enterprises helped cushion the impact of the crisis. We therefore expect property values to be very stable and rental income to remain largely steady.

A significant increase in the price of residential construction, driven by a rise in building costs, shortages of the necessary raw materials and capacity bottlenecks in the construction industry are likely to have a negative impact. This will also lead to less and less affordable and social housing: in 2002 there were more than 2.6 million residential units available under the rent control system, while in 2021 this figure dropped to just under 1.1 million.

Even though the Bank's market share in the institutional housing industry is already high based on the number of residential units, we see excellent opportunities for acquiring new clients and enhancing our existing client relationships during the remainder of the 2021 financial year. We plan to achieve this by continuing to invest in the expansion of the "Housing Industry Ecosystem", the cross-sector development of interface products, and the expansion into adjacent ecosystems, such as companies from the utilities and waste disposal industries. The focus here remains on, for example, the functional expansion of the Aareal Portal corporate client platform as regards the digitalisation of client communication and account processing.

In our view, the range of services that connect alternative online payment solutions to existing systems, thus helping to overcome process breaks (even across industry sectors), are particularly interesting. The Aareal Exchange & Payment Platform, which integrates alternative payment methods with existing accounting systems, has been available since 2020 with an interface to viacash and was expanded in May 2021 to include additional payment methods such as PayPal and credit cards. We also see potential in technical solutions for automating billing processes as part of electromobility in the network of charging stations. The corresponding Aareal Connected Payments product was launched successfully on the market in 2020. Further growth is anticipated from the integrated rental security product Aareal Aval and from Aareal Meter, a solution that uses mobile meter reading and subsequent data capture without disrupting traffic to provide a digital solution to a labour-intensive analogue process gap.

In view of this, we are aiming for renewed net commission income growth over the previous year (2020: € 26 million) and currently expect an average deposit volume from the housing industry slightly above € 11 billion. The persistently low interest rate environment, which is relevant for the results from our deposit-taking business, will continue to burden 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, stable and additional source of funding for Aareal Bank.

Aareon segment

Aareon will continue to implement and accelerate its growth strategy in the 2021 financial year. In this context, the Aareon Flight Plan 2021 was developed and launched in the fourth quarter of 2020. This plan integrates measures from a Value Creation Programme, including inorganic growth projects, as well as investments in existing and new products.

The Covid-19 pandemic already impacted Aareon in the first half of the year, and will continue to do so throughout 2021, particularly in the consulting business in Germany. The Covid-19 pandemic is expected to result in greater digitalisation needs in the medium term and therefore to an increase in the demand for digital solutions and advisory services. In this context, Aareon continues to expect double-digit growth rates of over 20 % in digital solutions in the 2021 financial year (2020: 19 %). Sales revenue generated from ERP products is expected to grow in the lower single-digit range. Overall, a marked increase in consolidated sales revenue is expected for 2021, to which further acquisitions are now also contributing. As a result of the marketing initiative for SaaS rental models for Aareon Wodis Sigma and Yuneo launched in Germany in the first half of the year, Aareon expects lower licence revenues than originally forecast. This is part of the Value Creation Programme. In the medium term, recurring revenues will also be higher as a result. Despite high investment expenditure, including for the existing product portfolio, we expect an increase in adjusted EBITDA[1].

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[1] "Earnings before interest, taxes, depreciation and amortisation" before new products, Value Creation Programme (VCP), ventures, M&A activities and non-recurring effects.

Aareon will become a "Rule of 40" entity in the medium term. This indicator is widely used in the software industry to identify efficient growth companies whose revenue growth and EBITDA margin add up to at least 40 %.

Demand for the new product generation Aareon Wodis Yuneo, which was introduced in 2020, will be important for the ERP business in the DACH region. Aareon anticipates further revenue growth for its ERP solution RELion, which focuses on the commercial property market. The business volume generated from Aareon Cloud Services and BauSecura insurance management will be up slightly on the previous year. Further growth will come from the acquisitions of Arthur Online Ltd, London (from February 2021), Twinq-B.V., Oosterhout, the Netherlands (from May 2021), and RentPro Ltd. and Curo Software Ltd. (Tilt), both Warrenpoint, UK (both from July 2021). In the Netherlands, despite the ongoing shift in the business model from licensing to SaaS operations, the 2020 revenue level is expected to be exceeded based on a strong order book. We also expect sales revenues to increase in France. On the UK market, client acquisitions in 2020 in particular are expected to have a positive impact on recurring revenues in 2021. In the Nordic region, sales will be somewhat lower because the new product-generation will be launched later than originally planned.

The digital solutions will make a decisive contribution towards realising the growth potential in the DACH region and in the international business. SaaS revenues are expected to increase for the WRM and CRM products due to additional products being rolled out. Regarding Business Relationship Management (BRM) products, the acquisition of Tactile Ltd. (Fixflo), London (from May 2021), will contribute to growth. Higher sales revenues with SRM products should be achieved thanks to a greater number of tradesmen' orders that are settled via Mareon. In France, Aareon sees significant growth opportunities through to the end of the year, particularly in the licensing business.

Aareon expects good demand for the consulting business, in particular for green consulting, against the background of the Covid-19 pandemic. Traditional consulting offerings are also expected to be used again increasingly during the year; nonetheless, renewed lockdowns will impact on consulting revenue in 2021. This will lead to significantly lower sales revenues than originally expected, particularly in the DACH region.

Aareon will continue in 2021 with the development drive in new products and services that was launched in 2019. The virtual assistant Neela and the Aareon Smart Platform and Smart Partner solutions will be developed further and new functional features added. Further product developments are planned for 2021 in preventive maintenance and in networking clients, public offices and utilities, among others, on a digital platform and for mobile solutions. Aareon is also investing in developing new lines of business by co-founding start-ups. Capacities were also extended to drive Aareon's inorganic growth.

Based on the preceding explanations, and including M&A transactions, Aareon anticipates a significant increase in sales revenues to between € 276 million and € 280 million for the current year (2020: € 258 million). Adjusted EBITDA[1] is likely to further increase to between € 63 million and € 65 million (2020: € 62 million).

Business strategy

Aareal Bank Group's strategy focuses on sustainable business success. Environmental, social and governance aspects are therefore key elements of its business strategy. The medium-term strategic development is therefore being pursued under the guiding principle of "Aareal Next Level". The general strategic orientation will continue – with large-volume, international commercial property financing on the one hand, and consulting offers and digital solutions for the institutional housing industry in Europe and related industries on the

[1] "Earnings before interest, taxes, depreciation and amortisation" before new products, Value Creation Programme (VCP), ventures, M&A activities and non-recurring effects.

other. The individual business activities will be developed in a targeted manner, in order to sharpen their own independent profiles, accelerate the Group's growth overall and create value for the shareholders and other stakeholders.

Within the scope of a strategic review, Aareal Bank examined whether Aareal Bank Group's business model would remain viable in a normalised environment, once the pandemic has been overcome. Some adjustments have been made within the existing "Aareal Next Level" strategic framework in order to be able to fully exploit the opportunities arising from changes induced by Covid-19, and to retain the Bank's successful performance in the future. The Company intends to exploit opportunities for profitable growth in all three segments:

The Structured Property Financing segment continues to focus on the controlled, risk-conscious expansion of its portfolio volume within its target range, taking advantage of its flexible approach with regard to countries, asset classes and financing structures.

