

Report of the Management Board to the Annual General Meeting regarding the authorisation to exclude of pre-emptive subscription rights proposed under agenda item No. 7 in accordance with section 71 (1) sentence 2 in conjunction with section 186 (4) sentence 5 of the AktG

The Management Board has submitted a written report regarding agenda item No. 7 in accordance with sections 71 (1) No. 8, 186 (4) sentence 2 of the AktG on the reasons for the proposed authorisation for the acquisition of treasury shares, subject to the partial restriction of the principle of equal treatment and any shareholders' disposal rights, and regarding the proposed authorisation for the sale of treasury shares other than via the stock exchange and in compliance with the principle of equal treatment and at the proposed issue price. This report is hereby disclosed as follows:

The purpose of the proposed authorisation is to enable the Company to acquire treasury shares in accordance with section 71 (1) No. 8 of the AktG, as was the case last year. As a rule, this would enable the Company to purchase treasury shares up to the equivalent of ten per cent (10%) of its registered share capital, up until and including 18 May 2015 (i.e. up to the maximum five years permitted by law), for purposes other than securities trading. With the proposed extension, the Company will be in a position to continue capitalising on the benefits of purchasing its own shares, in both its own interests and those of its shareholders, until said date. The number of shares the Company is permitted to own is restricted by law to ten per cent (10%) of its registered share capital, including the authorisation to purchase treasury shares for securities trading purposes, as proposed under agenda item No. 6 (section 71 (2) of the AktG). The acquisition may take place via the stock exchange or via a public offer to purchase at the prices stipulated in the authorisation and based on the prevailing market price. This provides a level playing field for all shareholders to sell shares to the Company, provided that the Company exercises its authorisation to purchase treasury shares. This approach safeguards shareholders' rights and preserves equality of treatment. Whenever a public offer is oversubscribed, acceptance must be effected on a pro-rata basis. The preferential

acceptance of a lower share quantity of up to 100 shares tendered per shareholder and commercial rounding may be provided for. This method is used to avoid fractional amounts when determining the individual purchase quotas and minor residual portions, thereby facilitating the technical handling.

Neither the offering price per share nor the threshold values of the purchase price range may exceed or fall below, by more than ten per cent (10%), the average closing price of the Company's shares in Xetra (or a comparable successor system) during the three trading days on the Frankfurt/Main stock exchange prior to the purchase, the assumption of an obligation to purchase or the public announcement of the purchase offer. The purchase offer may provide further conditions.

In addition to the purchase via the stock exchange or by means of a public offer to buy, directed at all shareholders, the authorisation also provides that the acquisition of treasury shares may be effected by using put or call options. This option, which is already part of the commercial practice of many DAX companies, would expand the Company's options of optimally structuring the acquisition of treasury shares. It may be advantageous for the Company to sell put options, to purchase call options or to sell Company shares using a combination of put and call options, instead of purchasing its treasury shares directly. The lifetime of the options must be selected in such a way as to ensure that the acquisition of shares by way of exercising options does not take place after 18 May 2015. This would ensure that the Company does not acquire treasury shares under section 71 (1) No. 8 of the AktG after this authorisation expires on said date. Moreover, the acquisition of treasury shares using equity derivatives is limited to 5 per cent (5%) of the Company's registered share capital existing at the time the relevant resolution is adopted by the Annual General Meeting.

The Company grants the purchaser of a put option the right to sell Company shares at a pre-determined price (exercise price) to the Company. In return, the Company receives an option premium which equates to the value of the disposal right granted by way of the put option, taking into consideration a variety of parameters, including exercise price and lifetime of the option and the volatility of the Company's share price. If and when the purchaser exercises the put option, the option premium paid by the purchaser reduces the

total price paid by the Company for the purchase of the shares. Exercising the put option would be financially advantageous to the purchaser only if the share price is below the exercise price at the time of exercise, as in this case the purchaser would be able to sell the shares at the higher exercise price. From the Company's perspective, the use of put options has the added advantage that the exercise price is determined as early as upon entering into the option transaction, while the outflow of liquidity will only take place on the exercise date. If the purchaser does not exercise the option because the share price exceeds the exercise price on the exercise date, the Company will not be able to purchase its treasury shares in this way, but would still retain the option premium collected.

Where the Company purchases a call option, it acquires the right to buy a predetermined number of treasury shares at a predetermined price (exercise price) from the option seller, for payment of an option premium. The exercise of the call option would be financially advantageous to the Company if the share price exceeds the exercise price, as in this case the Company would be able to buy the shares from the seller at the lower exercise price. By acquiring call options, the Company can, inter alia, limit price risks if the Company itself is obligated to transfer shares at a later time, in connection with conversion rights from convertible bonds for example.

