Volksbanken Raiffeisenbanken
cooperative financial network

ANNUAL REPORT 2018

dzhyp.de

DZ HYP

OVERVIEW

€ mn	2018	2017*)	DG HYP
DEVELOPMENT OF NEW BUSINESS			
Commercial Real Estate Investors	7,725	7,105	6,431
Retail Customers/Private Investors	2,232	2,049	
Housing Sector	1,013	975	
Public Sector	894	765	198
PORTFOLIO DEVELOPMENT	31 Dec 2018	1 Jan 2018	31 Dec 2017
Total assets	75,891	75,156	36,826
Mortgage loans	45,289	42,510	20,505
Originated loans to local authorities	11,789	12,479	5,530
Local authority lending**)	12,608	12,992	5,604
Bank bonds	571	723	723
Mortgage-backed securities (MBS)	542	745	745
Pfandbriefe and other debt securities	49,995	50,340	17,900
Own funds	2,276	n/a	1,743
Total capital ratio (%)	13.3	n/a	14.4
Common equity tier 1 ratio (%)	9.0	n/a	8.4
PROFIT AND LOSS ACCOUNT	1 Jan to 31 Dec 2018	1 Jan to 31 Dec 2017*	1 Jan to 31 Dec 2017
Net interest income	524	481	276
Net commission result	-27	-15	34
Administrative expenses	294	228	129
Net other operating income/expenses	8	-3	-4
Risk provisioning	-69	-23	-6
Net financial result	38	69	2
Operating profit	180	281	173
Allocation to the fund for general banking risks	45	100	40
Partial profit transfer	16	16	16
Taxes	64	90	67
Profit transfer	55	75	50
Cost/income ratio (%)	60.0	51.8	45.8
Return on equity (%)	11.5	15.1	16.2
NUMBER OF EMPLOYEES	31 Dec 2018	1 Jan 2018	31 Dec 2017
Annual average	873	852	480

*) Aggregate figures of the individual institutions
**) Lending transactions with national governments and sub-sovereign entities as well as state-guaranteed corporate bonds.

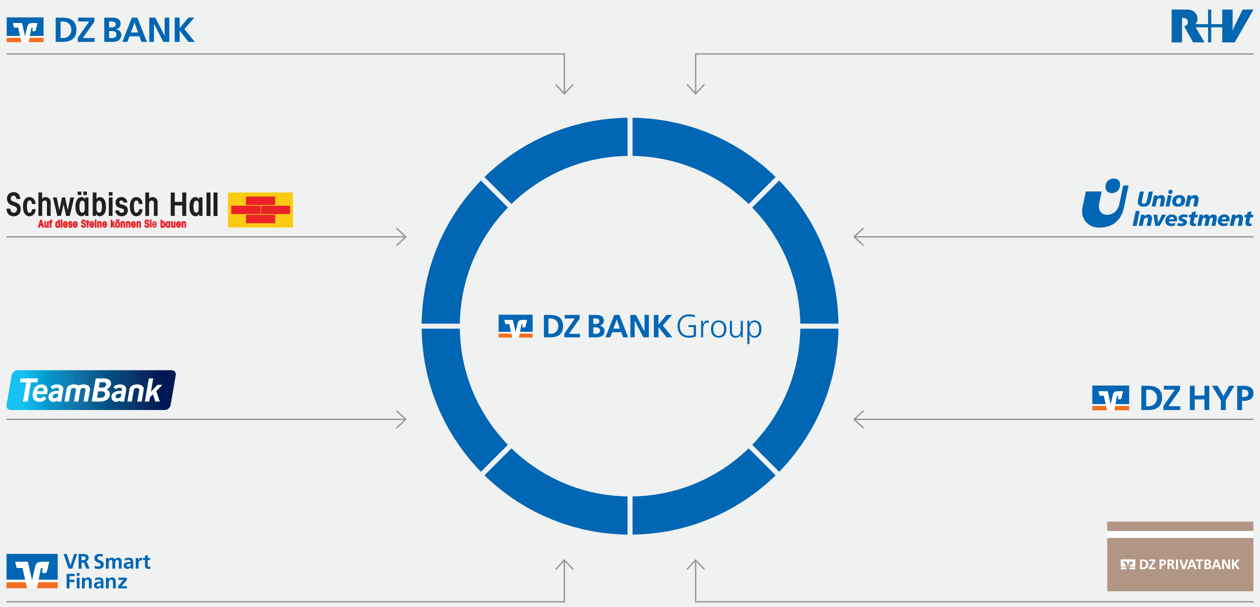
Genossenschaftliche FinanzGruppe
Volksbanken Raiffeisenbanken

ANNUAL REPORT 2018

dzhyp.de

DZ HYP

DZ HYP – PART OF A STRONG GROUP



DZ HYP is part of the DZ BANK Group and therefore part of the German Cooperative Financial Network, which comprises approximately 875 individual cooperative banks. In terms of total assets, it ranks among the largest financial services organisations in Germany. Within the Cooperative Financial Network, DZ BANK AG acts as the central institution, tasked with supporting the local cooperative banks' transactions as well as strengthening their competitive position. It operates as a commercial bank, and exercises the holding entity function for the DZ BANK Group.

The DZ BANK Group includes Bausparkasse Schwäbisch Hall, DZ HYP, DZ PRIVATBANK, R+V Insurance, Team-Bank, Union Investment Group, VR Smart Finanz, and various other specialist financial services providers. The various DZ BANK Group entities and its strong brands are the cornerstones of a comprehensive range of financial services offered to (and through) the Cooperative Financial Network. The DZ BANK Group has organised its strategy and range of services for the cooperative banks and their customers along the lines of four business segments: Retail Banking, Corporate Banking, Capital Markets and Transaction Banking.

Combining banking services with insurance products, home loan savings and a range of investment services has a long tradition within the German cooperative banking sector. The specialist institutions within the DZ BANK Group each offer highly competitive and appropriately-priced products in their respective area of expertise. This allows Germany's cooperative banks to offer their customers an end-to-end range of first-class financial services.

CONTENTS

4 Letter from the Management Board

6 Report of the Supervisory Board

12 DZ HYP
12 Partner for real estate financing and public-sector lending in the German cooperative financial network
14 Digitalisation
15 Sustainability

20 Management Report
20 Business Model
26 Economic Report
26 Economic Environment
28 Development of the Real Estate Markets
34 Business Development
34 Credit Business
36 Refinancing
40 Net Assets, Financial Position and Financial Performance
40 Net Assets
42 Financial Position
43 Financial Performance
50 Report on Opportunities, Risks and Expected Developments
50 Report on Opportunities
51 Risk Report
69 Report on Expected Developments
74 Employees

77 Financial Statements
78 Balance Sheet
80 Profit and Loss Account
81 Statement of Changes in Equity
82 Cash Flow Statement
83 Notes to the Financial Statements
83 General Notes
89 Notes to the Balance Sheet
100 Notes to the Profit and Loss Account
101 Coverage
108 Other Information on the Annual Financial Statements

111 Responsibility Statement

112 Independent Auditor's Report

118 Service
118 Corporate Bodies and Committees, Executives
123 DZ HYP Addresses

LETTER FROM THE MANAGEMENT BOARD

The Management Board of DZ HYP
From left to right: Manfred Salber, Dr Georg Reutter (CEO), Dr Carsten Düerkop

Ladies and Gentlemen, dear business associates,

2018 was both an eventful and challenging year for DZ HYP. Summer saw us successfully conclude the merger between DG HYP and WL BANK. At the same time, we continued to focus very intensely on our business. The higher volume of new business in real estate financing and local authority lending – compared with the previous year – shows that we have been able to play to our strength of broad diversification with four business segments. This confirms that we have taken the right step by merging. We are particularly pleased to have maintained a high level of close partner-like cooperation with the Volksbanken Raiffeisenbanken cooperative bank network in our new structure as DZ HYP. Being one of the leading players in real estate financing on the German market also enabled us to further strengthen the positioning of the Cooperative Financial Network overall.

The performance of capital markets was shaped by increased volatility in the year under review. This was primarily driven by the phase-out of the European Central Bank's bond-buying programme, uncertainty surrounding the United Kingdom's withdrawal (Brexit) from the European Union (EU), and growing trade conflicts between major economies accompanied by the introduction of punitive tariffs. Capital markets activity in 2019 is also likely to be influenced by the political events mentioned. Another issue will be the extent to which Italy is able and prepared to cut its budget deficit. If government debt (already high) rises further, the country may quickly become a serious burdening factor for the entire euro area. In the year under review, Italy recorded a second consecutive slowdown in economic growth, following four years of continuous upturn. Concerns about a potentially uncontrolled Brexit, new EU emission regulations and simmering international trade conflicts have curbed the growth of most of the economies in the single-currency area. The euro area's economic outlook for the current year remains guarded.

The German economy also lagged behind the strong prior-year trend, although growth rates were recorded for the ninth consecutive year. However, the weaker increase in gross domestic product is also due to temporary non-recurring effects. Nevertheless, a look back at the year as a whole shows that the external economic environment has clouded noticeably. Private consumption, the positive investment trend, a good employment situation and rising incomes all had a stabilising effect. Amidst an environment of growing global uncertainty, Germany's economic conditions are still stable in this respect. At the same time, we can expect to see growth rates slow further in 2019.

German real estate markets were unflustered by the economic trend in the year under review and made a very strong showing. The ongoing low-interest rate policy continued to provide positive stimulus. Against this backdrop, market activity was driven by the fast pace of growth. Together with housing investments, the German commercial real estate market generated a result of around € 79 billion in 2018 that was slightly higher than the previous year but falling just short of 2015's record € 80 billion. This was accompanied by rising prices. The demand for residential real estate for own use has remained high in many places. This development also led to a continued increase in rents and prices on the private residential real estate markets that was increasingly visible outside metropolitan areas given the high level in many cities. We may see this trend continue in the current year.

Amidst this environment, we enjoyed a pleasing new business volume totalling around € 11 billion in real estate financing, continuing the sound performance of the previous year. In three of our business segments – Commercial Real Estate Investors, Housing Sector and Retail/Private Investors – we succeeded in boosting new business. We even recorded growth rates in our Public Sector division. The result shows that even in our merger year, we have been able to fulfil our aspiration of being a reliable bank for our customers, cooperating closely with the German cooperative banks.

The resulting positive momentum in new business is also reflected in the Bank's net interest income, and demonstrates its strength. The increase in the average strategic real estate loan portfolio in particular has a positive effect. The net commission result was down year-on-year, due – among other things – to the brokerage payments to cooperative banks. Administrative expenses rose in the year under review, due – amongst other things – to merger-related expenses.

The ongoing demand for real estate indicates that this year will be a good one for the industry. Persistent low interest rates, a sound domestic economy and the appeal of the German market for foreign investors are key factors in this context. For us as a leading real estate bank in Germany, this means that we will continue to be able to leverage our potential in all business segments in 2019, and to further consolidate our stable position on the market. Our consistent and decentralised approach – with two head offices in Hamburg and Münster, six regional centres and eight regional offices – allows us to continue to serve our customers and the cooperative bank network as a one-stop shop with our extensive offering across Germany. This, together with our high level of expertise, sustainable partnership and competent expertise, sets us apart from the competition. Following the merger, we will work on further optimising our internal structures whilst driving technical and cultural integration. We consider ourselves to be well positioned for the challenges to come, and expect 2019 to be a stable year for DZ HYP.

Yours sincerely,

Dr Georg Reutter
Chief Executive Officer

Dr Carsten Düerkop

Manfred Salber

The Management Board
Hamburg and Münster, March 2019

REPORT OF THE SUPERVISORY BOARD

Chairman of the Supervisory Board
Uwe Fröhlich

DZ HYP's business once again showed better development than expected during the year under review, despite the impact of the measures relating to the merger. As far as its new business is concerned, the Bank managed to weather increasingly fierce competition and strike a balance between the work associated with the merger and its market coverage, and succeeded in transferring the solid position previously enjoyed by the two predecessor institutions to DZ HYP. All in all, DZ HYP achieved successful commercial performance in the 2018 financial year.

This performance was helped along by the sustained favourable economic climate in Germany, which provided a positive environment for the Bank's business. The 2018 financial year was characterised by buoyant activity on the real estate market, with demand showing no signs of slowing as sought-after properties remain in short supply. While moves by the European Central Bank to start unwinding its expansionary policy open up the prospect of a moderate increase in interest rates in principle, the yield advantage offered by real estate makes it an attractive investment that is in demand among investors and retail customers alike.

The Bank's working relationship with the German cooperative banks also proved successful during the year under review. This confirms DZ HYP's strong roots in the German Cooperative Financial Network (Genossenschaftliche FinanzGruppe) and its strategic focus, which is geared towards the joint lending business with the cooperative banks. The new joint lending business volume showed positive development in the 2018 financial year, and the Bank maintained a high level of cooperation with the cooperative banks.

With regard to refinancing, the Bank once again reaped the benefits of its membership of the Cooperative Financial Network and its strong credit quality. In this respect, the merged DZ HYP, as one of the largest Pfandbrief banks in Germany, was awarded a solid rating that bears testimony to its convincing performance.

In the year under review, the Supervisory Board dealt intensively, and on an ongoing basis, with the merger of DG HYP and WL BANK to form the Bank, which was merged with retroactive effect from 1 January 2018 (for commercial law purposes), and renamed DZ HYP AG. This involved looking at the progress made in, and requirements imposed by, the legal merger; it also involved the move to a uniform IT system together with the strategic and organisational structure of the merged institution. The Supervisory Board's discussions and resolutions also, however, addressed DZ HYP's rules and regulations, the exchange of WL BANK shares in connection with the merger and the associated valuations and capital measures, as well as the expansion of the Management Board to include four members, the appointment of a second Chief Executive Officer of the Management Board, and the application for a dual registered office for the Bank in Hamburg and Münster/Westphalia.

In 2018, the Supervisory Board also dealt regularly and in detail with business developments in what are now the Bank's four business segments (Commercial Real Estate Investors, Housing Sector, Public Sector, Retail Customers/Private Investors), and the Bank's portfolio quality, which continues to show positive development. It also gave considerable attention to DZ HYP's risk management system, as well as the regulatory requirements and the extent to which these were met. The further development of the associated reporting system was another focal point.

The activities of the Supervisory Board not only focused on assessing the work and qualifications of the Supervisory Board and Management Board at regular intervals, but also looked at the Bank's remuneration systems and the report of the Remuneration Officer, the target achievement levels of, and remuneration paid to, members of the Management Board, updating the targets for the promotion of the under-represented gender on the Supervisory Board and the Management Board, as well as the job description and candidate profile for the Supervisory Board.

After Mr Frank M. Mühlbauer resigned from the Management Board with effect from 31 December 2018, the Supervisory Board held an extraordinary meeting to discuss the consequences of his resignation, the options available for appointing a successor, and the individual and collective suitability of the remaining three Management Board members. This discussion was also considered to be of particular importance in light of the measures still to be implemented in order to consolidate the two merged institutions in the existing locations.