Within the Banking & Digital Solutions segment, Aareal Bank aims to expand its equity-efficient business in particular, and thus increase net commission income, mainly by expanding its product offering in the digital segment and through further strategic partnerships.

The Bank aims to further strengthen the market position of its IT subsidiary Aareon in the coming years and to significantly increase the value and earnings contribution for the Group and its shareholders. Together with its partner Advent International, which acquired a minority stake in Aareon in the second half of 2020 (closing in October 2020), the Bank intends to further intensify the company's pace of growth, through organic growth initiatives as part of the Value Creation Programme as well as through new, digital products and solutions in particular, and through greater up- and cross-selling in the existing client base. It is also planning further related acquisitions. An institutionalised M&A pipeline supports our inorganic growth.

Besides the growth initiatives for the three segments, Aareal Bank Group will use additional levers to sustainably raise profitability, including an optimisation of the funding mix and the capital structure. In addition, numerous measures are being implemented to enhance the efficiency of the organisational structure, processes and infrastructure. As an example, the "IT Next Level" initiative will further reduce complexity in the IT infrastructure, expanding cloud-based applications. In addition, the Group plans to streamline management structures across divisions.

Given the general market environment, regulatory dividend restrictions, and the prospects arising from the results of our strategic review process, including Aareon's Value Creation Programme, our shareholder group together with its expectations have already changed, with further changes possibly arising in this respect. One indicator of this is the significant interest that financial investors have been showing for some time now in companies operating in the financial sector. Should new investors acquire substantial stakes in Aareal Bank, further strategic options could arise.

Group targets

Besides the strategic measures and initiatives within the framework of "Aareal Next Level", Aareal Bank Group's focus in the 2021 financial year has been and will continue to be on coping with the impact of the Covid-19 pandemic in the best way possible – together with its clients. In this context, it is crucial to determine how quickly the emerging recovery of the real economy gains momentum. With a view to the economic development, Aareal Bank Group continues to anticipate a "swoosh-shaped" trend and expects a marked recovery during this year and 2022.[1)]

Based on this assumption and current insights, Aareal Bank Group expects a clearly positive

[1)] For details, please refer to our explanations and the description of macro-economic influencing factors in the Report on Expected Developments and Opportunities of the Structured Property Financing segment.

consolidated operating profit in a range of between € 100 million and € 175 million for 2021 as a whole, despite high loss allowance (2020: € -75 million). Taking the non-recurring adverse tax effect into account, the tax rate for 2021 is expected at an average of 55 %. With operating profit at the upper end of the range, the expected tax rate would be around 50 %, and 60 % at the lower end of the range – in each case in line with the relative share of non-tax-deductible items in the result. Depending on said range of operating profit, earnings per share (EpS) is projected – on a purely mathematical basis – between around € 0.40 and around € 1.20 (2020: € -1.50), with RoE after taxes between around 1 % and around 3 % (2020: -3.6 %). Naturally, in the current environment, this forecast is subject to significant uncertainty, especially with regard to the assumed duration and intensity of the crisis, the pace of recovery and the associated effects on our clients, as well as prevailing uncertainty concerning regulatory and accounting provisions, and the possibility that individual loan defaults cannot be reliably predicted.

Income is expected to rise significantly over the previous year. Net interest income should rise to between € 550 million and € 580 million (2020: € 512 million), reflecting the higher (and further growing) loan portfolio. Net commission income should rise further, thanks in particular to Aareon's growth, to between € 250 million and € 270 million (2020: € 234 million). Based on our "swoosh" scenario, we estimate loss allowance to be in a range between € 125 million and € 200 million (2020: € 344 million). Uncertainty affecting this item is higher than usual on account of the Covid-19 pandemic, also against the background of the rapid spread of the highly contagious Delta variant, and any potential restrictions which might apply from the autumn of this year.

Administrative expenses are expected to amount to between € 520 million and € 540 million (2020: € 469 million). Besides lower cost savings due to Covid-19, this reflects the planned growth of Aareon and the initiatives launched on the basis of the strategic review.

In the Structured Property Financing segment, a portfolio size of around € 29 billion is planned by the end of the year, market conditions permitting and subject to exchange rate fluctuations. Aareal Bank expects new business volume of € 7 billion to € 8 billion on this basis.

For the Banking & Digital Solutions segment, we are aiming at further slight net commission income growth (2020: € 26 million) and expect an average deposit volume from the housing industry of around € 11 billion.

It is expected that Aareon will see a marked increase in sales revenue in the region of € 276 million to € 280 million for the current year (2020: € 258 million). Adjusted EBITDA[1] is expected to further increase to between € 63 million and € 65 million (2020: € 62 million).

Aareal Bank envisages to achieve consolidated operating profit in an amount of approximately € 300 million already in 2023. This is of course provided the pandemic has been fully overcome by then.

With regard to capitalisation, Aareal Bank expects a CET1 ratio (Basel IV (phase-in)) of more than 16 % by the end of the year, despite the planned portfolio growth and subject to further regulatory changes or requirements.

[1] "Earnings before interest, taxes, depreciation and amortisation" before new products, Value Creation Programme (VCP), ventures, M&A activities and non-recurring effects.

Consolidated Interim Financial Statements
Statement of Comprehensive Income
Income Statement

€ mn	Note	1 Jan-30 Jun 2021	1 Jan-30 Jun 2020
Interest income from financial instruments (ac and fvoci)		367	370
Interest income from financial instruments (fvpl)		14	22
Market-driven modification gains		1	0
Interest expenses for financial instruments (ac and fvoci)		35	42
Interest expenses for financial instruments (fvpl)		66	104
Market-driven modification losses		1	1
Net interest income	1	**280**	**245**
Loss allowance excluding credit-driven net modification gain or loss		40	106
Credit-driven net modification gain or loss		0	0
Loss allowance	2	**40**	**106**
Commission income		146	137
Commission expenses		28	26
Net commission income	3	**118**	**111**
Net gain or loss on the derecognition of financial assets (ac)		6	11
Net gain or loss on the derecognition of financial liabilities (ac)		2	5
Net gain or loss on the derecognition of financial assets (fvoci)		0	–
Net derecognition gain or loss	4	**8**	**16**
Net gain or loss from financial instruments (fvpl)	5	-4	-7
Net gain or loss from hedge accounting	6	-2	2
Net gain or loss from investments accounted for using the equity method		-1	0
Administrative expenses	7	268	238
Net other operating income/expenses	8	-18	-10
Operating profit		**73**	**13**
Income taxes		40	-3
Consolidated net income		**33**	**16**
Consolidated net income attributable to non-controlling interests		2	1
Consolidated net income attributable to shareholders of Aareal Bank AG		31	15
Earnings per share (EpS)			
Consolidated net income attributable to shareholders of Aareal Bank AG[1]		31	15
of which: allocated to ordinary shareholders		24	7
of which: allocated to AT1 investors		7	8
Earnings per ordinary share (€)	9	0.40	0.11
Earnings per AT1 unit (€)	9	0.07	0.08

