

## Report of the Supervisory Board of Aareal Bank AG, Wiesbaden

Dear shareholders,

During the financial year 2013, Aareal Bank AG once again performed successfully, mastering the challenges presented by the demanding market environment. Aareal Bank achieved consolidated operating profit which exceeded both the results posted in 2011 and the previous year's figures.

The Supervisory Board considers Aareal Bank AG's consistently positive results as evidence for the viability and operative strength of the Group's business model.

During the financial year under review, the Supervisory Board continually advised, monitored, and supervised the management of the Company. The Management Board informed the Supervisory Board regularly, without delay and comprehensively, both orally and in writing, of all the issues important to the Bank. The Management Board reported on the Group's situation, business development, key financial indicators and market developments. In addition, detailed reports and explanations were given to the Supervisory Board regarding the current liquidity status and liquidity management measures taken, the prevailing risk situation, and on risk control and risk management measures taken within the Group. The Supervisory Board also received comprehensive reports on the development of business segments, and on operative and strategic planning. The Supervisory Board was informed about, and involved in, all important decisions. All material events were discussed and examined in detail; where a Supervisory Board

resolution was required, the decision proposals were submitted to the Supervisory Board and a decision taken. In cases where resolutions needed to be passed in between scheduled Supervisory Board meetings, such resolutions were passed by way of circulation or via conference calls.

Furthermore, between the meetings of the Supervisory Board, the Chairman of the Management Board kept the Chairman of the Supervisory Board – until 22 May 2013, Mr Hans Reich, and from 22 May 2013 onwards, Ms Marija G. Korsch – informed, on a continuous and regular basis, both orally and in writing, on all material developments of the Company. The Chairman of the Management Board maintained close contact with the Chairmen of the Supervisory Board, in order to discuss key issues and important decisions personally.

## Activities of the plenary meeting of the Supervisory Board

Six plenary meetings of the Supervisory Board were held during the year under review, of which five were scheduled meetings. During the meetings, the members of the Supervisory Board received reports and explanations by the members of the Management Board, and discussed these in detail. Proceedings and reports during all scheduled meetings focused on the way the Bank dealt with the challenges posed by the European sovereign debt crisis, and the resulting effects upon Aareal Bank AG.

In its discussions, the Supervisory Board also concerned itself with changes to the regulatory framework, in great detail. During the year under review, this included the decisions to establish a uniform European Banking Authority under the auspices of the European Central Bank and the regulations implementing the Basel III framework (the Capital Requirements Regulation (CRR) and the Capital Requirements Directive (CRD IV)).

Throughout the financial year, in the course of all meetings as well as during the periods between meetings, the Management Board informed the Supervisory Board about economic and market developments and their potential impact on Aareal Bank Group, in a timely, complete and comprehensible manner. This included detailed explanations of the appropriate measures taken in response to the challenges arising from the European sovereign debt crisis, and from other market developments.

During the scheduled plenary meetings of the Supervisory Board, the Management Board reported to the Supervisory Board regularly and comprehensively; these reports also covered the development of the Structured Property Financing and Consulting/Services segments, focusing on current economic developments. Within regular intervals, the Supervisory Board was informed of the Bank's liquidity status and the related steps taken by the Bank's Treasury. In addition, the Supervisory Board was informed about the business development of the entire Aareal Bank Group, on the basis of

actual figures and projections. The Management Board also reported regularly on the quality of the property financing portfolio, against the background of general market trends and expected changes on the various property markets. The focal points of the various Supervisory Board meetings are presented below:

One meeting in March focused exclusively on Aareal Bank's strategic options, and on the challenges presented in the prevailing market environment.

During the extraordinary meeting in March, the Chairman of the Supervisory Board declared that he would resign from his chairmanship and from membership of the Supervisory Board, with effect from the end of the Annual General Meeting on 22 May 2013. During the same meeting, the Supervisory Board accepted the proposal to elect Ms Marija G. Korsch as the Chairman of the Supervisory Board, succeeding Mr Reich.

During an additional, scheduled meeting in March, the Supervisory Board concerned itself in detail with the financial statements and consolidated financial statements presented for the 2012 financial year, and with the auditors' report. The relevant facts were presented in the Supervisory Board report for the previous year. In addition, the proposal regarding the selection and subsequent appointment of the external auditor for the Annual General Meeting was discussed. This also included the scope and focal points of the audit for the 2013 financial year, as defined by the Supervisory Board. Other issues covered in the meeting in March included the preparations for the Annual General Meeting in May 2013. This meeting also discussed the annual reports submitted by Internal Audit and by the Compliance Officer. Furthermore, the proposals submitted by the Nomination Committee to fill the vacancy as a result of Mr Reich's retirement were discussed, and the Supervisory Board decided to propose Mr Richard Peters as a candidate for election to the Supervisory Board to the Annual General Meeting.