The Supervisory Board and its Committees

During the year under review, the Supervisory Board of DZ HYP and its committees monitored the Management Board's management of the Bank according to statutory regulations and those set out in the Bank's Articles of Incorporation, and also took decisions on those transactions required to be presented to the Supervisory Board for approval. To fulfil its tasks, the Supervisory Board engaged a Nomination Committee, a Remuneration Oversight Committee, an Audit Committee, and a Risk Committee during the 2018 financial year.

The self-evaluation of the Supervisory Board and evaluation of the Management Board (of then DG HYP) performed between April and May 2018 concluded that the structure, size, composition and performance of the Supervisory Board and Management Board, as well as the knowledge, abilities and experience of the individual members of both the Supervisory Board and Management Board (as well as both Boards as a whole) were wholly in accordance, both with the statutory requirements and with those requirements set out in the Bank's Articles of Incorporation. The Supervisory Board also has adequate human and financial resources at its disposal to assist members in taking up office, and ensure they receive in-house training to help them maintain the required expertise. The next regular evaluation of DZ HYP's Supervisory Board and Management Board is scheduled for the first half of 2019.

Cooperation with the Management Board

The Management Board reported to the Supervisory Board on DZ HYP's situation and performance, general business developments, profitability and risk exposure, regularly, in good time and comprehensively, both in writing and in verbal reports. Furthermore, the Supervisory Board was informed by the Management Board about the Bank's operative and strategic planning, and about material lending exposures and investments. The Management Board provided the Supervisory Board with regular information on the progress made in its discussions, first of all regarding the merger of DG HYP and WL BANK and – once the merger had been entered into the Commercial Register – regarding the further structuring and strategic focus of the merged DZ HYP.

The Supervisory Board discussed these issues, current developments and matters relating to the Bank's strategic focus with the Management Board; it advised the Management Board, and supervised the management of the Company. The Supervisory Board was involved in all decisions that were of fundamental importance to the Bank.

Meetings of the Supervisory Board

The Supervisory Board convened six times during the 2018 financial year. In addition, the committees engaged by the Supervisory Board – the Nomination Committee, the Remuneration Oversight Committee, the Audit Committee and the Risk Committee – convened on numerous occasions during 2018. The Chairmen of the various committees regularly gave accounts of their work to the plenary meeting.

Between meetings of the Supervisory Board, the Management Board informed it in writing of key events and transactions. In regular discussions with the Chief Executive Officer of the Management Board outside the meetings, the Chairman of the Supervisory Board and the Chairmen of the Committees also discussed key decisions, particular transactions, and the development of the Bank's business and risk exposure. Overall, the members of the Supervisory Board and its Committees participated regularly in the meetings of the respective bodies and written resolutions during the 2018 financial year. To avoid any conflicts of interest in the Risk Committee, one committee member did not participate in the respective resolutions. There were no other potential conflicts of interest during the year under review.

Cooperation with the external auditors

Ernst & Young GmbH Wirtschaftsprüfungsgesellschaft, Stuttgart, which presented a declaration of independence to the Supervisory Board, audited the annual financial statements of DZ HYP, including the accounting records and management report of DZ HYP for the 2018 financial year presented to it by the Management Board, and found these to be in line with statutory requirements. It issued an unqualified audit opinion. The audit report was submitted to members of the Supervisory Board, and was discussed in detail during Supervisory Board meetings. The Supervisory Board agreed to the results of the audit by the auditors, in line with a recommendation by the Audit Committee.

Approval and confirmation of the financial statements

The Supervisory Board and the Audit Committee reviewed the annual financial statements and the management report of DZ HYP in detail at their meetings. The Chairman of the Audit Committee notified the Supervisory Board about the detailed discussions of the Committee regarding the financial statements and the management report of DZ HYP. The auditor's representatives participated in the Supervisory Board meeting to adopt the annual financial statements, and in the preparatory meetings of the Audit Committee and the Risk Committee, and reported on the key findings of their audit in detail. They were also available to answer questions by Supervisory Board members. The Supervisory Board raised no objections with regard to the accounts. The Supervisory Board approved the financial statements of DZ HYP as at 31 December 2018, prepared by the Management Board, in its meeting on 29 March 2019. The financial statements are thus confirmed.

Personnel changes within the Supervisory Board and the Management Board

Mr Uwe Berghaus resigned from his office as Chairman of the Supervisory Board and from his positions on the Risk and Audit Committee with effect from 31 July 2018. The Supervisory Board elected Mr Uwe Fröhlich, who had been elected to the Supervisory Board as a new member by the General Meeting of Shareholders with effect from 28 May 2018, as Chairman of the Supervisory Board, and appointed him to the Risk and Audit Committees, with effect from 1 August 2018. Mr Heinrich Stumpf, Mr Werner Thomann and Mr Holger Willuhn all resigned from their positions with effect from 27 July 2018. Mr Rainer Peters, Mr Johannes Röring and Mr Hans-Peter Ulepić were elected as new members of the Supervisory Board of DZ HYP by the Annual General Meeting, with

effect from 28 July 2018. The Supervisory Board appointed Mr Rainer Peters to the Risk Committee with effect from the same date.

In connection with the merger to form DZ HYP, the Supervisory Board appointed Mr Frank M. Mühlbauer and Dr Carsten Düerkop to the Bank's Management Board with effect from 27 July 2018. Within this context, Mr Frank M. Mühlbauer was appointed as second Chief Executive Officer of the Management Board, alongside Dr Georg Reutter. This means that, with effect from 27 July 2018, the Management Board of DZ HYP comprised the two Chief Executive Officers, Mr Frank M. Mühlbauer and Dr Georg Reutter, as well as the other members Dr Carsten Düerkop and Mr Manfred Salber.

Mr Frank M. Mühlbauer left the Management Board of DZ HYP at his own request, with effect from 31 December 2018. The Supervisory Board would like to thank Mr Mühlbauer for his merits and for his achievements whilst at the Bank, in particular also with regard to the successful structuring and strategic orientation of the merged DZ HYP.

Otherwise, there were no changes to the members of the Supervisory Board and the Management Board during the 2018 financial year.

The Supervisory Board would like to thank the Management Board and all of DZ HYP's employees for their commitment and their successful work during the 2018 financial year, especially in light of the impact of the merger.

Hamburg and Münster, 29 March 2019

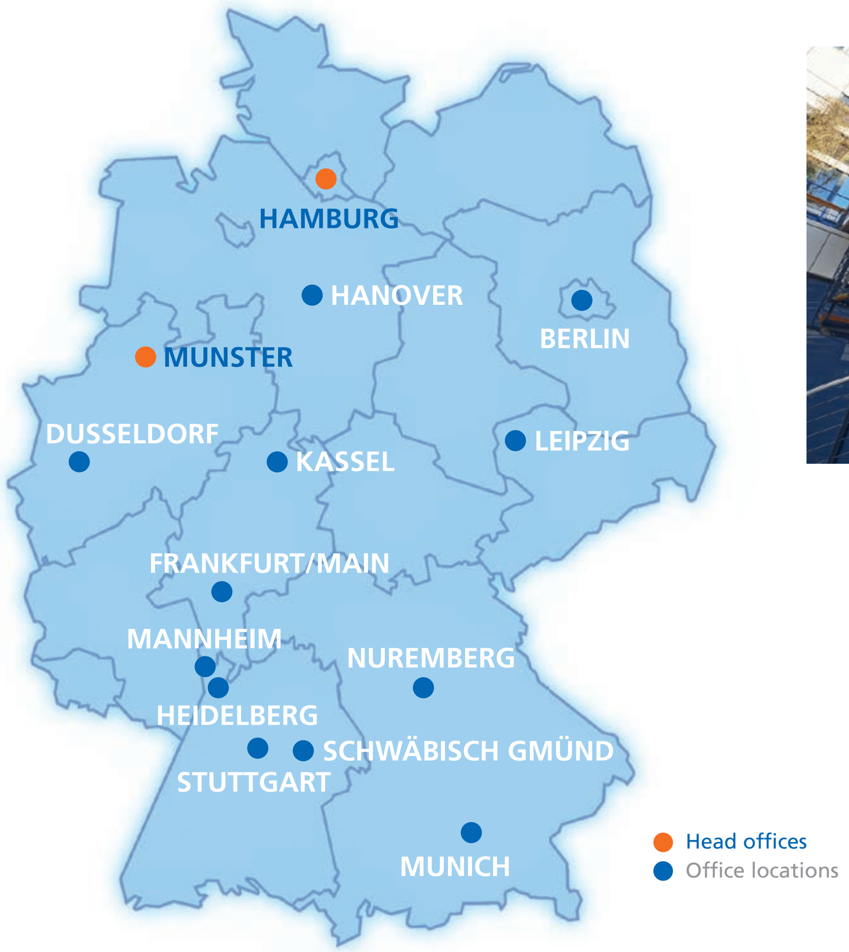
Uwe Fröhlich
Chairman of the Supervisory Board

CLOSE. TOGETHER. SUCCESSFUL.

DZ HYP, a leading German real estate bank, is entering the market

On 27 July 2018, DG HYP and WL BANK merged with retroactive effect from 1 January 2018, to DZ HYP. Since then, the Bank has been providing its clients and partners from the Cooperative Financial Network with a one-stop shop offering a comprehensive range of services in four divisions: Commercial Real Estate Investors, Housing Sector, Public Sector and Retail Customers/Private Investors.

DZ HYP employs approximately 870 staff members in two head offices, six regional centres, and eight regional offices. And it is these staff members who make the Bank a trustworthy and competent partner in real estate financing and public-sector lending. Broad regional diversification enables DZ HYP to be near its clients, as well as the cooperative banks.



We have completed a successful first financial year as DZ HYP, confirming our conviction that the merger was the right decision. Our broadly diversified market positioning enables us to further expand the competitive position of the Bank and the Cooperative Financial Network.

DR GEORG REUTTER,
CHIEF EXECUTIVE OFFICER OF THE MANAGEMENT BOARD

ABOUT DZ HYP

PARTNER FOR REAL ESTATE FINANCING AND PUBLIC-SECTOR LENDING IN THE GERMAN COOPERATIVE FINANCIAL NETWORK

As a member of the Cooperative Financial Network, DZ HYP is committed to the success of its partners and clients. The Bank is successfully and sustainably strengthening the market position of the cooperative banks in the business areas of Commercial Real Estate Finance, Housing Sector, Public Sector and Retail Customers/Private Investors. In DZ HYP, local cooperative banks have a highly competent partner supporting them, with a strong funding base, a broad, decentralised approach and close proximity to their clients.

Its central business policy role is to anchor real estate financing and local authority lending in the Cooperative Financial Network, and to realise financing solutions together. To this end, DZ HYP offers the German cooperative banks an extensive and outcome-oriented range of products and services, working hand-in-hand with them to cultivate the regional markets. Cooperation is a guarantee for successfully tapping potential in real estate financing and public-sector lending. In this context, both sides benefit from the partnership – DZ HYP from the direct contact with regional clients, and the German cooperative banks from the business relationships arising from developing the market throughout Germany.

In the business with Commercial Real Estate Investors, cooperation with DZ HYP puts the cooperative banks in a position to realise larger financing solutions for their medium-sized clients, as well as diversifying their own risk. In the Housing Sector business, too, the German cooperative banks can tap into the specific financing expertise of their partner within the network, while at the same time contributing their regional market knowledge. The Bank acts as a centre of competence within the DZ BANK Group for coverage of public-sector clients. In the Retail Customers/Private Investors business, DZ HYP offers the cooperative banks various credit models for tailored cooperation and longer fixed-interest periods.

Other services offered to the Cooperative Financial Network include the rating of commercial real estate clients, property valuations performed by the Bank's own appraisers or its wholly-owned subsidiary VR WERT Gesellschaft für Immobilienbewertungen mbH, a municipal ranking that uses the latest data to provide information on the economic, budgetary and debt situation of the municipalities in the individual business regions, and the daily "Investor Barometer" newsletter on terms and conditions.

Good ratings confirmed

In the 2018 financial year, Standard & Poor's (S&P) reviewed DZ HYP's rating in the light of the merger of DG HYP and WL BANK and rated the resulting diversification as advantageous, particularly in the real estate portfolio. As a result, it confirmed DZ HYP's good issuer rating of "AA-"/"A-1+", with a stable outlook. By awarding this rating, S&P has acknowledged DZ HYP's core function both within the DZ BANK Group and within the Cooperative Financial Network, with its deep integration into the sector and its membership of the deposit insurance scheme of the National Association of German Cooperative Banks (Bundesverband der Deutschen Volksbanken und Raiffeisenbanken – "BVR"). S&P also confirmed the top "AAA" rating for DZ HYP's Mortgage and Public Pfandbriefe after the merger of the two cover assets pools, and assigned them a stable outlook.

FitchRatings evaluated DZ HYP as part of the joint rating awarded to the Cooperative Financial Network and confirmed the issuer rating of "AA-", as well as the short-term rating of "F1+". The stable outlook was maintained.

RATING OVERVIEW

	Standard & Poor's	FitchRatings *
ISSUER CREDIT RATING	AA-	AA-
Outlook	stable	stable
Short-term liabilities	A-1+	F1+
ISSUE RATINGS		
Mortgage Pfandbriefe	AAA	–
Public Pfandbriefe	AAA	–
LONG-TERM LIABILITIES		
- Preferred Senior Unsecured	AA-	AA-
- Non-Preferred Senior Unsecured	A+	AA-

* Joint rating of the Cooperative Financial Network

DIGITALISATION

Digitalisation initiatives continued

Digitalisation and growing technological innovation are not only changing the economy and society, but also the working environment. More than one-third of communication takes place via digital channels. Yet digitalisation is much more than simply an issue of IT and processes: it brings about profound changes in markets and business models. DZ HYP already confronted these challenges a few years ago, when it launched various digitalisation initiatives – involving products, processes, the technical infrastructure, client interfaces, and also employee requirements and future personnel development.

In the year under review, various digitalisation projects at DZ HYP were successfully finalised. These include, by way of example, the electronic exchange of data in connection with residential and commercial real estate developments: launched in a pilot project, electronic processes are deployed to simplify and accelerate payments.

Securing the future viability of the lending business

During the year under review, the Bank has continued to be involved in the development of innovative value-added services. DZ HYP analytics offers highly informative reports in a compact format for all major real estate market segments in more than 11,000 communities nationwide. These reports are available via an online shop. The analyses show the development of price data for multi-family homes, owner-occupied apartments and owner-occupied homes, as well as rental data for the residential, retail and office segments over the last ten years. A Middle Office Platform (MOP) enabling digital process integration throughout the cooperative banks is currently being developed, to ensure the future viability of the lending business in private home loan financing. In its work to develop the MOP, DZ HYP is employing agile methods and state-of-the-art software technology, allowing the parties involved to achieve secure and user-friendly integration.

The smart use of client and market data will be a critical success factor on the competitive landscape within the real estate industry. With this in mind, DZ HYP implemented its first few projects dealing with smart data and in-memory technologies in the year under review. These projects will be expanded further over the coming years as the technologies become increasingly established.