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

Statement of Comprehensive Income

Reconciliation from Consolidated Net Income to Total Comprehensive Income

€ mn	1 Jan – 30 Jun 2021	1 Jan – 30 Jun 2020
Consolidated net income	**33**	**16**
Items that will not be reclassified subsequently to profit or loss		
Changes in the reserve from remeasurements of defined benefit plans	**25**	**-9**
Remeasurements of defined benefit plans	36	-13
Taxes on remeasurements of defined benefit plans	-11	4
Changes in the reserve from the measurement of equity instruments (fvoci)	**1**	**0**
Gains and losses from equity instruments (fvoci)	1	0
Reclassifications to retained earnings from equity instruments (fvoci)	–	–
Taxes on gains and losses from equity instruments (fvoci)	0	0
Items that are reclassified subsequently to profit or loss		
Changes in the reserve from the measurement of debt instruments (fvoci)	**-4**	**-5**
Gains and losses from debt instruments (fvoci)	-6	-8
Reclassifications to the income statement from debt instruments (fvoci)	–	–
Taxes on gains and losses from debt instruments (fvoci)	2	3
Changes in the reserve from foreign currency basis spreads	**-2**	**4**
Gains and losses from foreign currency basis spreads	-3	6
Reclassifications to the income statement from foreign currency basis spreads	–	–
Taxes on gains and losses from foreign currency basis spreads	1	-2
Changes in currency translation reserves	**5**	**-3**
Gains and losses from translating foreign operations' financial statements	3	-2
Reclassifications to the income statement from translating foreign operations' financial statements	–	–
Taxes on gains and losses arising from translating foreign operations' financial statements	2	-1
Other comprehensive income	**25**	**-13**
Total comprehensive income	**58**	**3**
Total comprehensive income attributable to non-controlling interests	3	1
Total comprehensive income attributable to shareholders of Aareal Bank AG	55	2

Statement of Financial Position

€ mn	Note	30 Jun 2021	31 Dec 2020
Assets			
Financial assets (ac)	10	**39,478**	**37,999**
Cash funds (ac)		5,838	4,744
Loan receivables (ac)		27,863	27,277
Money market and capital market receivables (ac)		5,705	5,884
Receivables from other transactions (ac)		72	94
Loss allowance (ac)	11	-472	-592
Financial assets (fvoci)	12	**3,971**	**3,672**
Money market and capital market receivables (fvoci)		3,965	3,667
Equity instruments (fvoci)		6	5
Financial assets (fvpl)	13	**2,265**	**3,167**
Loan receivables (fvpl)		624	856
Money market and capital market receivables (fvpl)		93	93
Positive market value of designated hedging derivatives (fvpl)		1,097	1,431
Positive market value of other derivatives (fvpl)		451	787
Non-current assets held for sale	14	59	–
Investments accounted for using the equity method		22	13
Intangible assets	15	306	207
Property and equipment	16	282	289
Income tax assets		126	116
Deferred tax assets		150	176
Other assets	17	457	431
Total		**46,644**	**45,478**
Equity and liabilities			
Financial liabilities (ac)	18	**41,153**	**39,823**
Money market and capital market liabilities (ac)		29,478	28,206
Deposits from the housing industry (ac)		10,957	10,592
Liabilities from other transactions (ac)		105	86
Subordinated liabilities (ac)		613	939
Financial liabilities (fvpl)	19	**1,753**	**1,906**
Negative market value of designated hedging derivatives (fvpl)		1,049	1,298
Negative market value of other derivatives (fvpl)		704	608
Provisions	20	548	583
Income tax liabilities		15	20
Deferred tax liabilities		37	36
Other liabilities	21	146	143
Equity	22	**2,992**	**2,967**
Subscribed capital		180	180
Capital reserves		721	721
Retained earnings		1,899	1,902
AT1 bond		300	300
Other reserves		-173	-197
Non-controlling interests		65	61
Total		**46,644**	**45,478**

Statement of Changes in Equity

€ mn	Subscribed capital	Capital reserves	Retained earnings	AT1 bond	Other reserves					Total	Non-controlling interests	Equity
					Reserve from remeasurements of defined benefit plans	Reserve from the measurement of equity instruments (fvoci)	Reserve from the measurement of debt instruments (fvoci)	Reserve from changes in the value of foreign currency basis spreads	Currency translation reserve			
Equity as at 1 Jan 2021	**180**	**721**	**1,902**	**300**	**-166**	**-4**	**12**	**-26**	**-13**	**2,906**	**61**	**2,967**
Total comprehensive income for the period	–	–	31	**–**	24	1	–4	–2	5	**55**	3	**58**
Payments to non-controlling interests	–	–	–	**–**	–	–	–	–	–	**–**	-2	**-2**
Dividends	–	–	-24	**–**	–	–	–	–	–	**-24**	–	**-24**
AT1 coupon	–	–	-14	**–**	–	–	–	–	–	**-14**	–	**-14**
Changes in ownership interests in subsidiaries	–	–	5	**–**	–	–	–	–	–	**5**	2	**7**
Other changes	–	–	-1	**–**	–	–	–	–	–	**-1**	1	**–**
Equity as at 30 Jun 2021	180	721	1,899	300	-142	-3	8	-28	-8	2,927	65	2,992

Mio. €	Subscribed capital	Capital reserves	Retained earnings	AT1 bond	Other reserves					Total	Non-controlling interests	Equity
					Reserve from remeasurements of defined benefit plans	Reserve from the measurement of equity instruments (fvoci)	Reserve from the measurement of debt instruments (fvoci)	Reserve from changes in the value of foreign currency basis spreads	Currency translation reserve			
Equity as at 1 Jan 2020	**180**	**721**	**1,812**	**300**	**-141**	**-4**	**7**	**-15**	**-1**	**2,859**	**2**	**2,861**
Total comprehensive income for the period	–	–	15	**–**	-9	0	-5	4	-3	**2**	1	**3**
Payments to non-controlling interests	–	–	–	**–**	–	–	–	–	–	**–**	-2	**-2**
Dividends	–	–	–	**–**	–	–	–	–	–	**–**	–	**–**
AT1 coupon	–	–	-16	**–**	–	–	–	–	–	**-16**	–	**-16**
Changes in ownership interests in subsidiaries	–	–	–	**–**	–	–	–	–	–	**–**	–	**–**
Other changes	–	–	–	**–**	1	–	–	–	–	**1**	–	**1**
Equity as at 30 Jun 2020	180	721	1,811	300	-149	-4	2	-11	-4	2,846	1	2,847

Statement of Cash Flows (condensed)

€ mn	2021	2020
Cash and cash equivalents as at 1 January	**4,744**	**1,494**
Cash flow from operating activities	1,465	2,909
Cash flow from investing activities	-10	-22
Cash flow from financing activities	-361	-28
Total cash flow	**1,094**	**2,859**
Cash and cash equivalents as at 30 June	**5,838**	**4,353**

Notes (condensed)

Basis of Accounting

Legal framework

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

This half-yearly financial report for the period ended 30 June 2021 was prepared pursuant to the provisions of section 115 of the German Securities Trading Act (Wertpapierhandelsgesetz – "WpHG") in conjunction with section 117 no. 2 of the WpHG and was approved for publication by the Management Board on 5 August 2021. It comprises the present condensed consolidated interim financial statements, as well as an interim group management report.