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The purpose of the May meeting of the Supervisory Board was to follow up on the Annual General Meeting of Aareal Bank AG, which preceded the meeting.

During the September meeting, corporate governance issues were presented and discussed, alongside other regulatory issues.

In the December meeting, the Management Board reported on the Group's corporate planning. The Management Board submitted and explained the corporate planning in detail to the Supervisory Board. The meeting also discussed corporate governance issues, as well as the requirements of the amendments to the German Banking Act concerning the structure of the Supervisory Board committees. The requisite resolutions were passed and implemented. Furthermore, the Supervisory Board adopted the regular Declaration of Compliance, pursuant to section 161 of the German Public Limited Companies Act (AktG), which was subsequently published on the Bank's website. Moreover, the Supervisory Board concerned itself with the latest amendments to the German Ordinance on Remuneration in Financial Institutions (InstVergV). With the support of external advisors, the Supervisory Board discussed individual items where action was required with respect to the remuneration concept, in the context of the corresponding governance structure, and adopted proposed resolutions where possible. The Supervisory Board duly noted a related implementation schedule, taking coordination with the Works Council and the Executive Staff Representative Committee into account.

In accordance with good corporate governance practice, the Supervisory Board also regularly examines the efficiency of its activities in order to identify any areas requiring improvement. The results of the efficiency examination conducted during the 2013 financial year were acknowledged by the members of the Supervisory Board, and were discussed in detail. No concrete need for action was identified.

Strategy documents were regularly submitted to, and discussed by the Supervisory Board, in accordance with the Minimum Requirements for Risk Management in Banks (MaRisk). In this context, the Supervisory Board received a report on the status and implementation of the latest amendments to the MaRisk. The results of the regular review of the Company's remuneration system were reported to the Supervisory Board. The Supervisory Board determined that the Company's remuneration system is appropriate.

The Chairmen of Supervisory Board committees regularly gave account of the work in the committees to the plenary meeting, answering all related questions submitted by the plenary meeting in detail.

Any Supervisory Board decisions which were taken by way of circulation were discussed at the subsequent meeting, to ensure that the members were able to reconcile the implementation of such decisions.

As part of preparing Supervisory Board decisions, a routine examination is carried out as to whether there are any conflicts of interest. No potential conflicts of interest that would need to be considered in the context of decision-making processes were identified during the financial year under review. The members of the Supervisory Board have declared in writing that no conflicts of interest pursuant to section 5.5.2 of the Corporate Governance Code arose during the financial year under review.

In addition to its regular meetings, the Supervisory Board convened for a separate meeting during which auditors PricewaterhouseCoopers provided information on current changes and deliberations in the regulatory and legal framework. This meeting provided the opportunity for a more detailed analysis and discussion of key topics, outside the regular work of the Supervisory Board.

## Activities of Supervisory Board committees

The Supervisory Board has established five committees in order to perform its supervisory duties in an efficient manner: the Executive Committee, the Risk Committee, the Committee for Urgent Decisions, the Accounts and Audit Committee, and the Nomination Committee. Explanations concerning the new structure of Supervisory Board committees in accordance with section 25d of the KWG are provided in the Corporate Governance Statement.

The Executive Committee of the Supervisory Board convened for three scheduled meetings and three extraordinary meetings. In the scheduled meetings, the Executive Committee prepared the proposed resolutions of the plenary meetings of the Supervisory Board. Strategic options of Aareal Bank were discussed during the extraordinary meetings; this included the acquisition of all shares in Corealcredit Bank AG, which was agreed upon on 22 December 2013.

The Risk Committee held four meetings during the year under review. The Management Board submitted detailed reports to the committee, covering all markets in which the Bank is active in the property finance business, as well as supplementary reports regarding the Bank's investments in securities portfolios. The committee members discussed these reports and market views in detail. The committee discussed the banking environment and the situation of the Bank's competitors. The committee also regularly dealt with loans requiring approval and transactions subject to reporting requirements. The committee discussed individual exposures of material importance to the Bank, which were presented and explained by the Management Board. Also, detailed reports were given regarding the Bank's liquidity status and funding.