The purchase price to be paid for the Company's shares is the exercise price agreed for the relevant option. The exercise price may exceed or fall below the stock exchange price of the Company's share on the day the option transaction is entered into, but must not exceed or fall below, by more than ten per cent (10%), the average closing price of the Company's share on Xetra (or a comparable successor system) during the three trading days on the Frankfurt/Main stock exchange prior to the relevant option transaction (in each case excluding ancillary costs but including the option premium paid or received). The option premium paid by the Company for call options must not significantly exceed, and the option premium collection for put options must not significantly fall below, the theoretical market price of the relevant options determined in accordance with recognised methods, mathematical valuation methods in particular; furthermore, the agreed exercise price must also be taken into consideration in the determination of said market price.

The way that the proposed authorisation is set out would preclude financial prejudice to shareholders if the Company repurchases treasury shares using equity derivatives. By determining exercise price and option premium as described above, and the mandatory requirement that options are only served by using shares of the Company that were purchased on the stock exchange, in accordance with the principle of equal treatment, at the prevailing share price at the time of the purchase on the stock exchange, it is ensured that the Company will receive or pay a fair market price and that the Company's shareholders who do not participate in these option transactions will not suffer financial prejudice. This is in keeping with the position of shareholders when treasury shares are repurchased via the stock exchange but not all of the Company's shareholders can in fact sell shares to the Company. The requirements for the structuring of the options as well as the requirements for the shares to be used for servicing the option rights ensure that the principle of equal treatment of all shareholders is accommodated to the fullest extent. Against this background, and given the legal notion underlying section 186 (3) sentence 4 of the AktG, it is reasonable that shareholders should not be entitled to enter into any such transactions with the Company. Likewise, shareholders have no right to enter into option transactions with the Company to the extent that any such transactions provide for a preferential offer related to smaller quantities of shares. By excluding the subscription and disposal right, the Company is put in a position where it can enter into option transactions as they arise. The Company would not have this opportunity to the same extent if the offer to purchase or sell options was extended to all shareholders.

Shareholders of the Company should only have a right to tender their shares to the Company, using equity derivatives, to the extent that the Company is under a specific obligation vis-à-vis these shareholders to accept their shares in connection with option transactions. Otherwise, equity derivatives could not be used for the repurchase of treasury shares, depriving the Company of the potential advantages associated therewith.

After careful consideration of the interests of the shareholders on the one hand and the interests of the Company on the other hand, the Management Board considers the non-granting or the restriction of disposal rights justified, given the advantages that

arise for the Company as a result of the use of equity derivatives when repurchasing treasury shares.

The treasury shares acquired under the authorisation proposed under agenda item No. 7 or under an earlier authorisation may be used as follows:

The shares acquired may either be called in, resulting in a reduction of registered share capital, or sold by public offer or via the stock exchange. These alternatives ensure that the shareholders' right to equal treatment will be observed upon disposal.

Agenda item No. 7 contains an additional proposal to authorise the Management Board to effect the sale of any treasury shares acquired in accordance with the authorisation pursuant to section 71 (1) No. 8 of the AktG, subject to the Supervisory Board's approval, via channels other than a sale via the stock exchange, or an offer to all shareholders (excluding shareholders' subscription rights pursuant to section 186 (3) sentence 4 of the AktG), provided that the sale is carried out at a cash price that is not significantly lower than the relevant stock exchange price of the Company's shares at the time of sale. In such cases, the management will minimise any discounts from the issue price in relation to the market price and is expected to limit any such discounts to a maximum not exceeding five per cent (5%). Any dilution of the value of shareholders' holdings will be avoided through the close link to the prevailing market price. The selling price of the treasury shares will be finalised immediately prior to use.

The total number of shares sold in this manner must not exceed ten per cent (10%) of the registered share capital, neither at the time the proposed authorisation comes into effect nor at the time of its utilisation. This threshold also includes any shares that were issued or sold during the term and prior to the exercising of this authorisation, in direct or analogous application of section 186 (3) sentence 4 of the AktG, and by virtue of other authorisations granted to the Management Board for the issue or sale of shares, or on the basis of resolutions passed by a General Meeting. Said ten-per-cent threshold shall also include shares the issuance of which is required under the terms of debt securities with embedded conversion or option rights on shares issued pursuant to section 186 (3) sentence 4 of the AktG (excluding shareholders' subscription rights), which are issued during the validity of the pro-

posed authorisation. This ensures that no treasury shares are sold (excluding shareholders' sub-subscription rights) in accordance with section 186 (3) sentence 4 of the AktG where this could result in shareholders' subscription rights being excluded for a total of more than ten per cent (10%) of the registered share capital in direct or analogous application of section 186 (3) sentence 4 of the AktG for no specific justifiable reason. This further limitation is in the interest of shareholders who wish to maintain their stake to the greatest extent possible.