Aareal Bank AG prepares its condensed consolidated interim 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 consolidated interim 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. The present interim report is based on the same consolidation methods as were applied in the consolidated financial statements 2020.

In the reporting period, several companies or groups were added to the reporting entity structure: Arthur Online Ltd. and Tactile Ltd. (Fixflow), two British software specialists for small and medium-sized property managers and for property servicing and maintenance, as well as Twinq Holding B.V., a Dutch software specialist for the private housing market. Moreover, companies were established for a Management Equity Programme introduced by Aareon. There were no other material changes to the reporting entity structure.

Accounting policies

Unless specifically indicated otherwise, the accounting policies applied in preparation of the consolidated financial statements 2020 were also applied in preparation of these condensed consolidated interim financial statements, including the calculation of comparative figures.

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

- **IFRS 9/IFRS 7 Interest Rate Benchmark Reform (Phase 2)**
  The second phase of the standard amendments as a result of the effects of the IBOR reform refers to the period when the existing interest rate benchmarks are replaced. Apart from hedge accounting requirements, the amendments concern practical expedients regarding the recognition of modifications of financial instruments and other disclosure requirements.

  The effects of the IBOR reform are analysed and monitored, and any resulting new requirements are implemented, as part of a separate project. The transition of collateral agreements and of discounting OTC derivatives has been implemented gradually on a case-by-case basis in accordance with the bilateral agreements between the counterparties from the second half of 2020. Any existing hedging relationships did not have to be discontinued.

  The necessary adjustments for new business were made to account for the new benchmark interest rates. The adjustments referred to the currencies EUR (€STR), GBP (SONIA), USD (SOFR) and CHF (SARON). First transactions involving the new benchmark rates have already been entered into.

  The existing transactions will be changed on a currency-by-currency basis. As a result of the discontinuation of the CHF and GBP LIBOR as at 31 December 2021, the related existing transactions will be switched to the new benchmark rates by year-end. First transitions to SONIA and SARON have already been made. This was partly implemented using the practical relief applicable to the accounting treatment for modifications.

  Overall, we do not expect any material effects from transition. To the extent that transactions are concluded using the new interest rate benchmarks and/or existing transactions are changed to refer to such new benchmarks, this will be taken into account as part of the risk management strategy.

- **Covid-19-related rent concessions**
  The amendments grant lessees an exemption from the assessment as to whether rent concessions granted due to the Covid-19 pandemic (such as rent free periods or temporary rent reductions) constitute a lease modification. If an entity elects to apply this exemption, rent concessions have to be accounted for as if they did not represent modifications of the lease agreement. The changes originally applied to rent concessions which lead to a reduction of the rental payments due on or before 30 June 2021. Application was prolonged in the current financial year until 30 June 2022. In the 2020 financial year, Aareal Bank Group decided to opt for an early application of these standards. There were no relevant rent concessions in the reporting period.

The revised standards did not have any material consequences for the consolidated financial statements of Aareal Bank Group.

Notes to the Statement of Comprehensive Income

(1) Net interest income

€ mn	1 Jan-30 Jun 2021	1 Jan-30 Jun 2020
Interest income from financial assets (ac and fvoci)	327	359
Loan receivables	327	359
Money market and capital market receivables	0	0
Interest income from financial liabilities (ac)	40	11
Money market and capital market liabilities	30	4
Deposits from the housing industry	10	7
Interest income from financial instruments (fvpl)	14	22
Loan receivables	9	10
Money market and capital market receivables	2	3
Other derivatives	3	9
Market-driven modification gains	1	0
Total interest and similar income	**382**	**392**
Interest expenses for financial liabilities (ac)	10	35
Money market and capital market liabilities	1	24
Deposits from the housing industry	0	0
Liabilities from other transactions	1	0
Subordinated liabilities	8	11
Interest expenses from financial assets (ac and fvoci)	25	7
Cash funds	17	5
Money market and capital market receivables	8	2
Interest expenses for financial instruments (fvpl)	66	104
Other derivatives	66	104
Market-driven modification losses	1	1
Total interest and similar expenses	**102**	**147**
Total	**280**	**245**

At € 280 million, net interest income was significantly higher than in the previous year (€ 245 million), as expected. This was largely due to the higher loan portfolio over the previous year and the interest benefit of € 12 million received as part of the ECB's Targeted Longer-Term Refinancing Operations (TLTRO 3).

(2) Loss allowance

€ mn	1 Jan-30 Jun 2021	1 Jan-30 Jun 2020
Additions	111	124
Reversals	70	18
Recoveries on loans and advances previously written off	1	0
Loss allowance – other items	–	–
Credit-driven net modification gain or loss	0	0
Total	**40**	**106**

As expected, loss allowance of € 40 million was significantly below the previous year's figure (€ 106 million), which was particularly influenced by Covid-19. The Stage 3 loss allowance mainly increased due to three new loan defaults. Moreover, we used a reversal of loss allowance for a defaulted loan to conclude the accelerated de-risking in Italy; on aggregate, this required additional loss allowance of € 13 million.

Please also refer to Note (11).

(3) Net commission income

€ mn	1 Jan - 30 Jun 2021	1 Jan - 30 Jun 2020
Commission income from		
ERP products (incl. add-on products)	91	87
Digital solutions	33	30
Banking business and other activities	22	20
Total commission income	**146**	**137**
Commission expenses for		
Purchased services	25	23
Banking business and other activities	3	3
Total commission expenses	**28**	**26**
Total	**118**	**111**

Net commission income increased as planned to € 118 million (H1 2020: € 111 million) as a result of higher commission income both in the Banking & Digital Solutions segment and at Aareon.

(4) Net derecognition gain or loss

€ mn	1 Jan - 30 Jun 2021	1 Jan - 30 Jun 2020
Net gain or loss on the derecognition of financial assets (ac)		
Loan receivables	9	11
Money market and capital market receivables	-3	–
Net gain or loss on the derecognition of financial liabilities (ac)		
Money market and capital market liabilities	2	5
Net gain or loss on the derecognition of financial assets (fvoci)		
Money market and capital market receivables	0	–
Total	**8**	**16**

The net derecognition gain of € 8 million (H1 2020: € 16 million) resulted from market-driven effects of early loan repayments, which also more than compensated for de-risking measures of € 3 million in the securities portfolio. In this context, Italian government bonds were sold in a nominal volume of € 50 million. The previous year's figure included non-recurring income from repurchases in the Treasury business within the scope of market support.

(5) Net gain or loss from financial instruments (fvpl)

€ mn	1 Jan-30 Jun 2021	1 Jan-30 Jun 2020
Net gain or loss from loan receivables	-4	-12
Net gain or loss from money market and capital market receivables	0	-5
Net gain or loss from other derivatives	3	9
Currency translation	-3	1
Total	**-4**	**-7**

The net gain or loss from financial instruments (fvpl) primarily resulted from credit-risk induced measurement losses of defaulted property loans.