DZ HYP also performed another review of the status quo of all four business segments in 2018, in order to identify any necessary initiatives. This involved comparing market trends and future scenarios against the measures that have already been initiated or planned, as well as identifying any threats and need for action.

Intensive market observation

Ongoing digitalisation will result in changes affecting processes in the financial sector and in the real estate industry in particular. A new generation of competitors is emerging through 'crowdfunding' platforms. Although FinTechs offer solutions that are also part of banks' core area of expertise, they have not been perceived as significant competitors to date, but rather as partners in cooperation models. Their strength lies in their ability to use new software and hardware solutions to make existing processes more efficient. DZ HYP is keeping a close eye on these developments and, together with its partners, will take any necessary measures in good time.

SUSTAINABILITY

Sixth sustainability report published

As a member of the DZ BANK Group, DZ HYP is committed to the fundamental cooperative concept of responsible business practices. This means that the Bank's entrepreneurial spirit has a long-term horizon; it uses natural resources in a sensitive and efficient manner, and takes risks and opportunities into consideration as part of its decision-making processes. DZ HYP has been providing transparent information about its sustainability performance in its annual sustainability reports since 2012. 2018 saw the publication of the sixth sustainability report for the 2017 financial year based on the G4 guidelines promulgated by the Global Reporting Initiative (GRI). Following the merger of DG HYP and WL BANK with retroactive effect from 1 January 2018, the sustainability activities pursued at the two locations in Hamburg and Münster are being consolidated, while sustainability management is being expanded to cover the Bank as a whole, with the active involvement of the departments in Münster. DZ HYP's first sustainability report will be published at the end of June 2019.

Sustainability ratings: DZ HYP awarded "prime" rating

In the year under review, the sustainability rating agency ISS-oekom confirmed DZ HYP's position as one of the best companies in its sector in terms of social and ecological performance, even after the merger. ISS-oekom awarded the Bank a "Corporate Rating" of "C". As a result, DZ HYP has once again been awarded "Prime" status, meaning that it ranks among the most sustainable institutions in the industry in the "Financials/Mortgage & Public Sector Finance" peer group.

Sustainable corporate governance and strategy

Responsible corporate governance based on the principles of DZ HYP's sustainability strategy is an essential prerequisite for the Bank's economic performance. As part of its business model, DZ HYP applies a conservative risk strategy, pursues long-term business relationships, and is committed to interacting with its clients in the spirit of partnership. The Bank assumes responsibility for its employees and is a committed member of society. This also means making a contribution to cutting CO_2 emissions, and both identifying climate risks and taking them into account in its business decisions. As a result, DZ HYP welcomes the current debate on how to create a more sustainable financial sector as part of the European Commission's "Financing Sustainable Growth" action plan.

Responsibility for its employees

Entrepreneurial success depends largely on the dedication and performance of the Bank's employees. As a result, DZ HYP pursues a human resources policy that strikes a balance between the needs of its employees and economic requirements in an environment characterised by demographic change. Key components of this policy include targeted personnel development, the recruitment and training of qualified trainees, and moves to promote career advancement among women. In addition to ensuring that its employees can reconcile their work and family commitments, DZ HYP offers an extensive corporate health management programme for its staff.

Social commitment

The cooperative basic values of aiding empowerment, solidarity, partnership and social responsibility are cornerstones of DZ HYP's social commitment. In keeping with these values, the Bank supports the Active Citizenship Association (Aktive Bürgerschaft), which advocates civic action and non-profit organisations. It also supports the CLUB OF ROME's German charter by providing the club's branch office with premises in Hamburg. DZ HYP is the host and financial backer of the annual meeting of the CLUB OF ROME schools network. The Bank was recognised as an educational partner for the schools in 2015, allowing it to contribute to the implementation and expansion of the CLUB OF ROME school network's activities at national level. Further examples of DZ HYP's professional commitment include its funding of German scholarships for students at HafenCity Universität university, the promotion of the "German Women in Real Estate VISIONALE 2018" initiative (Frauen in der Immobilienwirtschaft VISIONALE 2018) and the alumni network of the real estate industry, IMMOEBS, as a premium partner.

Within the scope of the "Schools and Business Partnership" project launched by a chamber of commerce and industry, DZ HYP cooperates with two schools in Münster, providing hands-on vocational orientation through internships and visits, thus promoting an understanding of the economy amongst young students. Acting as 'training ambassadors', selected vocational trainees visit schools, giving authentic insights into the vocational training required to become a bank officer, and into the dual course of study. Likewise, DZ HYP offers students internships designed to support vocational orientation, as part of the "Don't leave school without the prospect of a job" project run by the State of North-Rhine Westphalia.

As part of its commitment to social responsibility, during the year under review the Bank subsidised the Hamburg Donor's Parliament (Hamburger Spendenparlament), which supports initiatives to help the homeless and people living in poverty and isolation. The Bank also held its fifth "Social Day" in the summer, when a team of employees got involved with the "Sternenbrücke" children's hospice during working hours to help with gardening work in Hamburg. In addition to other customer-related donations, the Bank once again doubled its employees' annual Christmas collection. The donation went to the "wish van" project organised by the German Federation of Samaritan Workers (ASB-Wünschewagen) and to the charity "basis und woge e.V." for its KIDS project. As in previous years, DZ HYP once again decided not to send out Christmas cards in 2018, instead using the amount saved to provide financial support to two social projects proposed by its employees.

Ecological responsibility

Since the beginning of 2018, extensive refurbishment work has been under way at the Hamburg head office, which also includes energy-efficient measures to modernise the building. Extensive renovation work has also now been approved for the Münster head office, with work scheduled to begin in early summer 2019. As well as improving the working environment, these construction measures aim to reduce energy requirements and improve pollutant emissions. The modernisation work will give both locations the opportunity to obtain certification from the German Sustainable Building Council (DGNB): the Hamburg office is aiming for a DGNB "silver" certificate, while Münster could achieve "gold" certification.

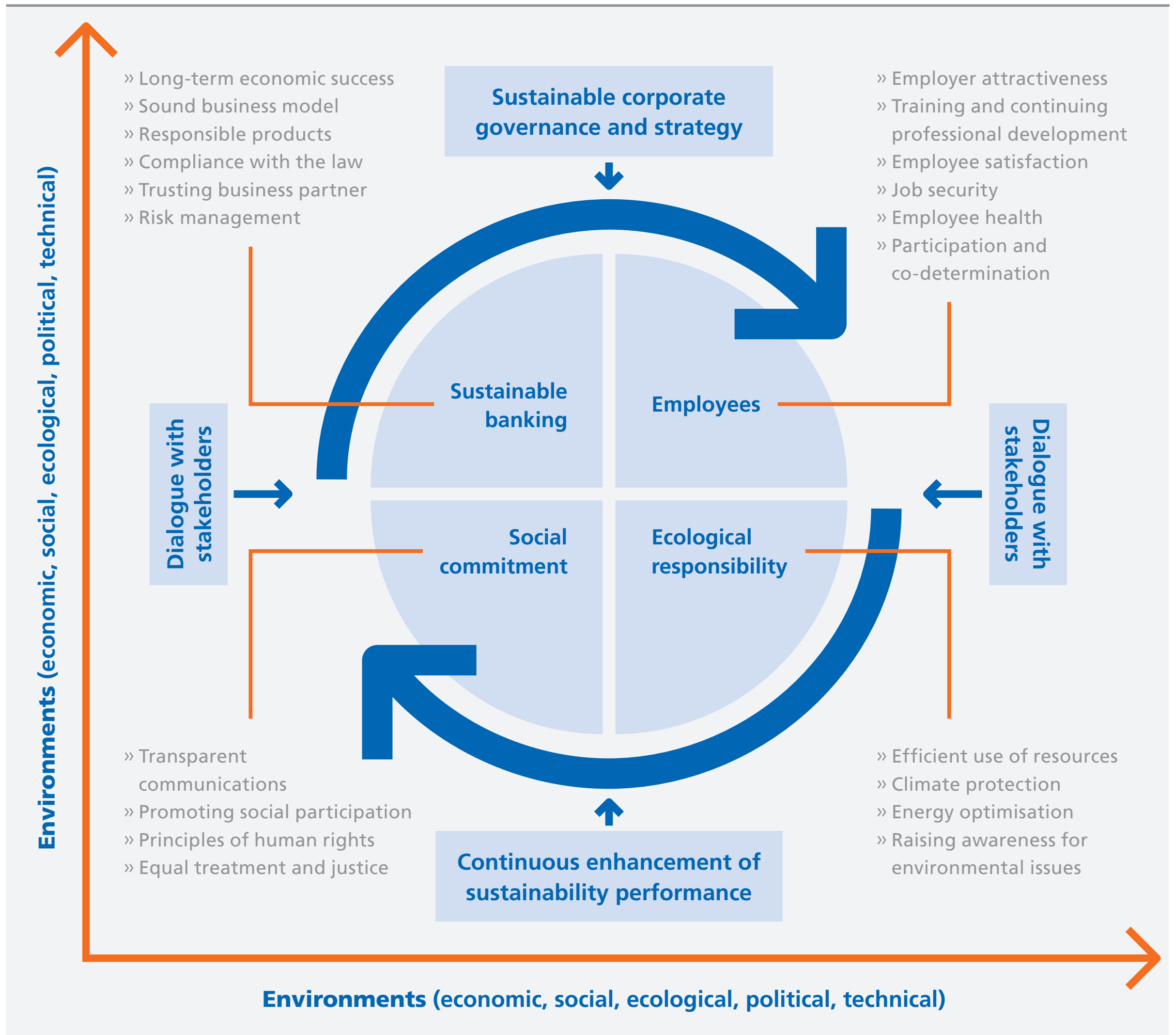
The responsible use of natural resources and environmental protection are of the utmost importance to DZ HYP in its day-to-day operations as well. The environmental team at DZ HYP ensures the implementation and further development of the environmental management system, involving the specialist departments in the process. The fact that the Münster site has been certified under the ÖKOPROFIT programme (an ecological project for integrated environmental technology involving the City of Münster, industry, chambers of commerce and national partners) since 2012 bears testimony to the high quality of the environmental management system. Other key steps in the year under review included the switch to almost 100% recycled paper bearing the Blue Angel ecolabel, and the move to transition the Bank's entire power supply to renewable energy sources.

In order to promote emission-free or low-emission mobility for employees, an electric car has been available to the Bank's staff at the Hamburg office for work-related travel since 2016. In Münster, the Bank allows its employees to lease a company bike or e-bike at a reasonable price via the bicycle leasing specialist JobRad.

Sustainability in the DZ BANK Group

With a view to integrating sustainability to an even greater extent in business processes, DZ HYP has been playing an active role in the DZ BANK Group's sustainability market initiative since 2012. This initiative aims to bundle sustainability-related activities, take advantage of market opportunities, avoid risks, and foster the active exchange of knowledge and experience between members of the Group. For this purpose, a permanent Corporate Responsibility Committee (CRC) was formed in 2014, of which DZ HYP is a member. The results of this collaboration include, for example, the introduction of a Group-wide database structure, common supplier standards, the development of a policy on sustainability in lending, and a coordinated environmental and climate strategy.

SUSTAINABILITY IN THE DZ BANK GROUP



THE COMMERCIAL REAL ESTATE INVESTORS DIVISION

ATTRACTIVE DIVERSITY

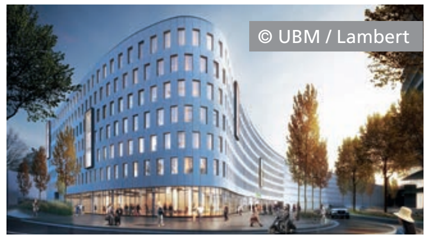
"Mixed-use" properties are appealing due to the varied opportunities of use

The ways in which we work, consume and move, are changing. Inner-city housing is more in demand than ever. Office employees prefer urban areas, and people are increasingly asking for short distances between their home, work and shopping facilities. Real estate providers have responded to this, developing new concepts adapted to the changing attitude towards life.

In the midst of current trend developments, one real estate type is especially gaining in importance: so-called "mixed-use" properties, offering housing, working space, shopping, fitness, continuing education and amusement. People do not need to commute, since work and leisure activities are perhaps only a few storeys apart from each other, making it efficient, resource-friendly and thus especially popular among young people. "Das Lebendige Haus" is a good example for a successful mixed property. It boasts a rental mix of gastronomy, commercial trade, conferences, co-working, fitness, and living. The concept is aimed specifically at achieving an experience which strikes a comfortable balance between working and private life inside a single property, with the emphasis on short distances – within the building, as well as an inner-city location.
The first "Lebendiges Haus" was opened mid-2016 closed to Dresdner's "Zwinger"; a second "Lebendiges Haus" followed at the end of 2018 in Leipzig (in the building of the former main post office, on Augustusplatz). Further locations are currently being planned.

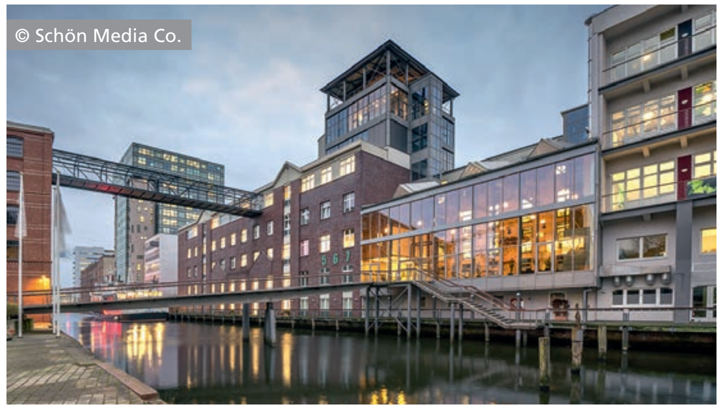
Steffen Günther, Head of Commercial Real Estate Investors Institutional & International Customers | Norbert Grahl, Head of Back-Office Commercial Real Estate Investors | Axel Jordan, Head of Commercial Real Estate Investors Corporates & Cooperative Banks

H31, Darmstadt



Holiday Inn Express, Dusseldorf

Maximiliansquartier, Berlin



The Channel, Hamburg

"Das Lebendige Haus", Dresden

DZ HYP supports "Das Lebendige Haus" as financing partner.

>> The desire to live and work in a lively atmosphere with short distances is increasing. "Mixed-use" properties are often based on sustainable and modern concepts. Whilst the variety of use requires intensive management, it also offers the advantage of letting small spaces, thus reducing the vacancy risk. We are convinced that properties with attractive mixed use will establish themselves on the market in the long term. <<

AXEL JORDAN, HEAD OF COMMERCIAL REAL ESTATE INVESTORS CORPORATES & COOPERATIVE BANKS

MANAGEMENT REPORT

BUSINESS MODEL

DG HYP and WL Bank merged to form DZ HYP in the 2018 financial year. The merger was entered into the Commercial Register as scheduled on 27 July 2018. The merger took effect retroactively from 1 January 2018. The strategic objective was to combine the two banks' existing areas of expertise whilst avoiding redundancy, providing clients with a one-stop shop, and in particular, to further enhance benefits for German cooperative banks. The merger marked the continuation of the consolidation process, together with an efficient positioning of the Cooperative Financial Network. Previous year's figures in the management report are aggregated figures for the individual institutions.