The committee regularly discussed reports on the Bank's risk situation, which were submitted and explained by the Management Board. Having discussed the contents with the Management Board, these were duly noted and approved by

the members of the committee. Besides credit and country risks, the committee concerned itself with market risks, liquidity risks, and operational risks. The committee discussed in detail the developments of the debt crisis and their implications for the business environment of Aareal Bank, the consideration of Aareal Bank's risk-bearing capacity and the detailed account of its capital ratios, as well as the implementation of the requirements in accordance with Basel III. The committee also decided on any other transactions requiring the Supervisory Board's approval pursuant to the Company's Memorandum and Articles of Association or the internal rules of procedure.

The Committee for Urgent Decisions is a sub-committee of the Risk Committee. It approves loans subject to approval requirements by way of circulation; for this reason, it did not hold any meetings. Any decisions which were taken between meetings of the Risk Committee were discussed at the subsequent meeting.

The Accounts and Audit Committee held six meetings during the year under review. During its meeting in February 2013, the Accounts and Audit Committee received and discussed the preliminary results for the 2012 financial year. During its March meeting, the committee received the external auditors' report on the 2012 financial year and discussed the results with the auditors in detail. The committee members read the audit reports provided; they formed their own judgement of the audit results on the basis of these reports, and by way of extensive discussions with the external auditors. In accordance with its duties under the Memorandum and Articles of Association, the Accounts and Audit Committee also discussed the selection of external auditors and the focal aspects of the audit for 2013 during the same meeting.

Proceedings at the meetings in August and November included information given to the committee on supplementary topics, such as measures to implement changed regulatory requirements. In addition to a report on the audit progress, the Management Board presented and explained

the updated Group planning to the committee during its December meeting. The committee also received reports submitted by Internal Audit and by the Compliance Officer, requesting and receiving detailed explanations. It discussed and duly noted the review of the internal control system, which was carried out in accordance with applicable law.

Furthermore, during the committee meetings in February, May, August and November 2013, the Management Board presented the quarterly results for the financial year, as well as the preliminary full-year results for 2012 prior to publication, in accordance with the German Corporate Governance Code; the committee members discussed the reports with the Management Board. As in the financial year under review, the preliminary results for 2013 were discussed at a meeting in February 2014.

In its meeting on 19 March 2014, the Audit Committee received the external auditors' detailed report on the audit and audit results for the 2013 financial year, and discussed these results extensively with the auditors and the Management Board.

The Nomination Committee convened once in 2013. The task of the committee is to coordinate and carry out the search for new shareholder representatives on the Supervisory Board, if a member representing shareholders retires from the Supervisory Board. Hans W. Reich resigned from his office with effect from 22 May 2013 during the financial year under review.

Where members of the Supervisory Board were unable to attend a meeting, they had announced their absence in advance, giving reasons. If material decisions were on the agenda, these Supervisory Board members submitted written instructions for the casting of their votes, or cast their votes afterwards, in writing. Attendance of Supervisory Board members at meetings is shown in the table below.

<b>Member of the Supervisory Board</b>	<b>Number of meetings attended / number of meetings (plenary and committee meetings)</b>
Hans W. Reich **	9 of 9
Marija G. Korsch	16 of 17
Erwin Flieger	17 of 17
York-Detlef Bülow *	17 of 18
Christian Graf von Bassewitz	15 of 16
Manfred Behrens	4 of 6
Thomas Hawel *	5 of 6
Dieter Kirsch *	10 of 10
Dr Herbert Lohneiß	10 of 10
Joachim Neupel	16 of 16
Richard Peters **	3 of 3
Prof Dr Stephan Schüller	17 of 18
Helmut Wagner *	6 of 6

\* employee representative

\*\* member of the Supervisory Board for only part of the financial year

## **Financial statements and consolidated financial statements**

The Supervisory Board instructed PricewaterhouseCoopers Aktiengesellschaft Wirtschaftsprüfungsgesellschaft, Frankfurt/Main, who were elected as auditors by the Annual General Meeting 2013, with the audit of the financial statements. The external auditors appointed submitted a statement regarding their independence to the Supervisory Board, who duly noted it. The Supervisory Board has no reason to doubt the accuracy of this statement of independence. Fulfilling their duties as commissioned by the Supervisory Board, PricewaterhouseCoopers Aktiengesellschaft Wirtschaftsprüfungsgesellschaft audited the financial statements prepared in accordance with the German Commercial Code (HGB) and the consolidated financial statements prepared in accordance with IFRSs, as well as the Management Report and the Group Management Report. Based on the results of their audit, PricewaterhouseCoopers Aktiengesellschaft Wirtschaftsprüfungsgesellschaft issued an unqualified audit opinion for the financial statements and consolidated financial statements.