(6) Net gain or loss from hedge accounting

€ mn	1 Jan-30 Jun 2021	1 Jan-30 Jun 2020
Ineffective portion of fair value hedges	-2	2
Ineffective portion of net investment hedges	0	0
Total	**-2**	**2**

(7) Administrative expenses

€ mn	1 Jan-30 Jun 2021	1 Jan-30 Jun 2020
Staff expenses	157	137
Wages and salaries	124	107
Social security contributions	20	18
Pensions	13	12
Other administrative expenses	89	80
Depreciation, amortisation and impairment of property and equipment and intangible assets	22	21
Total	**268**	**238**

Administrative expenses rose to € 268 million (H1 2020: € 238 million). As expected, this is due on the one hand to business expansion and investments into new products, Aareon's Value Creation Programme (VCP), ventures and M&A activities, as well as to lower cost savings made during the Covid-19 pandemic, compared to the previous year. On the other hand, compared with the previous year and in relation to the planning, higher provisions were recognised overall for the bank levy and contributions to the deposit guarantee scheme, due to a deposit protection event (Greensill) and other effects.

(8) Net other operating income/expenses

€ mn	1 Jan-30 Jun 2021	1 Jan-30 Jun 2020
Income from properties	6	5
Income from the reversal of provisions	0	0
Income from goods and services	0	0
Other operating income	6	19
Total other operating income	**12**	**24**
Expenses for properties	13	26
Expenses for other taxes	3	3
Miscellaneous other operating expenses	14	5
Total other operating expenses	**30**	**34**
Total	**-18**	**-10**

Net other operating income/expenses were burdened by € 11 million in interest on tax back payments as well as lower results from properties held by the Bank, as a result of Covid-19. The previous year's result included a Covid-19-related impairment of a property held by the Bank.

(9) Earnings per share

Earnings per ordinary share are determined by dividing the earnings attributable 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.

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. Basic earnings per AT1 unit correspond to diluted earnings per AT1 unit.

Notes to the Statement of Financial Position

(10) Financial assets (ac)

€ mn	30 Jun 2021	31 Dec 2020
Cash funds (ac)	**5,838**	**4,744**
Cash on hand	0	0
Balances with central banks	5,838	4,744
Loan receivables (ac)	**27,863**	**27,277**
Property loans	27,479	26,852
Public-sector loans	343	360
Other loan receivables	41	65
Money market and capital market receivables (ac)	**5,705**	**5,884**
Money market receivables	1,029	1,029
Promissory note loans	1,645	1,714
Bonds	3,031	3,141
Receivables from other transactions (ac)	**72**	**94**
Trade receivables	25	40
Other financial receivables	47	54
Total	**39,478**	**37,999**

(11) Loss allowance (ac)

30 June 2021

€ mn	Stage 1	Stage 2	Stage 3	Receivables from other transactions (ac)	Total loss allowance (ac)
Balance as at 1 January	**19**	**77**	**492**	**4**	**592**
Additions	8	21	80	0	**109**
Utilisation	–	–	146	1	**147**
Reversals	8	20	40	0	**68**
Transfer to Stage 1	0	0	–	–	**–**
Transfer to Stage 2	-5	5	–	–	**–**
Transfer to Stage 3	–	0	0	–	**–**
Interest rate effect	–	–	37	–	**37**
Currency adjustments	0	3	10	0	**13**
Transfers	–	–	-64	–	**-64**
Balance as at 30 June	**14**	**86**	**369**	**3**	**472**

The loss allowance for financial assets measured at amortised cost refers to loan receivables, money and capital market receivables as well as receivables from other transactions (largely trade receivables) that are measured at amortised cost.

30 June 2020

€ mn	Stage 1	Stage 2	Stage 3	Receivables from other transactions (ac)	Total loss allowance (ac)
Balance as at 1 January	**22**	**16**	**345**	**3**	**386**
Additions	20	17	82	2	**121**
Utilisation	–	–	7	–	**7**
Reversals	6	7	4	0	**17**
Transfer to Stage 1	0	0	–	–	**–**
Transfer to Stage 2	-3	3	–	–	**–**
Transfer to Stage 3	–	-1	1	–	**–**
Interest rate effect	–	–	3	–	**3**
Currency adjustments	0	0	-3	0	**-3**
Balance as at 30 June	**33**	**28**	**417**	**5**	**483**

(12) Financial assets (fvoci)

€ mn	30 Jun 2021	31 Dec 2020
Money market and capital market receivables (fvoci)	**3,965**	**3,667**
Bonds	3,965	3,667
Equity instruments (fvoci)	**6**	**5**
Equities and other non-fixed income securities	0	0
Other investments	6	5
Total	**3,971**	**3,672**

(13) Financial assets (fvpl)

€ mn	30 Jun 2021	31 Dec 2020
Loan receivables (fvpl)	**624**	**856**
Property loans	621	852
Other loan receivables	3	4
Money market and capital market receivables (fvpl)	**93**	**93**
Promissory note loans	89	89
Bonds	–	–
Fund units	4	4
Positive market value of designated hedging derivatives (fvpl)	**1,097**	**1,431**
Positive market value of fair value hedges	1,058	1,343
Positive market value of net investment hedges	39	88
Positive market value of other derivatives (fvpl)	**451**	**787**
Positive market value of economic hedging derivatives	304	578
Positive market value of miscellaneous derivatives	147	209
Total	**2,265**	**3,167**

(14) Non-current assets held for sale

Property loans with a carrying amount of € 59 million held by the Structured Property Financing segment fulfilled the criteria for being classified as "held for sale" as at 30 June 2021. Both property loans have now been sold. The criteria for classification as "held for sale" were met after 30 June 2021 for another property loan in the amount of € 69 million, which is also expected to be sold in the second half of the year.

(15) Intangible assets

€ mn	30 Jun 2021	31 Dec 2020
Goodwill	182	102
Proprietary software	57	55
Other intangible assets	67	50
Total	**306**	**207**

The increase in goodwill reflected the acquisitions of Arthur Online Ltd, Tactile Ltd (Fixflo), and Twinq Holding B.V.

(16) Property and equipment

€ mn	30 Jun 2021	31 Dec 2020
Land and buildings and construction in progress	256	260
Office furniture and equipment	26	29
Total	**282**	**289**

(17) Other assets

€ mn	30 Jun 2021	31 Dec 2020
Properties	334	326
Contract assets	22	19
Miscellaneous	101	86
Total	**457**	**431**

(18) Financial liabilities (ac)

€ mn	30 Jun 2021	31 Dec 2020
Money market and capital market liabilities (ac)	**29,478**	**28,206**
Money market liabilities	8,788	8,717
Promissory note loans	3,742	4,077
Mortgage Pfandbriefe	11,180	9,755
Public-sector Pfandbriefe	1,883	1,971
Other debt securities	3,885	3,686
Other financial liabilities	0	0
Deposits from the housing industry (ac)	**10,957**	**10,592**
Payable on demand	8,788	8,426
Term deposits	2,169	2,166
Liabilities from other transactions (ac)	**105**	**86**
Trade payables	9	13
Other liabilities	96	73
Subordinated liabilities (ac)	**613**	**939**
Total	**41,153**	**39,823**

(19) Financial liabilities (fvpl)

€ mn	30 Jun 2021	31 Dec 2020
Negative market value of designated hedging derivatives (fvpl)	**1,049**	**1,298**
Negative market value of fair value hedges	1,048	1,298
Negative market value of net investment hedges	1	–
Negative market value of other derivatives (fvpl)	**704**	**608**
Negative market value of economic hedging derivatives	284	128
Negative market value of miscellaneous derivatives	420	480
Total	**1,753**	**1,906**

(20) Provisions

€ mn	30 Jun 2021	31 Dec 2020
Provisions for pensions and similar obligations	443	474
Provisions for unrecognised lending business	4	4
Other provisions and contingent liabilities	101	105
Total	**548**	**583**

Changes in the discount rate applicable to pensions 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. The discount rate was 1.15 % as at 30 June 2021 (31 December 2020: 0.74 %).