The commercial real estate bank for the Cooperative Financial Network

DZ HYP is a leading provider of real estate finance and a major Pfandbrief issuer in Germany, as well as a centre of competence for public-sector clients within the Volksbanken Raiffeisenbanken Cooperative Financial Network. The Bank is active in four segments: Commercial Real Estate Investors, Housing Sector, Public Sector, and Retail Customers/Private Investors. In its business activities, DZ HYP targets its clients directly and acts as a partner to the approximately 900 cooperative banks in Germany. This means that the Bank is helping to strengthen the Cooperative Financial Network in its successful and sustainable positioning in the market.

Joint market coverage with the German cooperative banks

Thanks to its size and stability, the German real estate market offers particular potential for successful business. The municipal business also offers attractive opportunities for successful market entry. DZ HYP provides its partner banks and clients in the four segments with an extensive range of tailor-made financing solutions, which are adapted to suit client needs and current market developments. The resulting opportunities are consistently exploited together with the German cooperative banks. Servicing these banks as an associated provider is a key element of the Bank's sales activities. It is committed to supporting the regional market development of the local banks with a broad, decentralised structure and close proximity to its customers.

Highly customised financing solutions for Commercial Real Estate Investors

In its Commercial Real Estate Investors division, DZ HYP engages in the business with investers directly or as a partner to the cooperative banks in Germany. The focus of the Bank's business activities is on financing properties in the German market. In addition, DZ HYP supports its German clients' investment projects in selected international markets. The Bank's focus is on the core segments of office, residential, and retail properties. DZ HYP is also involved in the specialist segments of hotels, logistics and real estate for social purposes, within the scope of its credit risk strategy. Target clients are private and institutional investors, as well as commercial and residential real estate developers. When selecting exposures, the priorities are the quality of the client relationship, the third-party usability of the financed property, and collateralisation through first-ranking mortgages.

Financing solutions for the Cooperative Financial Network

With the IMMO META product family, DZ HYP offers German cooperative banks a high-performance and comprehensive range of products for successful cooperation in the field of commercial real estate financing. The core product is IMMO META REVERSE+, through which a large number of cooperative banks can acquire individual tranches of a financing arrangement concluded by DZ HYP, as partners in the syndicate, of equal rank and in a standardised manner. The German cooperative banks can access an online platform, to simplify the process and ensure efficient distribution. A framework agreement must be concluded prior to utilisation. Since it was launched on the market back in 2009, almost 500 framework agreements have been concluded with cooperative banks, with around 320 institutions having participated in financing transactions on one or more occasions.

Further products of a cooperation based on partnerships are IMMO META REVERSE and IMMO META. Via the latter, DZ HYP participates pari passu with cooperative banks in commercial real estate financing for regional SME real estate clients. The cooperative banks retain their leadership role with such financing. Using IMMO META REVERSE, the cooperative banks can get involved in selected large-volume projects in their regions, from as early as the origination phase. The cooperative banks themselves decide on the level of their involvement, participating on a pari-passu basis.

Successfully managing real estate risks

To complement its product range in the field of commercial real estate finance, DZ HYP makes a web-based, convenient rating application that is uniform across the cooperative network available to the German cooperative banks in the form of "agree21VR-Rating-IMMO". This allows the cooperative banks to determine the customer-specific default risk associated with their commercial real estate customers. DZ HYP offers this application in collaboration with Fiducia & GAD IT AG and parcIT GmbH. The banks can use the process to implement a modern risk management process that takes account of all the relevant factors. It is aimed at cooperative banks that focus on commercial real estate finance, and at those for which commercial real estate accounts for a significant proportion of their credit portfolio. The rating application provides a key foundation for joint commercial real estate lending business within the Cooperative Financial Network, and is encountering continuous demand growth. As at 31 December 2018, 472 German cooperative banks were using agree21VR-Rating-IMMO, compared to approximately 400 in 2017.

A strong partner for the Housing Sector

DZ HYP is a major finance provider to the German housing sector, and a leading institution within the Cooperative Financial Network. This area of business is originated both using a direct business approach and in close cooperation with cooperative banks. DZ HYP also cooperates with selected intermediaries. The focus is on customised financing solutions for residential or mixed-use properties, with fixed interest rates for up to 30 years. Cooperative, municipal, church-based and other housing companies in Germany receive loans and forward loans for their new construction, modernisation and renovation projects, also in combination with subsidised development loans granted by the German government-owned development bank (Kreditanstalt für Wiederaufbau – "KfW"). DZ HYP focuses on long-standing customer relationships with companies that create sustainable and affordable housing for broad sections of the population. It is a premium sponsoring member of the German Federal Association of German Housing and Real Estate Companies (Bundesverband deutscher Wohnungs- und Immobilienunternehmen e. V. – "GdW") and a sponsoring member of numerous regional associations. In this capacity, it is committed to intensive dialogue between real estate financing providers and housing companies.

Centre of competence for the Public Sector

As a centre of competence for public-sector clients within the Cooperative Financial Network, DZ HYP supports cooperative banks across Germany in developing their business with regions, towns/cities and local authorities, their legally dependent operations and municipal administrative unions. The core of both the business conducted jointly with the German cooperative banks and the direct business is the granting of short-term public-sector loans and municipal loans/promissory note loans, as well as bonds. Around 80 per cent of the municipal business transactions are placed with DZ HYP by the Cooperative Financial Network. The spectrum of collaboration ranges from purely commission-based, intermediated business to joint client development. In addition, DZ HYP offers banks a municipal ranking that uses the latest data to provide information on the economic, budgetary and debt situation of the municipalities in the individual business regions. The public-sector client target group includes smaller and medium-sized municipalities in particular. Across Germany, the Bank has around 7,000 municipalities among its business partners. The DZ HYP portfolio also includes Public/Private Partnerships (PPPs). For specific projects, other experts from the DZ BANK Group are also included.

Tailored solutions for Retail Customers/Private Investors

As part of the Cooperative Financial Network, DZ HYP also works closely with cooperative banks in the retail business. Joint customers include private developers and investors acquiring properties as owner-occupier, or for investment purposes. The latter are targeted exclusively in the intermediated or syndicated lending business with the cooperative banks.

DZ HYP offers initial and follow-up financing for new construction, purchase and modernisation/refurbishment, both as conventional home loan financing and in combination with subsidised development loans from the KfW Group's portfolio of public-sector subsidised development loans. The fixed-interest periods range up to 30 years. Various special options for repayment deferral and/or unscheduled repayments allow for individual solutions in standardised processes to meet the needs of the customers. DZ HYP's front end is deeply integrated in cooperative banks' core banking systems, and therefore compatible with their data processing. This enables the Bank to achieve a highly efficient joint construction financing process without unnecessary duplication or system breaks. The joint customers benefit from fast and reliable loan decisions using the full range of financing products. Collaboration always requires a framework agreement.

Real estate valuation expertise

The valuation of real estate properties is essential in order to conduct pricing commensurate with risk and guarantee the portfolio quality of the loans. The approximately 60 employees in DZ HYP's real estate valuation team and the wholly-owned subsidiary VR WERT Gesellschaft für Immobilienbewertungen mbH have excellent qualifications, and the majority of them are certified by the industry certification body HypZert.

DZ HYP's real estate valuation team values properties financed by the Bank with a focus on the Housing Sector/Retail Customers/Private Investors. The range of services offered includes market value and mortgage lending value appraisals in accordance with the Regulation on the Determination of the Mortgage Lending Value (BelWertV), spot checks of valuations and appraisals performed by contractual partners (cover pooling), as well as advice/consultancy on real estate matters. DZ HYP's appraisers are involved in the development of the Cooperative Financial Network's valuation systems and make compendia and practical guidelines available for this purpose.

VR WERT is a wholly-owned subsidiary of DZ HYP and values properties financed by the Bank with a focus on commercial real estate investors, who require a particularly sophisticated and individual case analysis. In addition, VR WERT appraises all types of real estate for banks, the corporate sector, investors, funds and housing cooperatives. The range of services offered includes market and mortgage lending value appraisals, advice/consultancy on real estate matters and product audits of appraisals performed by German cooperative banks. Depending on what the client requests, mortgage lending values are calculated in accordance with the Regulation on the Determination of the Mortgage Lending Value or the uniform Valuation Directive 3.0 (Wertermittlungsrichtlinie 3.0) of the Cooperative Financial Network.

Close at hand, flexible and effective

DZ HYP is represented nationwide, with two head offices in Hamburg and Münster, six regional centres in the business hubs of Hamburg, Berlin, Dusseldorf, Frankfurt, Stuttgart and Munich and eight regional offices in Hanover, Heidelberg, Kassel, Leipzig, Mannheim, Münster, Nuremberg and Schwäbisch-Gmünd. The decentralised structure ensures regional proximity to both customers and local cooperative banks. Front-office and back-office facilities are both to be found at the regional centres, laying the ground for a flexible and effectively managed lending process. Other factors in our success include professionalism, in-depth technical expertise, funding power and a high degree of market penetration backed by an efficient network.

Jürg Schönherr, Head of Housing Sector & Private Investors | Markus Wirsen, Head of Back-Office Housing Sector, Private Investors & Retail Customers

THE HOUSING SECTOR DIVISION

STRATEGIC DEVELOPMENT OF RESIDENTIAL QUARTERS

Holistic planning is gaining importance

Which requirements will people have regarding their living environment? Which needs will they develop, in the wake of demographic change and digitalisation, inclusion, and new working environments? Nowadays, housing providers need to develop plans to address these questions, and have to answer them holistically if they want to offer sustainable real estate on the market.

Strategically planned, modern residential quarter development takes the entire spatial and social infra-structure of a location into consideration. The aim is to create the best prerequisites for an environment of "encounter and support", which all inhabitants benefit from. The residential complex "Kastanienhöfe" in Düsseldorf-Eller, for example, offers a common living environment for young and old, singles and families, people with and without disabilities. The green courtyard, with its majestic population of old chestnut trees, invites residents to relax. Furthermore, central meeting space – or "gathering space" – encourages a closer neighbourhood community. All 101 apartments and access areas are easily accessible or even barrier-free. In cooperation with Lebenshilfe e.V., a registered association to support the disabled, eight of the apartments to let come with ambulant care for residential groups or individual tenants.

DZ HYP supports the "Kastanienhöfe" property in Düsseldorf-Eller as financing partner.

© Düsseldorfer Bau- und Spargenossenschaft eG (all images)

» Sustainable residential quarters have to respond to changing needs regarding mobility, local retail, and services adapted to specific phases of life. Good concepts, including strategic planning, allow for an attractive housing supply and sustainably increase the value of a property. «

JÜRG SCHÖNHERR, HEAD OF HOUSING SECTOR & PRIVATE INVESTORS

ECONOMIC REPORT

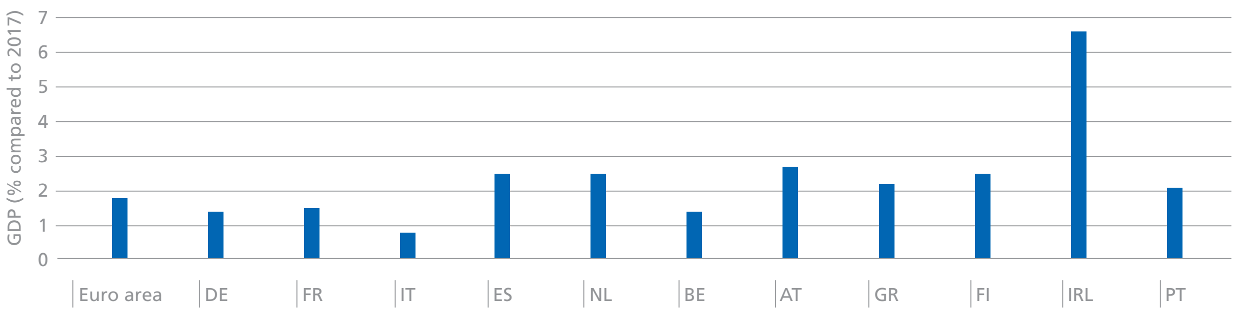
ECONOMIC ENVIRONMENT

German economic growth slows

The German economy remained on its nine-year growth trajectory in 2018, albeit reporting the weakest growth in gross domestic product since 2013, at 1.5 per cent (previous year: 2.2 per cent). The problems faced by the automotive industry in connection with the new emissions standard put a particular damper on the economy. Positive impetus is being provided by the labour market, which remains in good shape, and wage increases. Domestic demand remains robust but has dipped somewhat, with consumers setting a larger chunk of their income aside in savings. By contrast, growth in capital expenditure was slightly higher than in 2017. Equipment investments in the corporate sector, in particular, have made a return to greater momentum, while the construction industry continued to boom.
Global demand for German industrial products tapered off in an environment marred by various political pressures, with German export growth more or less being sliced in half in 2018. As imports grew at a slightly faster pace last year, foreign trade slowed the economy down on the whole. At 1.3 per cent, employment growth was more or less on a par with the last three years. This is likely to boost consumer enthusiasm among private households.

The rate of growth in government consumer spending fell again in 2018 and is currently sitting at only 1.1 per cent. Investments in public civil engineering, in particular, have been upped considerably in a year-on-year comparison. Research and development expenditure has also increased. Against the backdrop of rising inflation rates, the rate of growth in private consumer spending comes to 1.0 per cent. German exports suffered as a result of the slowdown in growth. Exports of goods and services in 2018 were 2.4 per cent higher (inflation-adjusted) than in 2017, when the increase of 4.6 per cent over 2016 was almost twice as high.

DEVELOPMENT OF GROSS DOMESTIC PRODUCT (GDP) 2018 – EURO AREA AND SELECTED OTHER COUNTRIES



Euro area	1.8	Italy	0.8	Belgium	1.4	Finland	2.5
Germany	1.4	Spain	2.5	Austria	2.7	Ireland	6.6
France	1.5	Netherlands	2.5	Greece	2.2	Portugal	2.1

Source: DZ BANK Research

Continuous growth in the euro area remains intact

The economic recovery in the euro area is meanwhile in its fourth consecutive year. Having overcome the deep recession of the financial crisis in 2009, and of 2012 and 2013 as a consequence of the sovereign debt crisis, the economy continued to recover in the year under review, with gross domestic product rising by 1.8 per cent, compared with the slightly higher level of 2.4 per cent in 2017. A potentially uncontrolled Brexit, i.e. the United Kingdom leaving the European Union (EU) without any form of exit agreement in place, new EU emission regulations, and simmering international trade conflicts, all curbed growth. Particularly the three largest countries in the euro area – Germany, France, and Italy – saw economic growth notably curtailed. The unemployment rate fell further, to 7.9 per cent in 2018, after 8.7 per cent the year before, thus increasing the consumer strength of private households.