The proposed authorisation therefore ensures that shareholders' financial and voting interests are appropriately taken into account when selling shares to the exclusion of subscription rights, whilst extending the Company's flexibility in the interest of all shareholders. The legal concepts embodied in section 186 (3) sentence 4 of the AktG have thus been properly considered and complied with. Amongst other things, this will provide the Company with an opportunity to offer shares to institutional investors or domestic and international investors and to expand its shareholder base, thereby stabilising the value of the shares. The Company will therefore have flexibility in adjusting its equity to commercial requirements and responding to favourable opportunities on the stock exchange. Moreover, shareholders have the option of maintaining the level of their shareholding in the Company by purchasing shares on the stock exchange.

In addition, the subscription rights of shareholders may also be excluded when selling shares for contributions in kind. This reflects the purpose of the authorisation included in the proposed resolution to maintain the Company's ability to act in the most flexible and cost-efficient manner when acquiring entities or agreeing on business combinations. Where appropriate, the Company may decide to offer its own shares as consideration for the acquisition of enterprises or participating interests (excluding shareholders' preemptive subscription rights if and when appropriate). Such share deals have become increasingly popular worldwide. The price at which the treasury shares will be issued in this case depends on the individual circumstances and the timing. With regard to price determination, the Management and Supervisory Boards will be guided by the Company's interests. The Management Board will use the stock exchange price of the Company's shares as a guideline when determining the value of the shares granted by way of con-

sideration; there are no plans to apply any fixed formula relating to the quoted market price, particularly to avoid the results of negotiations being called into question by fluctuations in the quoted market price.

It is also proposed that the Company continue to be authorised to use any treasury shares it has acquired to satisfy the rights of holders of convertible bonds and/or bonds cum warrants. This may result in a reduction of any capital increase from conditional capital, if required. The use of existing treasury shares instead of a capital increase or cash payment may be financially advantageous; the authorisation is intended to increase flexibility in this regard. At present, no option or conversion rights or conversion obligations exist that would be eligible for servicing through treasury shares under the proposed authorisation.

Furthermore, the Company shall have the ability to partially exclude shareholders' subscription rights upon the disposal of shares via an offer to all shareholders in favour of the holders of conversion or option rights. In this way, subscription rights to shares could also be granted to these holders that would entitle said holders to the same extent as they would have been entitled upon exercising their conversion or option rights or upon performance of a conversion obligation. This would enable the Company to avoid a reduction in the option or conversion price, which would be the consequence of issuing treasury shares without granting subscription rights to the holders of options and conversion rights in accordance with the terms and conditions governing the convertible bonds and bonds cum warrants.

Furthermore, the Management Board should be authorised, subject to the Supervisory Board's approval, to exclude shareholders' subscription rights for fractional amounts upon the disposal of treasury shares via an offer to all shareholders. The purpose of this authorisation is to create subscription ratios that result in as few fractional shares as possible in order to facilitate the technical settlement of issuing shares. As freely marketable fractions, the shares excluded from the shareholders' pre-emptive rights will either be sold at the stock exchange or otherwise disposed of on a "best efforts" basis. The Management Board will endeavour to keep the amount of freely marketable fractions as small as possible. Through the limitation to such fractional amounts, shareholders do not suffer any material dilution of their shareholdings. The

shareholders' financial interests will be safeguarded by the obligation to ensure best possible realisation.

As long as the Bank avails itself of a recapitalisation measure under section 7 of the German Financial Markets Stabilisation Fund Act (Finanzmarktstabilisierungsfondsgesetz – "FMStFG"), the Management Board will only utilise these authorisations after consultation with the German Financial Markets Stabilisation Fund.

The option of purchasing and using treasury shares by direct or indirect subsidiaries of the Company, or by third parties for account of the Company or its direct or indirect subsidiaries, provides the Company with additional flexibility in the utilisation of its treasury shares.

The Management Board will only make use of this authorisation if the exclusion of subscription rights in individual instances is in the best interest of the Company and its shareholders. Similarly, the Supervisory Board will only grant the necessary approval if these requirements have been met.

Whenever the Management Board utilises one of the above-mentioned authorisations, it will report on this at the next General Meeting as well as in the annual report.

The report of the Management Board regarding agenda item No. 7 on the reasons for the authorisations provided thereunder for the exclusion of shareholders' subscription rights will be available for shareholders at the Company's offices (Paulinenstrasse 15, 65189 Wiesbaden) from the day on which the Annual General Meeting is called. The report will also be available at the Annual General Meeting itself. Upon request, said report will be sent to every shareholder, without delay, free of charge. The report is also available on the internet on <http://www.aareal-bank.com>