(21) Other liabilities

€ mn	30 Jun 2021	31 Dec 2020
Lease liabilities	81	82
Deferred income	1	1
Liabilities from other taxes	38	35
Contract liabilities	21	20
Miscellaneous	5	5
Total	**146**	**143**

(22) Equity

€ mn	30 Jun 2021	31 Dec 2020
Subscribed capital	180	180
Capital reserves	721	721
Retained earnings	1,899	1,902
AT1 bond	300	300
Other reserves		
Reserve from remeasurements of defined benefit plans	-142	-166
Reserve from the measurement of equity instruments (fvoci)	-3	-4
Reserve from the measurement of debt instruments (fvoci)	8	12
Reserve from foreign currency basis spreads	-28	-26
Currency translation reserves	-8	-13
Non-controlling interests	65	61
Total	**2,992**	**2,967**

The item "Reserve from the measurement of debt instruments (fvoci)" includes loss allowance of € 0 million (31 December 2020: € 0 million).

Treasury shares

No treasury shares were held during the period under review.

Distributions

Aareal Bank intends to pay a dividend in a total amount of € 1.50 per share in 2021 for the financial year 2020. This is subject to the relevant supervisory and regulatory requirements. The payout would need to be made in two steps.

In compliance with the requirements published by the European Central Bank (ECB) on 15 December 2020, the Annual General Meeting resolved on 18 May 2021 that the net retained profit of € 89,785,831.50 for the financial year 2020, as reported under the German Commercial Code (HGB), be used to distribute a dividend of € 0.40 per share (€ 23,942,888.40 in total) and to transfer the remaining amount

(€ 65,842,943.10) to profits carried forward. Following the announcement issued by the ECB on 23 July 2021, and depending on further economic developments, regulatory requirements, the Bank's capital position and its risk situation, in the absence of material adverse developments the Bank plans to convene an extraordinary Annual General Meeting, to be held during the fourth quarter of 2021, to decide on the intended remaining payout of € 1.10 per share, amending the resolution dated 18 May 2021 on the appropriation of profits.

In addition, on 30 April 2021, the Management Board resolved on a distribution in relation to the AT1 instruments, in accordance with the terms and conditions of the notes.

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

Notes to Financial Instruments

A detailed description of the system in place at Aareal Bank Group to measure, limit, and manage risks throughout Aareal Bank Group is presented in the Risk Report as part of the Interim Group Management Report. The disclosures on the description and the extent of the risks arising from financial instruments in accordance with IFRS 7 are included (in part) in the Risk Report.

(23) Determination of fair value

The determination of fair value is governed by IFRS 13 and applies to both financial instruments and non-financial assets or liabilities. In accordance with IFRS 13.9, the fair value is defined as the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction under current market conditions at the measurement date. 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. The principal market is the market with the greatest volume and the highest level of activity for the asset or liability to which Aareal Bank has access. The most advantageous market is the market that maximises the amount that would be received to sell the asset, or minimises the amount that would be paid to transfer the liability.

Fair value hierarchy

In accordance with IFRS 13.72 et seqq., the fair value determination is based on the fair value hierarchy pursuant to which the inputs used are classified into various hierarchy levels on the basis of their respective market proximity and objectivity. The fair value of assets and liabilities is allocated to Level 1 of the fair value hierarchy if it is determined on the basis of unadjusted qualifying prices in active markets for identical assets or liabilities. Fair values determined using inputs other than qualifying prices included within Level 1 that are observable for the financial instrument, either directly or indirectly, are included in Level 2 of the fair value hierarchy. 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. The estimation uncertainties as regards fair value measurement increase the higher the level is.

Measurement methods

The property and public-sector loans included in loan receivables are 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 the case of defaulted loans, future cash flows are reduced by the expected losses.

Debt securities and promissory note loans for which no current market price is available in an active market are measured through an analysis of future payments using the fully-capitalised earnings value approach, where the inputs are based on observable market data to the extent possible. 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 numerical procedures.

In the case of unquoted financial investments in equity instruments, the costs of acquisition may also be the best estimate of fair value. Their recoverability is reviewed regularly.

The fair value of OTC 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 of 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. Since the derivatives are part of highly effective collateral agreements (Credit Support Annex to the ISDA Master Agreement and Collateral Annex to the German Master Agreement on Financial Derivatives Transactions) which are each subject to a master collateralisation agreement, measurement adjustments to reflect any potential counterparty credit risk or own credit risk (CVA and DVA) are not required for reasons of materiality. The Bank uses the overnight interest rate swap curve (OIS curve) for the measurement of derivatives secured by cash collateral.

Amortised cost is an adequate estimate of fair value for cash funds, other loan receivables as well as short-term money market receivables and liabilities.

(24) Fair value hierarchy in accordance with IFRS 13

The carrying amounts of financial instruments held by Aareal Bank Group which are reported at fair value in the statement of financial position are presented in the following table according to the three-tier fair value hierarchy pursuant to IFRS 13.72 et seq. The presentation is made for each class of financial instrument:

30 June 2021

€ mn	Total fair value	Fair value level 1	Fair value level 2	Fair value level 3
Financial assets (fvoci)	**3,971**	**3,965**	**5**	**1**
Money market and capital market receivables	3,965	3,965	–	–
Equity instruments	6	–	5	1
Financial assets (fvpl)	**2,265**	**0**	**1,637**	**628**
Loan receivables	624	–	–	624
Money market and capital market receivables	93	0	89	4
Positive market value of designated hedging derivatives	1,097	–	1,097	–
Positive market value of other derivatives	451	–	451	–
Financial liabilities (fvpl)	**1,753**	**–**	**1,753**	**–**
Negative market value of designated hedging derivatives	1,049	–	1,049	–
Negative market value of other derivatives	704	–	704	–

31 December 2020

€ mn	Total fair value	Fair value level 1	Fair value level 2	Fair value level 3
Financial assets (fvoci)	**3,672**	**3,667**	**3**	**2**
Money market and capital market receivables	3,667	3,667	–	–
Equity instruments	5	–	3	2
Financial assets (fvpl)	**3,167**	**0**	**2,307**	**860**
Loan receivables	856	–	–	856
Money market and capital market receivables	93	0	89	4
Positive market value of designated hedging derivatives	1,431	–	1,431	–
Positive market value of other derivatives	787	–	787	–
Financial liabilities (fvpl)	**1,906**	**–**	**1,906**	**–**
Negative market value of designated hedging derivatives	1,298	–	1,298	–
Negative market value of other derivatives	608	–	608	–

In the first six months of the 2021 financial year, there were no transfers between the hierarchy levels for the various financial instruments.