Private consumption was the main driver behind the gross domestic product in the first three quarters of 2018. Compared to the previous year's quarters, private consumption increased by 2.8 per cent, thus contributing around 54.0 per cent to gross domestic product. Gross investments (including inventory changes) and government spending also rose by 6.0 per cent and 2.8 per cent, respectively. Overall, both factors account for about 41.5 per cent of gross domestic product. The number of exports also went up in the period under review – however, the same applied to imports. Net exports (total exports minus total imports) accounted for 4.5 per cent of gross domestic product.

The United Kingdom's exit from the EU

At the beginning of 2018, the United Kingdom and the EU drew up a withdrawal agreement capturing the compromises agreed upon in 2017. It is a compromise, and fulfils some significant aspects which the British population voted on in the 2016 referendum: withdrawing from the free movement of persons and from the ongoing payment commitments to Brussels. In turn, the United Kingdom will have to leave the European Single Market. A controlled exit was determined for 29 March 2019. The threat of an uncontrolled Brexit remains, coming along with uncertainty and dampened growth expectations.

Reduction in the asset purchase programme

On 13 December 2018, the Governing Council of the European Central Bank (ECB) decided that December 2018 would signal the end of its net asset purchase programme. At the same time, key interest rates were left unchanged. The strength of domestic demand and growth in the euro area are creating increasing inflationary pressure. As a result, the ECB's Governing Council expects inflation to continue to edge towards the inflation target even after the net asset purchase programme has ended. The main refinancing rate has been sitting at zero per cent since March 2016. The rate for the deposit facility was -0.40 per cent and 0.25 per cent for the peak refinancing facility during the year under review.

Sources: DZ BANK Research, German Federal Statistical Office, European Central Bank

MARKET DEVELOPMENTS

Development of the Real Estate Markets

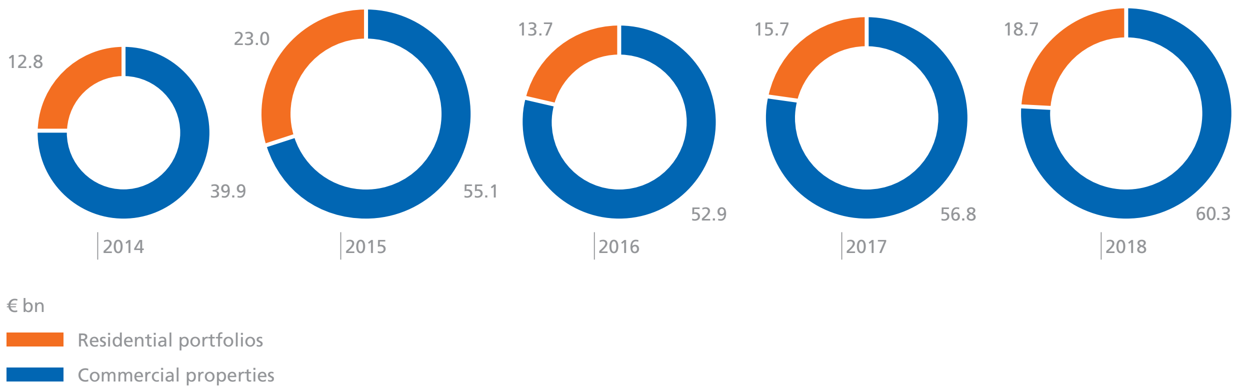
Flourishing investment market

The business environment for the German commercial real estate market remained positive in the 2018 financial year. Thanks to the persistent low-interest rate environment, a stable, albeit weakening, upward trend in the German economy, and the unchanged favourable labour market and wage developments, the upswing on the investment market continued unabated in the year under review. At around € 60.3 billion (excluding residential properties), the volume of commercial real estate transactions outstripped the record result achieved in the previous year by € 3.5 billion. This represents an increase of 6 per cent and marks the highest full-year result seen in the last ten years. Including the "Living" usage class (residential portfolios, "micro-apartments" and long-term care properties), the total transaction volume came to € 79 billion. The good result recorded in the year under review is not only attributable to strong demand but also to the noticeable increase in prices, which also substantiate the higher transaction volume.

Thanks to stable political conditions and years of positive economic development in Germany, foreign investors continued to show keen interest in the market in 2018. Around 42 per cent of the overall transaction volume was attributable to international investors. Looking at the investment market (as a whole), the seven large German real estate locations of Berlin, Dusseldorf, Frankfurt, Hamburg, Cologne, Munich and Stuttgart accounted for a transaction volume of € 46.0 billion in 2018 – up 20 per cent on the previous year. Activity among investors outside of the country's major cities remained at the previous year's level. With a transaction volume of € 33.0 billion, only slightly less commercial real estate was traded in regional locations throughout Germany than in the previous year (around € 34.2 billion). Frankfurt was the strongest market, with a transaction volume of more than € 11.6 billion and an increase of 49 per cent over 2017, followed by Berlin with € 10.8 billion (-8 per cent). Considerable gains were also made by Hamburg (+44 per cent), where the volume increased to € 7.2 billion, and Stuttgart (+56 per cent), where real estate worth € 2.5 billion was traded. With the exception of Berlin, the only city in which the transaction volume fell was Cologne.

As regards the various asset classes, investors focused once again on office properties, which accounted for 37 per cent or just under € 29 billion of the volume. At € 21 billion, residential real estate accounted for around 27 per cent, while retail properties made up a share of 13 per cent at € 10 billion. The transaction volume for logistics properties was down slightly year-on-year: around € 7.9 billion was invested in this asset class in 2018, representing 10 per cent of the transaction volume. Additionally, new and revitalised neighbourhoods and mixed-use properties are emerging increasingly in the inner-cities; at almost € 4.0 billion, these accounted for around 5 per cent of the transaction volume.

COMMERCIAL REAL ESTATE FINANCE VOLUMES IN GERMANY



Source: Jones Lang LaSalle

Upward trend in the residential investment market continues

The demand for residential real estate and portfolios rose considerably again in the year under review. At € 18.7 billion, the financial year under review exceeded the previous year by nearly 19 per cent, thus recording the second-best result of the previous ten years. Market activity was defined largely by smaller transactions. Portfolios with fewer than 800 units accounted for more than 90 per cent of turnover, with a total volume of just under € 10 billion. The transactions featured only four portfolios with more than 4,000 residential units. Pension schemes and special funds executed mainly medium-sized and smaller transactions in the last year, thus reporting asset generation of € 4.9 billion together with public housing enterprises. Housing developers sold approximately 20,000 apartments worth nearly € 5.0 billion, which represents an increase of 40 per cent over 2017. A large part of this growth is a result of price increases observed on the market. The commercial residential investment market is dominated by national investors; less than one quarter are foreigners. Foreign activities thus did not reach the previous year's volume in 2018, but were more or less in line with the levels seen in the last five years.

Rental development reflects demand

Strong demand for the commercial real estate markets impacted on rental development once again in 2018. There was no end in sight to the growth path for office and residential real estate rentals, despite a slight dip in growth rates. In the retail segment, however, top rents stagnated. This was due to what was already a high rental level and to the growing significance of online trading, which is putting pressure on growth in inner-city retail business despite the favourable consumption conditions.

Demand for office space remains unchanged

Because of the stable economic environment and rising employment related to this, demand for office space remained high across Germany's seven prime locations during the 2018 financial year. Yet, given the level of demand for office space, construction activity for new office space was decidedly muted. Because vacant and difficult-to-rent office properties were also converted into residential or hotel real estate, vacancy rates have fallen further and rents have risen.

The lowest vacancy rates in the year under review were measured in Munich and Berlin, with 1.5 and 1.7 per cent respectively, followed by Stuttgart with 2.2 per cent. The figure in Hamburg came to 3.6 per cent, whilst Dusseldorf's vacancy rate was much higher at 6.8 per cent. Frankfurt had the highest rate of 7.6 per cent. On average, top rents for the seven prime locations increased by 4.4 per cent in 2018. The highest rate of growth was recorded in Berlin with 11.6 per cent, followed by Cologne with 4.8 per cent and Hamburg with 3.8 per cent. Owing to the demand for office properties arising from Brexit, the international financial centre of Frankfurt maintained its lead, with top office rents of € 39.50 per square metre, over the long-standing runner-up, Munich, with € 37.20 per square metre. Berlin, which was still comparatively cheap a few years ago, was the third-most expensive location in Germany for office properties in 2018, with a top rent of € 33.50 per square metre.

Retail rents persist at a high level

The boost in consumption brought about by the macroeconomic conditions impacted on retail trade in the seven prime locations. Nevertheless, there was no further increase in top rents, which are already at a very high level thanks to the long-standing popularity of prime locations in Germany's metropolitan areas. This is compounded by the change in consumer buying behaviour, where the focus is no longer exclusively on physical shopping. As a result, especially chains in the textile sector are placing their bet on smaller branch networks, with smaller shop sizes. Even though retail turnover has been on an upswing for years, growth is primarily attributable to e-commerce, and not to stationary retail. Accordingly, the share of pure sales areas is falling, while the importance of gastronomic concepts in particular is growing.

This development led to a widespread stagnation of rental development: for the first time since 2004, inner-city retail rents are going down, albeit marginally. Top rents per square metre ranged from € 245 in Stuttgart and € 255 in Cologne to as much as € 345 in Munich at the end of 2018. At € 282 and € 285 respectively, Dusseldorf and Hamburg were slightly below the average rent for prime locations of € 289 per square metre. Frankfurt's top rent of € 300 in the year under review was roughly on par with the average. At € 310, Berlin is Germany's second most expensive retail location. Only Dusseldorf saw top rents increase marginally in 2018, namely by 0.7 per cent. At the other five prime locations, they remained at the consistently high level of the previous year.

Residential construction once again fails to keep up with demand

The population of Germany's prime locations increased for the fifth time in succession. As a result, the demand for housing continued to increase. Despite a significant upturn, the current level of construction activity is still falling considerably short of the number of new homes (approximately 400,000 apartments) that need to be built every year. Between January and November 2018, approvals across Germany were granted for 315,200 apartments, corresponding to growth of 0.5 per cent year-on-year. In addition, approvals for single-family homes and duplexes showed a downward trend (-0.5 per cent and -5.2 per cent, respectively). Thus, the increase was solely due to apartments in multi-family homes with a rise of 4.5 per cent. As a result, the gap between demand and supply is becoming wider and wider. The situation is exacerbated by the trend towards single-person households. Intensive residential construction is being hampered by a lack of land zoned for building and capacity shortages in the construction industry. What is more, the apartments being built tend to be at the luxury end of the market, exacerbating the bottlenecks in affordable housing, which are more pronounced overall. The housing industry is tackling this issue, by offering affordable housing far below average existing rents at prime locations.

Residential rents are rising at a comparatively moderate pace

In the year under review, residential rents rose again in all prime locations, albeit with varying degrees of momentum. The average first-occupancy rent rose by 4.1 per cent to € 14.80 per square metre in 2018. The increase in Dusseldorf, however, was only moderate, at 0.8 per cent. First-occupancy rents grew at a somewhat faster pace in Hamburg and Frankfurt – at 2.2 per cent and 2.6 per cent. In Cologne, the rate of increase rose by 4.0 per cent. Rent increased at a much greater pace in Berlin, with 8.0 per cent, and in Stuttgart with 9.0 per cent. On average, rents of € 12.90 per square metre had to be paid for first occupation in Dusseldorf in 2018. Cologne and Berlin were only slightly more expensive with € 13.00 and € 13.50 respectively. Rents in Hamburg with € 14.20 and in Stuttgart with € 15.80 were around the average of the prime locations. At € 15.50, rents in Frankfurt exceeded the average, while Munich was ahead by a large margin at € 19.00. The average rent for renewals in the prime locations grew a little more slowly in 2018, by 3.7 per cent to € 12.60 per square metre, which is, among other things, a result of institutional restrictions (limited rental increases) in the portfolio. On average, the absolute difference between first-occupancy and re-rental rents amounts to € 2.30 per square metre. It is highest in Berlin (€ 3.20), whilst Cologne is on the lower end of the range with € 1.50.

Prices on the housing markets rise again

Persistently low interest rates and stable economic development once again ensured high demand on the

German residential property market in 2018. Against this background, prices for both commercially-managed multi-family homes as well as for purchases of owner-occupied apartments have risen again. On the whole, year-on-year price increases for residential real estate across Germany have, however, been muted. Whilst price momentum in owner-occupied apartments still amounts to 8.9 per cent, thus lying slightly below the previous year's level of 10.9 per cent, single-family homes and terraced houses have a decline to show for (5.3 per cent and 7.4 per cent, respectively; 2017: 7.6 per cent and 8.3 per cent, respectively).

The upward trend is stronger in the metropolitan areas, larger conurbations, and university cities. As such, the price of owner-occupied apartments increased by 8.8 per cent in the seven largest German cities in 2018, starting at what was already a high level in the previous year. Prices in other cities also rose, by between 8 and 9 per cent. Re-urbanisation tendencies and low interest rates remained a key driver here, making even expensive city apartments affordable for buyers, and motivating investors to switch from the capital markets into the real estate market.

Municipalities in better financial shape

Bolstered by higher tax revenues, the coffers of Germany's municipalities were well in the black, with a financing surplus of just under € 800 million in the first half of 2018*). At around € 123.5 billion, the revenues generated by local authorities and associations of local authorities were up by 4.8 per cent on a year earlier. Expenditure came to € 122.7 billion, rising by 4.7 per cent in the first half of 2018, i.e. at almost the same pace as revenue. Municipal debt totalled € 135.5 billion.

While disparities between municipalities in individual federal states and within one and the same federal state became slightly less pronounced in the first half of 2018, they persisted nonetheless. This was due to quantitative additional demand that was left unsatisfied due to demographic development (rising numbers of children and school pupils), unmet additional demand due to rising quality standards (air quality and the move to more climate-friendly transport policies), as well as capacity and exogenous effects (construction prices). The deleveraging and consolidation programmes already in place in several federal states, such as the pact aimed at strengthening city finances (Stärkungspakt Stadtfinanzen) in North Rhine-Westphalia, started to bear fruit in the first half of 2018 and illustrate the high level of system support and predictability in Germany. In this environment, the credit quality of German municipalities can be considered solid.

*) Data for 2018 as a whole was not yet available at the time the report was prepared.