All members of the Supervisory Board received the audit reports regarding the financial statements and the consolidated financial statements, including all annexes thereto, in good time before the meeting during which the audit results were discussed. Having examined the documents provided, the Supervisory Board members formed their own judgement of audit results. The representatives of the external auditor participated in the meeting of the Supervisory Board, during which the financial statements were discussed, and gave a detailed account of the results of their audit. The representatives of PricewaterhouseCoopers Aktiengesellschaft Wirtschaftsprüfungsgesellschaft were available to the Supervisory Board to answer further questions, and to provide additional information. All questions were answered to the full satisfaction of the Supervisory Board.

The financial statements and management report of Aareal Bank AG, prepared in accordance with the HGB; and the consolidated financial statements and the Group Management Report prepared in accordance with IFRS and the proposal of the Management Board regarding the appropriation of profit and the audit report were examined in detail. No objections were raised to the audit results. In its meeting on 26 March 2014, the Supervisory Board approved the results of the audit. The Supervisory Board approved the financial statements and Management Report of Aareal Bank AG, prepared in accordance with the HGB, together with the consolidated financial statements and the Group Management Report prepared in accordance with IFRSs, and thus confirmed the financial statements of Aareal Bank AG. The Supervisory Board examined and discussed with the Management Board its proposal regarding the appropriation of profit. On the basis of the discussion, the Supervisory Board endorsed the proposal for the appropriation of profit submitted by the Management Board.

## Personnel matters

Hans W. Reich retired from his office as Chairman and as a member of the Supervisory Board, with effect from the end of the Annual General Meeting of Aareal Bank AG on 22 May 2013. Hans W. Reich's tenure was shaped by a number of key challenges for Aareal Bank, which the Bank mastered during his chairmanship of the Supervisory Board. The Supervisory Board regrets that the Bank has lost a renowned expert in international banking, and would like to sincerely thank Mr Reich for his long-standing and successful service on the Bank's Supervisory Board.

At the same time, the Supervisory Board welcomes new member Richard Peters and looks forward to a fruitful and successful cooperation. Mr Peters is President and Chairman of the Management Board of Versorgungsanstalt des Bundes und der Länder ("VBL"). He has been a member of VBL's Management Board since 1998, first with responsibility for VBL's investments and subsequently for VBL's insurance business and benefits. The Supervisory Board is delighted to have won a capital markets expert and wishes Mr Peters every success for his mandate.

Mr Dirk Große Wördemann resigned from Aareal Bank at his own request, with effect from 31 May 2013, in order to focus more on real estate investments, as he had done prior to joining Aareal Bank. He will continue to work for the Bank, as an advisor. Mr Große Wördemann had been a member of Aareal Bank's Management Board since November 2010. The Supervisory Board thanks Mr Große Wördemann for his contributions to the Bank.

The Bank's Supervisory Board appointed Ms Dagmar Knopek as a member of the Management Board with effect from 1 June 2013. The Supervisory Board is delighted that it was able to appoint Ms Knopek, who has been working for Aareal Bank for many years and commands extensive experience in the international commercial property finance business. The Supervisory Board wishes Ms Knopek every success in her new area of responsibility.

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In conclusion, the Supervisory Board would like to thank the Management Board and all of the Group's employees for their strong commitment during the 2013 financial year, which was once again eventful. The commitment and strong motivation of all employees of Aareal Bank Group made the Company's success possible, and thus enabled the Bank to successfully master the challenges of recent months.

### **Special transactions**

During the year under review, Aareal Bank Group acquired all of the shares of Corealcredit Bank AG, Frankfurt/Main, which specialises in commercial property financing in Germany. A corresponding agreement was concluded on 22 December 2013 with the previous owner, a company of US financial investor Lone Star. The Supervisory Board has been involved in the entire process and was always comprehensively kept informed by the Management Board. The Supervisory Board has approved the transaction; with the acquisition, Aareal Bank AG further expands its position in commercial property finance.

**Frankfurt, March 2014**

**For the Supervisory Board**



**Marija G. Korsch (Chairman)**