The fair values of loan receivables recognised at fair value in the statement of financial position that are assigned to Level 3 of the fair value hierarchy developed as follows during the period under review:

Loan receivables (fvpl)

€ mn	2021	2020
Fair value as at 1 January	**856**	**1.050**
Change in measurement	**-4**	**-13**
Portfolio changes		
Additions	17	111
Derecognition	245	336
Deferred interest	0	0
Fair value as at 30 June	**624**	**812**

Financial instruments held in the Bank's portfolio contributed € -6 million to the net gain or loss from financial instruments (fvpl) (H1 2020: € -13 million).

Regarding loan receivables (fvpl), the add-ons for risks specific to the counterparty represent the material input parameter not observable in the market. Regarding the non-defaulted loans, an increase/decrease by 1 % would lead to a decrease/increase of the fair value by approximately € 15 million (H1 2020: approximately € 20 million).

(25) Comparison of carrying amounts and fair values of financial instruments

The fair values of financial instruments are compared with their carrying amounts (including loss allowance) in the following table. The presentation is made for each class of financial instrument:

€ mn	30 Jun 2021 Carrying amount	30 Jun 2021 Fair value	31 Dec 2020 Carrying amount	31 Dec 2020 Fair value
Financial assets (ac)	**39,065**	**39,273**	**37,407**	**37,655**
Cash funds	5,838	5,838	4,744	4,744
Loan receivables[1]	27,457	27,701	26,695	26,952
Money market and capital market receivables	5,701	5,665	5,879	5,869
Receivables from other transactions	69	69	89	90
Financial assets (fvoci)	**3,971**	**3,971**	**3,672**	**3,672**
Money market and capital market receivables	3,965	3,965	3,667	3,667
Equity instruments	6	6	5	5
Financial assets (fvpl)	**2,265**	**2,265**	**3,167**	**3,167**
Loan receivables	624	624	856	856
Money market and capital market receivables	93	93	93	93
Positive market value of designated hedging derivatives	1,097	1,097	1,431	1,431
Positive market value of other derivatives	451	451	787	787
Financial liabilities (ac)	**41,153**	**41,363**	**39,823**	**40,033**
Money market and capital market liabilities	29,478	29,647	28,206	28,371
Deposits from the housing industry	10,957	10,958	10,592	10,592
Liabilities from other transactions	105	104	86	86
Subordinated liabilities	613	654	939	984
Financial liabilities (fvpl)	**1,753**	**1,753**	**1,906**	**1,906**
Negative market value of designated hedging derivatives	1,049	1,049	1,298	1,298
Negative market value of other derivatives	704	704	608	608

[1] Including non-current assets held for sale

Segment Reporting

(26) Segment results

€ mn	Structured Property Financing		Banking & Digital Solutions		Aareon		Consolidation/ Reconciliation		Aareal Bank Group	
	1 Jan – 30 Jun 2021	1 Jan – 30 Jun 2020	1 Jan – 30 Jun 2021	1 Jan – 30 Jun 2020	1 Jan – 30 Jun 2021	1 Jan – 30 Jun 2020	1 Jan – 30 Jun 2021	1 Jan – 30 Jun 2020	1 Jan – 30 Jun 2021	1 Jan – 30 Jun 2020
Net interest income	260	226	22	20	-2	-1	0	0	280	245
Loss allowance	40	106			0	0			40	106
Net commission income	4	3	13	12	107	102	-6	-6	118	111
Net derecognition gain or loss	8	16							8	16
Net gain or loss from financial instruments (fvpl)	-4	-7		0		0			-4	-7
Net gain or loss from hedge accounting	-2	2							-2	2
Net gain or loss from investments accounted for using the equity method			-1		0	0			-1	0
Administrative expenses	134	117	36	35	104	92	-6	-6	268	238
Net other operating income/expenses	-20	-11	0	0	2	1	0	0	-18	-10
Operating profit	**72**	**6**	**-2**	**-3**	**3**	**10**	**0**	**0**	**73**	**13**
Income taxes	40	-5	-1	-1	1	3			40	-3
Consolidated net income	**32**	**11**	**-1**	**-2**	**2**	**7**	**0**	**0**	**33**	**16**
Consolidated net income attributable to non-controlling interests	0	0	0	0	2	1			2	1
Consolidated net income attributable to shareholders of Aareal Bank AG	32	11	-1	-2	0	6	0	0	31	15
Allocated equity[1]	1,686	1,809	258	194	38	42	533	466	2,515	2,511
RoE after taxes (%)[2] [3]	3.0	0.2	-1.1	-1.5	-0.2	27.7			1.9	0.5
Employees (average)	**787**	**779**	**382**	**377**	**1,837**	**1,718**			**3,006**	**2,874**
Segment assets	**34,277**	**34,213**	**11,907**	**10,740**	**460**	**369**			**46,644**	**45,322**

[1] For management purposes, the allocated equity is calculated for all segments from 2021 onwards on the basis of capital requirements pursuant to Basel IV (phase-in). Reported equity on the statement of financial position differs from this. Aareon's total equity as disclosed in the statement of financial position amounts to € 141 million.
[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.

Commission income from contracts with clients is allocated to the segments as follows:

	Structured Property Financing		Banking & Digital Solutions		Aareon		Consolidation/ Reconciliation		Aareal Bank Group	
	1 Jan– 30 Jun 2021	1 Jan– 30 Jun 2020	1 Jan– 30 Jun 2021	1 Jan– 30 Jun 2020	1 Jan– 30 Jun 2021	1 Jan– 30 Jun 2020	1 Jan– 30 Jun 2021	1 Jan– 30 Jun 2020	1 Jan– 30 Jun 2021	1 Jan– 30 Jun 2020
€ mn										
ERP products (incl. add-on products)					100	96	-9	-9	91	87
Digital solutions					33	30			33	30
Banking business and other activities	5	5	17	15					22	20
Total	**5**	**5**	**17**	**15**	**133**	**126**	**-9**	**-9**	**146**	**137**

Other Notes

(27) Contingent liabilities and loan commitments

€ mn	30 Jun 2021	31 Dec 2020
Contingent liabilities	189	163
Loan commitments	1,410	1,258
of which: irrevocable	1,033	896

(28) Employees

The number of Aareal Bank Group employees is shown below:

	30 Jun 2021[1]	Average 1 Jan - 30 Jun 2021[2]	31 Dec 2020[1]	Average 1 Jan - 31 Dec 2020[2]
Salaried employees	2,865	2,837	2,817	2,751
Executives	171	169	165	164
Total	**3,036**	**3,006**	**2,982**	**2,915**
of which: part-time employees	171	581	584	567

[1] This number does not include 133 employees of the hotel business (31 December 2020: 35 employees).
[2] This number does not include 60 employees of the hotel business (1 January to 31 December 2020: 52 employees).