Sources: Jones Lang LaSalle, bulwiengesa, IVD Immobilienverband Deutschland, Destatis

DEVELOPMENT OF RESIDENTIAL REAL ESTATE PRICES* IN GERMANY

Percentage change compared to 2017

* Existing properties, medium residential value

Source: IVD-Wohn-Preisspiegel 2018 | 2019

Siegfried Schneider, Head of Back-Office Treasury & Public Sector | Markus Krampe, Head of Public Sector

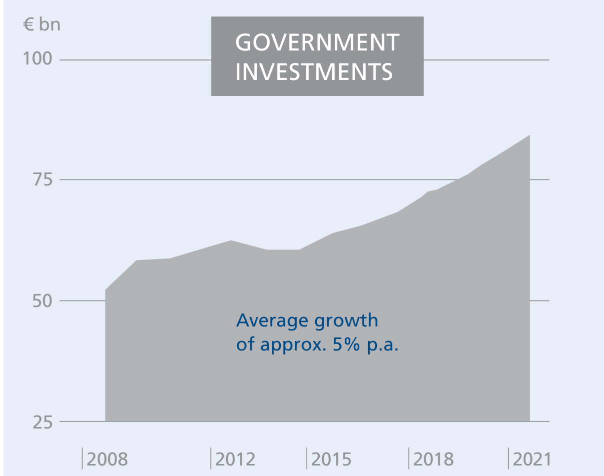
THE PUBLIC SECTOR DIVISION

REDUCING THE INVESTMENT BACKLOG

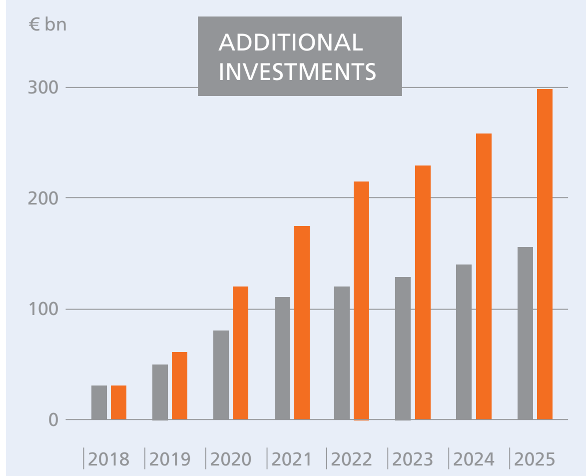
Increasing number of infrastructure projects

The persistent low-interest rate environment in Germany and the continued high tax revenues allow for a gradual reduction of the municipal investment backlog. Within this context, infrastructure projects are crucial. This not only applies to the expansion of roads, railway networks and water routes, but also investments in institutions necessary for a functioning community – including not only the aforementioned traffic facilities, but also communication networks, energy and water supply, waste disposal, and social institutions for education, safety, health, and culture. The newly constructed police station in Melsungen is an example of a successfully implemented municipal infrastructure project. Within the scope of a Public/Private Partnership (PPP), the federal state of Hessen has won a private partner for the planning, construction and management of the building over a contractual period of 30 years. Once the contract expires, the federal state will become the owner of the property. The new building adheres to the cutting-edge energy standards in Hessen, but it was also built according to the current specialised standard required of a Hessen police station, with high-quality technical equipment.

FUTURE INVESTMENT REQUIREMENTS: PUBLIC-SECTOR INVESTMENTS ARE RAPIDLY INCREASING



Database: German Federal Statistical Office, February 2017; 2017–2021: Ministry of Finance projections
Source: German Federal Ministry of Finance



Estimated volume of additional investments required to achieve the targets set in Germany

Scenario 1: increase in investment rate
Scenario 2: additional investments to close the gap

Source: Ernst&Young

© Landesbetrieb Bau und Immobilien Hessen (LBIH)

The construction of the new police station in Melsungen is supported by DZ HYP as financing partner.

» The investment backlog of the past years is burdening many municipalities. DZ HYP thus also sees its specialist range of services as a contribution to securing public-sector services of general interest. The Bank advises and accompanies public-sector clients in financing infrastructure projects – together with its partners, the local cooperative banks. «

MARKUS KRAMPE, HEAD OF PUBLIC SECTOR

© Landesbetrieb Bau und Immobilien Hessen (LBIH)

BUSINESS DEVELOPMENT

Credit Business

Strong development in the real estate and municipal business

In a climate characterised by persistently low interest rates and a stable economy, the demand for real estate remained high in 2018. DZ HYP worked together with its partners and clients, intensively and successfully, in this environment. The volume of new business in DZ HYP's Commercial Real Estate Investors, Housing Sector, and Retail Customers/Private Investors segments totalled € 10,970 million (2017: € 10,129 million*)). Including public-sector lending, the Bank originated new business of € 11,864 million (2017: € 10,894 million) in its four segments in 2018. Key factors in the Bank's success include its business model, which is geared towards sustainability and has a long-term focus, and its cooperation with its partners and clients in a relationship based on trust.

Higher new business generated with commercial real estate investors

DZ HYP's Commercial Real Estate Investors business showed encouraging development, despite the challenging competitive environment. At € 7,725 million (2017: € 7,105 million), the Bank's new business volume was up year-on-year. The German core market accounted for € 7,420 million, in line with the Bank's strategic focus. To avoid cyclical peaks in the portfolio, DZ HYP generally continued to apply its conservative risk strategy with strict quantitative targets for its financing decisions in the year under review. The consolidation and harmonisation of the merged banks' previous credit risk strategies, the increased alignment with the cooperative banks' business model, and the further development of regulations for core real estate, all led to moderate adjustments. Besides carrying out a comprehensive qualitative analysis of properties and location, including stress testing, the quality of the client relationship is essential.

DZ HYP maintained a high level of cooperation within the Cooperative Financial Network in the area of Commercial Real Estate Investors. Joint lending business with the cooperative banks totalled € 3,451 million in 2018 (2017: € 3,559 million). This stable development shows that commercial real estate finance – as part of the corporate client business in the Cooperative Financial Network – continues to attract considerable interest from amongst banks. DZ HYP cooperates with around 360 cooperative banks in this area of business on a regular basis.

DZ BANK's real estate finance business transferred to DZ HYP

As part of the process of consolidating the business activities of the Cooperative Financial Network, a decision was made in 2017 to bundle the commercial real estate financing business absorbed from WGZ BANK in the course of the merger with DZ BANK, at DZ HYP. The real estate finance portfolio was originally sized at around € 2.6 billion and the process of gradual transfer to DZ HYP started at the end of 2017, with a scheduled completion date at the end of 2020. Following the completion of extensive project work in the year under review, a total of nine commitments with a loan repayment sum of € 96.5 million were successfully transferred to DZ HYP by December 2018.

Commitment volume in the housing sector up year-on-year

In the housing sector business, the competition again moved up a notch in 2018 due to the increasing range of market participants. Nevertheless, DZ HYP also reported successful development in this business area in the year under review. Despite the fierce competition, the commitment volume slightly exceeded the solid € 975 million witnessed in the previous year, coming in at € 1,013 million in 2018. In particular, the Bank provided long-term financing for investment projects focusing on new construction and modernisation measures. The ongoing commitment to cultivating existing customer relationships, as well as the successful acquisition of new customers in the regional market areas, contributed to this development. In addition, the Bank successfully continued its collaboration with the cooperative banks in the spirit of trust and partnership.

*) The previous year's figures on the business development refer to the merged institution.

Growth achieved in the retail customer business

Within the Volksbanken Raiffeisenbanken Cooperative Financial Network, real estate financing with retail customers and private investors is of key importance as a high-quality anchor product. DZ HYP believes this business area makes an important contribution to strengthening cooperation and customer acquisition within the Cooperative Financial Network. Customer demand for long fixed-interest periods remained stable in the 2018 financial year, supported by the ongoing low interest rates. Thanks to the good refinancing options available to it, DZ HYP is in a position to provide financing at favourable conditions over long fixed-interest periods. While the cooperative banks often provide real estate loans with fixed-interest periods of up to ten years using their own funds, a very large portion of the long-term intermediated business in the segment covering fixed-interest periods of between 10 and 30 years is placed with Pfandbrief banks such as DZ HYP.

Business with retail customers and private investors is still attracting a growing number of intermediary partners within the Cooperative Financial Network. This provides the basis for the successful new business figures that DZ HYP achieved in private real estate lending in the year under review. The Bank achieved a year-on-year increase in the volume of new commitments in this division to € 2,232 million (previous year: € 2,049 million). The volume of new commitments (retail customers) intermediated via the core banking procedures of the Cooperative Financial Network and the Genopace and Baufinex network portals also increased to € 1,468 million (previous year: € 1,436 million). The volume of new commitments in the business with private investors also contributed to the positive development seen in the financial year under review, with new business of € 764 million (previous year: € 613 million). This means that DZ HYP once again achieved good results, also taking the challenging competitive landscape into account.

Local authority lending business expanded

DZ HYP is the centre of competence for business with public-sector clients in the Cooperative Financial Network. In this function, it supports cooperative banks in developing business with domestic local authorities as well as their legally dependent operations, which are serviced across Germany. DZ HYP originated new business with a volume of € 894 million in loans to local authorities during the period under review (previous year: € 765 million), of which € 639 million (previous year: € 561 million) was intermediated by cooperative banks and € 255 million (previous year: € 204 million) was originated through direct business. 84 per cent of all transactions in this business area were intermediated by cooperative banks. This includes € 108 million (previous year: € 53 million) in short-term public-sector loans.

Reduction of non-strategic portfolios

DZ HYP's non-strategic portfolio comprises the portfolio of mortgage-backed securities (MBS) and the non-strategic part of the sovereign/bank securities portfolio; in particular Portugal, Italy and Spain. The primary objective is to run the portfolio down carefully. In the second half of 2018, the non-strategic portfolio was wound down further as a result of repayments and maturities – from € 5 billion as at 30 June 2018 to € 4.7 billion as at 31 December 2018. DZ HYP will continue to adhere to these strategies and the resulting portfolio reduction.

VR WERT

VR WERT, a wholly-owned subsidiary of DZ HYP, performed well during the 2018 financial year: for the first time in the company's history, revenues made it into the double digit millions at € 10.0 million (previous year: € 9.8 million), with around 2,600 expert valuations performed.

Refinancing

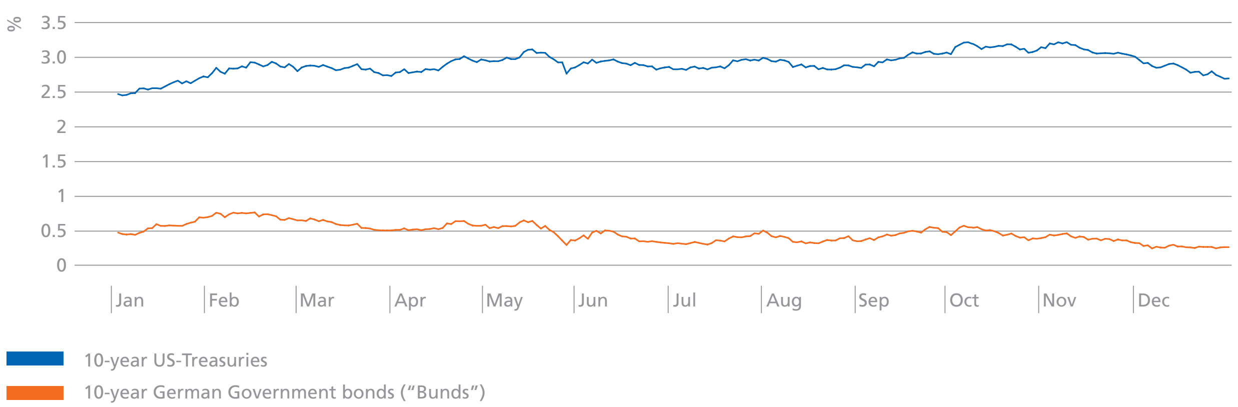
ECB's withdrawal pushes refinancing premiums up

The capital markets environment in the 2018 financial year was influenced to a considerable degree by the ECB's monetary policy withdrawal from the bond markets, political factors such as the preparations for Brexit, the parliamentary elections in Italy and subsequent budget disputes with the EU, as well as trade conflicts between the world's major economies. These factors led to increased volatility on the capital markets.

In particular, the changes announced in 2017 to the ECB's buying behaviour as part of its bond purchase programme (CBPP III – Covered Bond Purchase Programme) had a lasting impact on the market for covered bonds. As of spring 2018, the Eurosystem started to gradually reduce its order volume in the primary market. At its monetary policy meeting in June, the ECB announced that it would be concluding its asset purchase programme at the end of 2018, as was to be expected. The ECB's withdrawal from the market in the form of a gradual reduction in order volumes led to lower demand for bonds and was reflected in significantly higher refinancing premiums for issuers – particularly from the second half of 2018 onwards. At the last central bank meeting of the year in December, the ECB Governing Council decided to end its net asset purchase programme at the end of 2018 – as expected. Furthermore, the ECB emphasised its intention to reinvest maturities even after the first interest rate hike. In addition, key interest rates in the euro area are to be kept at their present levels at least through the summer of 2019.

In contrast to the euro area, the US Federal Reserve raised its key interest rate in four steps, by 25 basis points in each case, over the course of 2018 in response to the positive economic situation and rising inflation. This steady cycle of interest rate hikes resulted in rising US yields, which dipped towards the end of the year as economic scepticism started to set in. In the euro area, on the other hand, the ten-year German government bond yield fluctuated between 0.6 and 0.3 per cent in the course of the year after climbing to over 0.8 per cent at the beginning of 2018. Towards the end of the year, the climate was dominated by numerous risk factors, prompting many investors to invest in safe German government bonds and putting yields on a downward trend again.

10-YEAR GERMAN GOVERNMENT BOND YIELDS AND US-TREASURIES



Sources: Datastream, DZ BANK Research

In this market environment, the 2018 financial year saw very lively issuance activity on the covered bond market. 96 issuers were responsible for a total of 173 new issues and taps with a volume of € 136.6 billion on the market for publicly placed euro benchmark covered bonds – an increase of 21.3 per cent as gainst the previous year. This issue volume was largely absorbed by investors from Germany and Austria, followed by buyers from the Benelux countries and French investors.*)

DZ HYP Pfandbriefe enjoy sustained demand

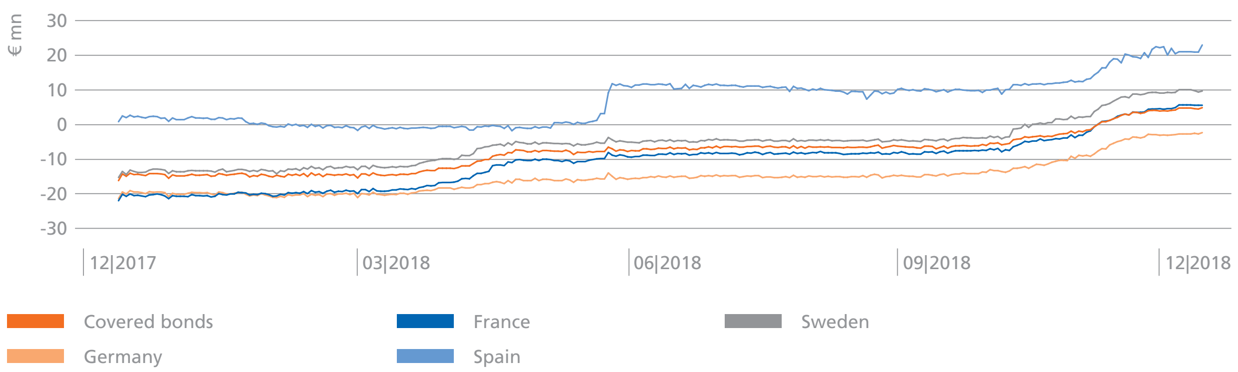
In 2018, the year of the merger, DZ HYP issued covered bonds totalling € 4.1 billion**). € 2.8 billion of this amount was attributable to publicly placed euro benchmark bonds, with € 1.0 billion attributable to DG HYP and € 750 million to the former WL BANK, as measured up until the merger date. The first DZ HYP benchmark issue of € 1.0 billion was successfully placed in early November following the launch of the "new" issuer on the market at a roadshow. The covered bonds in benchmark format are all Mortgage Pfandbriefe.

Private placements generated a total volume of € 1.4 billion with investors, with Mortgage Pfandbriefe accounting for € 1.3 billion of new issuance, and Public Pfandbriefe for € 140 million. As at the 2018 balance sheet date, DZ HYP Pfandbriefe with a total volume of € 44.1 billion were outstanding (previous year: € 44.2 billion), with € 28.9 billion attributable to Mortgage Pfandbriefe (previous year: € 27.3 billion).

DZ HYP generated most of its unsecured funding of € 5.1 billion using issues within the Cooperative Financial Network. The total volume of unsecured funding amounted to € 22.2 billion as at the year-end (previous year: € 21.8 billion).

*) Source: DZ BANK Research
**) Excluding € 500 million in short-term issues for the purpose of participating in Deutsche Bundesbank's long-term refinancing transactions

FUNDING SPREADS FOR 5-YEAR COVERED BONDS (SPREADS OVER SWAPS, IN BASIS POINTS)



Sources: DZ BANK Research, Markit

THE RETAIL CUSTOMERS/PRIVATE INVESTORS DIVISION

ACHIEVING ENERGY EFFICIENCY WITH LOW INTEREST RATES

Climate protection enhances attractiveness of real estate

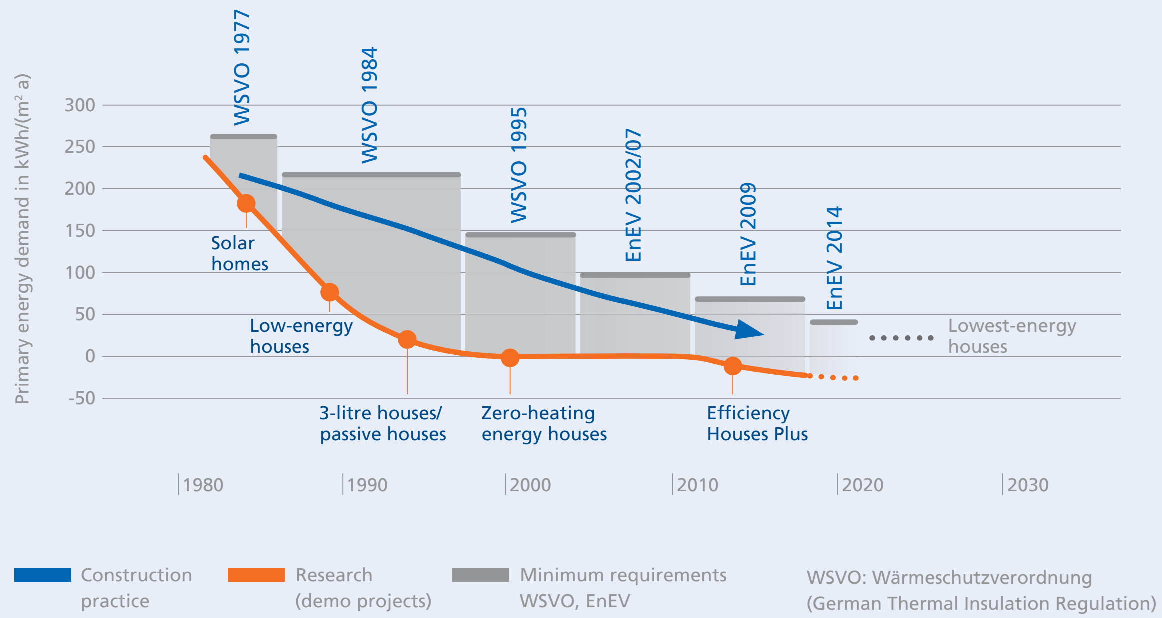
Thomas Plum, Head of Retail Customers & Relationship Manager Cooperative Banks | Markus Wirsen, Head of Back-Office Housing Sector, Private Investors & Retail Customers

Nowadays, energy-efficient construction is the rule rather than the exception. Stricter rules – which over the last 40 years have led to a much lower permissible level of primary energy use in new single-family homes are not the only reason. The reality is that construction practice also now focuses on energy saving, often widely exceeding legal requirements. Today, more than half of newly constructed housing adheres to the Efficiency House 55 standard. Passive houses and energy-generating buildings are also now regularly part of many developments.
The current low-interest rate environment offers builder-owners particularly good options to make their dream of a climate-friendly and energy-efficient own home come true. In the long term, this saves money (despite higher construction costs), since only around 3 per cent of the entire budget is allocated to higher energy-saving requirements when building new single-family homes.
In addition, investing in climate change sustainably reinforces the value stability of the property. Many interested parties exploit the opportunity to build future-proof in the current environment, resulting in a win-win situation for developers, municipalities (by allocating construction lots for climate-friendly new construction) and the environment.

Efficiency House Plus residential area in Friedberg/Hügelshart, a construction project by asset bauen wohnen gmbh

PRIMARY ENERGY DEMAND OF A SINGLE-FAMILY HOME

Primary energy demand development of single-family homes in the last decades. The lower curve documents exemplary research projects, the upper curve the legal minimum requirements. Innovative construction practice moves between these levels.



WSVO: Wärmeschutzverordnung (German Thermal Insulation Regulation)
EnEV: Energieeinsparungsverordnung (German Energy Saving Regulation)

Source: Fraunhofer Institute for Building Physics (IBP)

» Responsibility is an important value in cooperative home loan financing. Local cooperative banks are able to provide their customers with good advice when it comes to climate-friendly construction. We support the banks with efficient processes and sustainable financing solutions. «

THOMAS PLUM, HEAD OF RETAIL CUSTOMERS & RELATIONSHIP MANAGER COOPERATIVE BANKS

NET ASSETS, FINANCIAL POSITION AND FINANCIAL PERFORMANCE

Net Assets

DZ HYP's total assets increased slightly in the 2018 financial year, by € 0.8 billion, to € 75.9 billion, largely driven by the portfolio of real estate loans, which showed a gratifying € 2.8 billion increase to € 45.3 billion. The Commercial Real Estate Investors portfolio increased by € 2.3 billion to € 23.8 billion – mainly as a result of the surprisingly high new business volume – whereas the real estate finance portfolio of Retail Customers/Private Investors (€ 13.3 billion) remained more or less on the same level with a slight decrease of € 0.1 billion, and the Housing Sector division generated a portfolio increase of € 0.5 billion to € 8.2 billion.

In originated local authority lending, the Bank's investment strategy continues to focus on supporting the cooperative banks in this line of business, whilst ensuring a balanced risk/return profile. New business originated during 2018 fell short of ongoing repayments, as expected, thus reducing the portfolio by € 0.7 billion to € 11.8 billion.

Furthermore, the public finance portfolio declined by a further € 0.4 billion, to € 12.6 billion during the year under review, as a result of maturities and repayments; this was in line with the Bank's strategy. The portfolio of bank bonds was also reduced by € 0.1 billion, to € 0.6 billion. Exposures to countries and banks that are particularly affected by the debt crisis have developed as follows (details excluding MBS):

	Sovereigns*)		Banks		Total	
Nominal amounts € mn	31 Dec 2018	01 Jan 2018	31 Dec 2018	01 Jan 2018	31 Dec 2018	01 Jan 2018
Spain	1,396	1,592	260	260	1,656	1,852
Italy	1,681	1,702	–	–	1,681	1,702
Portugal	750	750	–	–	750	750
Total	3,827	4,044	260	260	4,087	4,304

*) including state-guaranteed corporate bonds and sub-sovereign entities

DZ HYP did not hold any public-finance exposures vis-à-vis Ireland and Greece, or bonds issued by banks in these countries. Loans and advances to banks exclusively consisted of covered bonds.

In 2018, the election of Europe-critical parties in Italy and the ongoing Brexit discussion marked the political environment in Europe, leading, amongst other things, to significantly wider credit spreads in Italian bonds. Even after the Italian government came to an agreement with the EU Commission on the planned new debt level, the spreads continue to be many times higher than that of German bonds. Further north, an agreement regarding a controlled exit of the United Kingdom from the EU has yet to be reached. In the event of a potentially critical development it can be assumed that the ECB will implement stabilising measures on the capital markets within the scope of its monetary policy.

Excluding derivatives hedges taken out within the scope of overall bank management, the hidden burdens for DZ HYP's securities (excluding MBS) that are treated as fixed assets totalled € 40.9 million as at 31 December 2018 (01/01/2018: € 51.4 million). This contrasts with undisclosed reserves in the amount of € 1,099.3 million (01/01/2018: € 1,362.4 million). Taking into account the net effects from hedges within the context of the overall management of the Bank, hidden burdens from this securities portfolio amounted to € 802.3 million (01/01/2018: € 750.2 million). Following a comprehensive assessment of these securities, DZ HYP has concluded that none of the securities are permanently impaired.

There have been no new investments in mortgage-backed securities (MBS) since mid-2007. The portfolio in this business area, which is being phased out, was reduced by € 0.2 billion to € 0.5 billion during the 2018 financial year, especially as a result of ongoing repayments, sales and exchange rate fluctuations. MBS holdings are intensively monitored by means of a detailed risk management system, regular analyses of individual exposures, and comprehensive stress testing. The development of material risk factors has confirmed the stabilisation of this non-strategic portfolio, which has been ongoing for several years now. Undisclosed reserves on the MBS portfolio totalled € 0.1 million on the reporting date (2017: € 0.8 million). Hidden burdens on this exposure in the amount of € 37.7 million (2017: € 37.6 million) predominantly reflect market illiquidity and stricter regulatory capital requirements. In this respect, DZ HYP anticipates a write-back over the remaining term of the MBS portfolio.

Overall, DZ HYP's credit portfolio was increased by 1.9 per cent during the 2018 financial year.

DEVELOPMENT OF LENDING VOLUME

			Change from the previous year	
€ mn	31 Dec 2018	01 Jan 2018	€ mn	%
Mortgage loans*)	45,289	42,510	2,779	6.5
Originated loans to local authorities**)	11,789	12,479	-690	-5.5
Public-sector lending***)	12,608	12,992	-384	-3.0
Bank bonds****)	571	723	-152	-21.0
MBS	542	745	-203	-27.2
Total	70,799	69,449	1,350	1.9

*) Mortgage loans including short-term loans collateralised by real property liens
**) Lending business with direct liability of German local authorities or their legally dependent operations
***) Securities issued by national governments and sub-sovereign entities as well as state-guaranteed corporate bonds
****) Securities issued by banks

DZ HYP's financial position is sound.

Regulatory capital

DZ HYP has used the so-called waiver option provided under section 2a of the German Banking Act (Kreditwesengesetz – "KWG"; old version) with effect from the reporting date of 31 December 2012. In accordance with section 2a (1), (2) and (5) of the KWG (as amended) in conjunction with section 6 (1) and (5) as well as section 7 of the EU Capital Requirements Regulation (CRR), the provisions of parts 2-5, as well as parts 7 and 8 of the CRR, do not need to be applied by DZ HYP on an individual basis, but are covered at DZ BANK Group level instead. However, DZ HYP will continue to make use of the regulatory capital requirements for internal management purposes. Since no comparative figures exist for the merged institution as at 1 January 2018, the key equity figures are only presented as at the reporting date of 31 December 2018.

	31 Dec 2018
Own funds (€ mn)	2,276
Total capital ratio (%)	13.3
Tier 1 ratio (%)	10.4
Common equity tier 1 ratio (%)	9.0

To further strengthen common equity tier 1 capital, in coordination with DZ BANK, DZ HYP agreed to allocate a material portion of the profit generated in the 2018 financial year to the fund for general banking risks pursuant to section 340g of the HGB.

Financial Position

Within the scope of liquidity management, DZ HYP differentiates between the ongoing liquidity management and structural funding. Appropriate management systems are in place for both types of liquidity. Liquidity management takes into account and complies with the limits of the internal liquidity risk model, DZ BANK's liquidity risk model, and the regulatory risk requirements.

» Ongoing liquidity management aims to guarantee a reliable and continuous provision of liquidity at all times. Given DZ HYP's integration in the Cooperative Financial Network and its affiliation with DZ BANK, DZ HYP consciously refrains from maintaining an independent market presence for the purposes of short-term liquidity management, which is carried out in close coordination with DZ BANK. Due to its central bank function within the Cooperative Financial Network, DZ BANK raises cash and cash equivalents of various maturities, and applies the funds raised within its Group. Within this Group liquidity management framework, subsidiaries such as DZ HYP may call upon funding from DZ BANK. This is based on closely coordinated, regular risk reporting about future changes to the liquidity position.

» Structural funding is exposed to the risk that, due to various influencing factors, the Bank might be unable to maintain the required funding levels, and that in certain circumstances, debt may not be sufficiently available in the desired maturities. As a Pfandbrief issuer, DZ HYP is licensed to issue Pfandbriefe. This licence is the foundation for covered funding, and thus provides a safe and cost-efficient way to raise liquidity. DZ HYP maintains its own market presence as a Pfandbrief issuer, placing Pfandbriefe with investors within as well as outside the Cooperative Financial Network.

The cash flow statement, published as part of the financial statements within this annual report, shows the changes in cash flows from operating activities, as well as from investing and financing activities, for the financial year under review and the previous year.

DZ HYP's liquidity situation is adequate.

Financial Performance

DZ HYP's financial performance continued to reflect a successful operating performance in real estate finance in 2018. Once again, stable net interest income was accompanied by reversals of write-downs. Significant amounts could be allocated to general risk provisions, whilst preserving the forecast profit transfer.

In its financial management and operational as well as strategic planning, DZ HYP measures the Bank's profitability using the financial performance data shown in the following table and derived from accounting under HGB, as well as the cost-income ratio and return on equity.

OVERVIEW OF THE PROFIT AND LOSS ACCOUNT

			Change from the previous year	
€ mn	**2018**	2017*)	€ mn	%
Net interest income	523.5	480.8	42.7	8.9
Net commission result	-27.4	-15.6	-11.8	-75.6
Administrative expenses	294.2	227.8	66.4	29.1
Net other operating income/expenses	7.9	-2.6	10.5	>100.0
Risk provisioning)**	-68.7	-22.8	-45.9	>-100.0
Net financial result*)**	38.5	69.4	-30.9	-44.5
Operating profit	**179.6**	**281.4**	**-101.8**	**-36.2**
Allocation to the fund for general banking risks	45.0	100.2	-55.2	-55.1
Taxes	63.3	89.9	-26.6	-29.6
Partial profit transfer	16.3	16.1	0.2	1.0
Profit transfer	55.0	75.2	-20.2	-26.9

*) Aggregate figures of the individual institutions
**) Equates to the income statement line items "write-downs and valuation allowances of loans and advances and specific securities, as well as additions to loan loss provisions"
***) Equates to the income statement line items "income from write-ups to participating interests, shares in affiliated companies and securities held as fixed assets"

Net interest income

DZ HYP's net interest income of € 523.5 million in 2018 was a welcome € 42.7 million higher than the previous year's figure (2017: € 480.8 million). The increase in the average strategic real estate loan portfolio in particular has a positive effect. In addition, the Bank realised a € 11.7 million premium payment from an open-market transaction with Deutsche Bundesbank, for the first time. The stable development of net interest income is evidence of DZ HYP's successful management of its banking book, which is geared towards generating long-term, matched-maturity margins.