(29) Related party disclosures in accordance with IAS 24

Together with Advent International, Aareal Bank set up a Management Equity Programme (MEP) for Aareon and, in line with its shareholding, contributed Aareon shares with a market value of € 6 million into a management equity company, in which individual members of Aareon's management were also able to acquire an interest at market value.

Other than that, there were no material transactions with related parties that would have to be reported here.

(30) Events after the interim reporting period

There were no material events after the end of the interim reporting period which would have to be reported here.

Executive Bodies of Aareal Bank AG

Supervisory Board

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

Richard Peters [1) 2) 3)]
Deputy Chairman of the Supervisory Board
President and Chairman of the Management Board of Versorgungsanstalt des Bundes und der Länder

Klaus Novatius [1) 2) 6)]
Deputy Chairman of the Supervisory Board
Aareal Bank AG

Jana Brendel [4) 5)]
Chief Information Officer of 1&1 Telecommunication SE

Christof von Dryander [1) 2) 3)]
Senior Counsel, Cleary Gottlieb Steen & Hamilton LLP

Thomas Hawel [5) 6)]
Aareon Deutschland GmbH

Petra Heinemann-Specht [3) 4) 6)]
Aareal Bank AG

Jan Lehmann [5) 6)]
Aareon Deutschland GmbH

Sylvia Seignette [4)]
Chairman of the Risk Committee
Former CEO for Germany and Austria, Crédit Agricole CIB

Elisabeth Stheeman [4) 5)]
External Member of the Financial Policy Committee and of the Financial Market Infrastructure Board, Bank of England

Hans-Dietrich Voigtländer [2) 3) 5)]
Chairman of the Technology and Innovation Committee
Associate Partner at BDG Innovation + Transformation GmbH & Co. KG

Prof. Dr Hermann Wagner [1) 3) 4)]
Chairman of the Audit Committee
German Chartered Accountant, tax consultant

Management Board

Hermann Josef Merkens
(until 30 April 2021)
Chairman of the Management Board

Marc Hess
Member of the Management Board

Dagmar Knopek
(until 31 May 2021)
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 Technology and Innovation Committee; 6) Elected by employees

Responsibility Statement

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

Wiesbaden, 5 August 2021

The Management Board

Marc Hess

Christiane Kunisch-Wolff

Thomas Ortmanns

Christof Winkelmann

Review Report

To Aareal Bank AG, Wiesbaden

We have reviewed the condensed consolidated interim financial statements for the period ended 30 June 2021 – comprising the statement of financial position, statement of comprehensive income, condensed statement of changes in equity, condensed statement of cash flows and selected explanatory notes – and the interim group management report of Aareal Bank AG, Wiesbaden, for the period from 1 January 2021 to 30 June 2021, which are part of the half-year financial report pursuant to section 115 of the German Securities Trading Act (Wertpapierhandelsgesetz – WpHG). The preparation of the condensed consolidated interim financial statements in accordance with International Accounting Standard IAS 34 Interim Financial Reporting, as adopted by the EU, and of the interim group management report in accordance with the Provisions of the German Securities Trading Act is the responsibility of the Company's Management Board. Our responsibility is to issue a review report on the condensed consolidated interim financial statements and on the interim group management report based on our review.

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

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

Frankfurt/Main, 6 August 2021

KPMG AG
Wirtschaftsprüfungsgesellschaft

Wiechens	Winner
Wirtschaftsprüfer	Wirtschaftsprüfer
[German Public Auditor]	[German Public Auditor]

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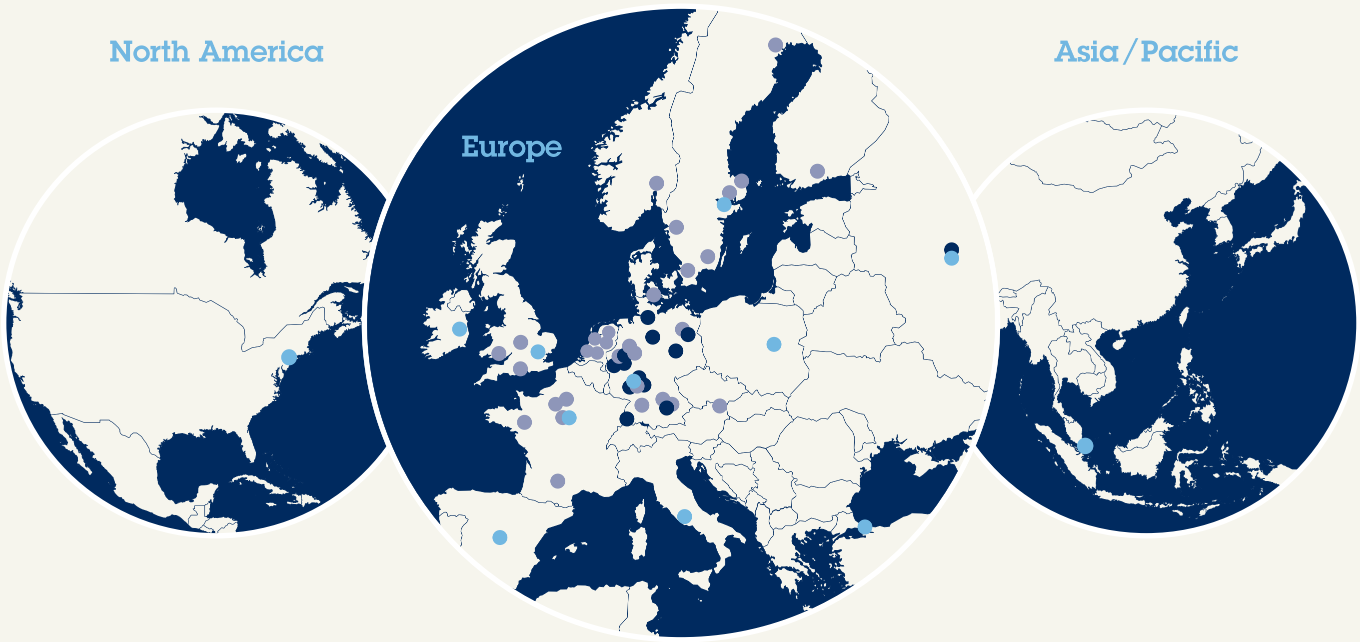
Financial Calendar

11 November 2021	Publication of results as at 30 September 2021
18 May 2022	Annual General Meeting

Locations/Imprint



● Structured Property Financing ● Banking & Digital Solutions ● Aareon

Aareal Bank, Real Estate Structured Finance: Dublin, Istanbul, London, Madrid, Moscow, New York, Paris, Rome, Singapore, Stockholm, Warsaw, Wiesbaden | **Aareal Estate AG:** Wiesbaden

Aareal Bank, Banking & Digital Solutions: Berlin, Essen, Wiesbaden | **Aareal First Financial Solutions AG:** Mainz | **Deutsche Bau- und Grundstücks-AG:** Berlin, Bonn, Düsseldorf, Frankfurt/Main, Freiburg, Hamburg, Hanover, Leipzig, Moscow, Munich | **plusForta GmbH:** Berlin, Düsseldorf

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Aareal Bank Group

08/2021

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