NET INTEREST INCOME IN DETAIL

€ mn	2018	2017
Interest income	2,003.1	2,066.2
Interest expense	1,482.3	1,587.7
Current income from participations	0.2	0.1
Income from profit pooling, profit transfer, and partial profit transfer agreements	2.5	2.2
Net interest income	523.5	480.8

Net commission result

The net commission result of € -27.4 million was down € 11.8 million on the comparable figure for the previous year of € -15.6 million. At the same time, € 20.9 million (2017: € 29.4 million) in commission income was generated from the lending business, which depends both on the respective product mix and disbursement. Moreover, € 45.1 million (2017: € 43.4 million) was paid for brokerage services from cooperative banks within the Cooperative Financial Network.

Administrative expenses

Administrative expenses, being the total of general administrative expenses (€ 289.2 million; 2017: € 223.5 million) and write-downs on intangible assets and tangible fixed assets (€ 5.0 million; 2017: € 4.3 million), were up by € 66.4 million in the 2018 financial year, clearly exceeding the previous year's figure of € 227.8 million. Personnel expenses of € 97.2 million were up € 12.2 million year-on-year, largely due to additions to pension provisions of € 6.0 million, inter alia, due to the deployment of new life tables, together with costs for new hires and one-off payments within the scope of a restructuring programme.

Consultancy costs for the implementation of the merger, which will continue to burden our finances far into 2019, resulted in expenses of € 60.6 million, i.e. an increase of € 41.5 million compared to the previous year (2017: € 19.1 million). Due to the progress made in this project, we are now assuming that expenses within this context will decrease.

The bank levy due for 2018 amounted to € 25.3 million – € 2.7 million higher than the previous year's figure of € 22.6 million. As in the previous year, the 85 per cent / 15 per cent rule was applied for the 2018 payment of contributions, so that a further € 4.5 million of the total contribution of € 29.8 million was deposited with Deutsche Bundesbank as cash collateral, in addition to the aforementioned € 25.3 million.

Net other operating income/expenses

Net other operating income and expenses, as the balance of the two income statement line items explained below, rose by € 10.5 million, from € -2.6 million to € 7.9 million. Other operating income of € 28.0 million materially exceeded the previous year's figure of € 21.6 million, mainly due to a reversal of provisions of € 6.6 million, whilst other operating expenses dropped, from € 24.2 million to € 20.1 million. The main driver behind this reduction is the addition to provisions carried out in the previous year to cater for a potential impact from the German Federal Court of Justice decision on customer rights.

Risk provisioning

DZ HYP's risk provisioning amounts to € -68.7 million (2017: € -22.8 million). Another positive result in the lending business (€ 9.9 million; 2017: € 24.6 million) compares to a negative result in the securities business of € -41.3 million (2017: € 66.5 million) and additions to the reserves pursuant to section 340f of the HGB. In the 2018 financial year, no material specific allowances were recognised in any of the four strategic segments. At the same time, specific loan loss provisions and portfolio-based allowance for credit losses were reversed, thanks to recoveries in the loan portfolio, improvements of collateralisation, and lower probabilities of default. Furthermore, the first-time application of IFRS 9 led to a net positive earnings effect in the amount of € 3.6 million, which is mirrored in risk provisioning in accordance with German commercial law. In order to offset potentially higher loan defaults in future downturns, in coordination with DZ BANK, DZ HYP decided to offset the positive loan loss provisioning balance in 2018 by means of a significant allocation to general risk provisions pursuant to section 340f of the HGB. The negative securities result mainly comprises expenses arising from the early redemption of Registered Pfandbriefe with the aim of managing the cover assets pools, and from the cancellation and measurement of own bonds taken back in the amount of € -36.7 million.

Net financial result

The net financial result fell from € 69.4 million in 2017 to € 38.5 million in 2018. It mainly includes net income of € 36.1 million from the sale of securities held as fixed assets, which is related to the redemption of Registered Pfandbriefe and promissory note loans, within the scope of managing the cover assets pools. The revaluation result (net) for the MBS portfolio amounted to € 1.3 million (2017: € -2.9 million).

Operating profit

Operating profit reflects DZ HYP's performance in its core business, and is used for the internal management of the operating divisions. Material non-recurring effects related to the risk exposures, as well as varying allocations to general risk provisions and the merger expenses, make it difficult to draw an annual comparison of DZ HYP's operating result. However, even despite the fact that operating profit of € 179.6 million (2017: € 281.4 million) was burdened by the material transfer to reserves pursuant to section 340f of the HGB, the figure once again significantly surpassed the Bank's projections.

Cost/income ratio

The cost/income ratio (CIR) expresses the ratio of administrative expenses (including other operating expenses) to the aggregate of net interest income, net commission result, and other operating income. The CIR serves as a yardstick for the efficiency of commercial activities, as well as an internal management parameter. Reflecting a lower level of non-recurring effects, the CIR of 60.0 per cent rose by 8.2 percentage points from 2017's 51.8 per cent.

Change in the fund for general banking risks

During the 2018 financial year, based on reasonable commercial assessment, € 45.0 million (2017: € 100.2 million) was allocated to the special item for general banking risks pursuant to section 340g of the German Commercial Code (HGB), to take account of particular risks facing the business area.

Taxes

Taxes must be determined on a stand-alone basis under the existing tax compensation agreement between DZ BANK and DZ HYP. Taxes amounting to € 63.3 million (2017: € 89.9 million) were allocated to DZ HYP. This includes a € 78.2 million income tax expense from tax allocations (2017: € 89.3 million) as well as an offsetting, non-recurring tax income of € 18.7 million incurred within the scope of the merger and reported under income taxes. Other tax expenses of € 3.7 million (2017: € 0.4 million) related in particular to non-recurring real estate taxes payable for the properties in Münster, due to the merger.

Profit transfer

DZ HYP allocated a partial profit of € 16.3 million (2017: € 16.1 million) to its silent partnerships – slightly higher than in the previous year, reflecting interest rate developments. After taxes, profits of € 55.0 million (2017: € 75.2 million) will be transferred to the owner, DZ BANK, in accordance with the distribution policy agreed with DZ BANK.

Return on equity

The return on equity (RoE) relates net income before taxes and allocation to general risk provisions to the average invested equity (funds from the portfolio of the year under review and the previous year). RoE of 11.5 per cent in the year under review clearly exceeded expectations.

Overall, DZ HYP's economic situation has thus stabilised at a comfortable level during the 2018 financial year. The Bank's robust financial performance is the result of a rigorously pursued business and risk strategy, whereby an accelerated build-up of hidden reserves and general risk provisions, combined with an absence of any obvious risks in the target business, has provided the basis for a sound financial position and performance, based on a viable business model.

STRUCTURE OF CIR COMPONENTS

€ mn	2018	2017*)
Administrative expenses	294.2	227.8
Other operating expenses	20.1	24.2
Total relevant expense items	314.3	252.0
Net interest income	523.5	480.8
Net commission result	-27.4	-15.6
Other operating income	28.0	21.6
Total relevant income items	524.1	486.8

*) Aggregate figures of the individual institutions

COMPOSITION OF NET INCOME BEFORE TAXES AND ALLOCATION TO GENERAL RISK PROVISIONS

€ mn	2018	2017
Net income before profit transfer	55.0	75.2
Allocation to general risk provisions pursuant to section 340f of the HGB	37.2	-19.1
Allocations to the fund for general banking risks pursuant to section 340g of the HGB	45.0	100.2
Tax expense on income	59.7	89.5
Net income before taxes and allocations to general risk provisions	196.9	245.8

CALCULATION OF AVERAGE INVESTED EQUITY

€ mn	2018	2017 (1 Jan 2018)	2016 (aggregate)
Share capital	150.0	150.0	175.4
Capital reserves	884.2	884.2	742.2
Retained earnings	93.1	93.1	209.7
General risk provisions pursuant to section 340f of the HGB	159.4	122.1	141.2
Fund for general banking risks pursuant to section 340g of the HGB	467.0	422.0	321.8
Equity	1,753.7	1,671.4	1,590.3
Average invested equity	1,712.6	1,630.9	

TOGETHER TOWARDS THE FUTURE

After intensive preparations, DZ HYP celebrated Day 1

Tartan tracks in the foyers, newly hoisted flags, and fresh new script for the façades: in broad sunshine, both DZ HYP head offices were ready for Day 1 on 27 July.

The months before the merger were extremely busy, with numerous employees putting in very long hours indeed. At the end of July the day had finally arrived: two became one. Despite ongoing merger work, Management Board and employees took the time to celebrate Day 1.

DZ HYP had organised employee receptions at both head offices in Hamburg and Munster. The focus of the events was on panel discussions with the Management Board. Under the slogan "Close. Together. Successful – Dialogue with the Management Board", the Board members talked about experiences gained in the merger process, and answered questions from the audience. They particularly emphasised the opportunities arising as a result of the merger. The Management Board also took advantage of the events to thank the employees for their hard work.

The labour-intensive integration processes have not yet been completed, and continue to claim a large number of resources within DZ HYP. The employee receptions however offered the opportunity to take a moment in the middle of day-to-day operations, and to jointly look back at what had been achieved.

REPORT ON OPPORTUNITIES, RISKS AND EXPECTED DEVELOPMENTS

REPORT ON OPPORTUNITIES

In addition to the opportunities already described in the Economic Report resulting from a real estate market environment that remains fundamentally positive, the merger of DG HYP and WL BANK that was completed in the year under review, to form the leading real estate bank and Germany's largest Pfandbrief issuer, has created specific opportunities for DZ HYP. In addition to risk diversification and the bundling of forces within the cooperative financial network, DZ HYP expects to achieve significant synergies as a result of avoiding duplicate investments. Furthermore, savings are expected to be achieved by bundling and standardising existing areas of expertise, structures and processes of the predecessor institutions. These savings will be offset by short-term merger expenses, although a large portion of these expenses has already been incurred in the past, mainly in 2018.

As a subsidiary of DZ BANK, DZ HYP is a member of the Cooperative Financial Network – a network characterised by a high degree of solidity, strong credit quality, and high liquidity through customer deposits. The broadly diversified market position of the Cooperative Financial Network forms a strong basis for DZ HYP to finance business, with a view to risks and returns.
DZ HYP will continue to use this ability to act in the future, jointly with the German cooperative banks, as a reliable financing partner to its clients.

In its projections, DZ HYP defines opportunities as positive unexpected deviations from the financial performance expected for the next financial year. The key factors determining value for the financial performance in this context (value drivers) were included in the forecast, as planning assumptions. Specifically, opportunities exist in the form of sources of income identified therein exceeding projections, or expenses remaining below projections. DZ HYP once again used these opportunities to its advantage during the 2018 financial year. In particular, risk costs and tax expenses were significantly lower than projected, meaning that, with income levels that were more or less on target, net income for the year before profit transfer outstripped the forecast overall.

Managing opportunities

Exploiting business opportunities whilst observing target returns is an integral part of DZ HYP's enterprise management system. The activities driven by the Bank's business model require the ability to identify, measure, assess, manage, monitor and communicate opportunities.

DZ HYP's opportunities management is integrated into DZ BANK Group's annual strategic planning process. Strategic planning allows the identification and analysis of trends and changes to the market, and to the competitive environment; it forms the basis for assessing potential opportunities. Reports submitted to the Management Board on opportunities arising from future business development, as derived from the business strategy, are based on the results of the strategic planning process. Staff are informed about potential opportunities identified in the course of communicating the business strategy.

Non-financial reporting

The German CSR Directive Implementation Act, which came into force in 2017, requires affected companies to issue a Non-Financial Statement covering various non-financial performance aspects, and to supplement their Corporate Governance Statement with a diversity concept. The Act has thus regulated reporting on certain sustainability-related topics for the first time. The objective of the EU Corporate Social Responsibility (CSR) Directive is to enhance transparency and promote discussion of social and ecological aspects of companies. Specifically, this requires the disclosure of information on environmental, social and employee aspects, on the respect for human rights, and the fight against corruption and bribery.

DZ HYP is included into the Non-Financial Statement of DZ BANK AG Deutsche Zentral-Genossenschaftsbank, Frankfurt am Main, and thus is exempt from issuing its own Non-Financial Statement. The consolidated Non-Financial Statement has been published in the chapter "Non-Financial Statement" in DZ BANK's Group Annual Report 2018, and can be downloaded from www.berichte2018.dzbank.de (in German only).

RISK REPORT

Under its former company name "DG HYP", in November 2012 DZ HYP notified the German Federal Financial Supervisory Authority (BaFin) and Deutsche Bundesbank that it would use the waiver pursuant to section 2a (2) of the German Banking Act (KWG, as amended at the time), with respect to the provisions of sections 10, 13 and 25a (1) sentence 3 no. 1 of the KWG. DZ BANK Group continued to make use of this waiver rule, which was incorporated into Article 7 of the CRR, and pursuant to which – provided certain conditions are met – the supervision of individual institutions domiciled in Germany within a group of institutions may be performed by the Group's supervisor, for DZ HYP during the 2018 financial year. DZ HYP continues to apply the waiver, with the objective of securing DZ HYP's integration into the risk management of DZ BANK Group. As a result, DZ HYP is not required to comply with the requirements set out in parts 2 to 5, 7 and 8 of the CRR on a single-entity level.

To qualify for the waiver, DZ HYP must be closely integrated into DZ BANK Group management processes, both through DZ BANK Group's committee structure and IRKS, the Group's integrated risk and capital management system which defines Group-wide standards for risk measurement and risk reporting. In the context of this integration, and for the purposes of the waiver, economic and regulatory capital adequacy is being monitored, ascertained and disclosed at the level of DZ BANK Group. The procedures established to safeguard the Bank's ability to secure adequate liquidity, from an economic as well as regulatory perspective, are outlined in the "Liquidity risk" chapter below.

DZ BANK's Group Management Report is in line with German Accounting Standard No. 20; to this extent, the specifications of DZ BANK's Group-wide risk management system can also be applied to DZ HYP. Against this background, DZ HYP performs a risk reporting system that is in line with the requirements of a subordinated entity.

Within the scope of the merger of DG HYP and WL BANK, numerous activities were initiated, including those designed to converge and harmonise the processes, methods and IT systems deployed in risk management. This included adjusting the risk strategies in place to date, the Risk Strategy Framework as well as the Risk Appetite Statement to the requirements of the merged Bank; the Management Board adopted these documents, effective from the date of the merger. Moreover, the merger was taken into consideration for strategic and operational planning for the 2018 financial year and beyond. Thanks to these measures, key elements of the risk management system were harmonised. DZ HYP's Management Board received the first report on the economic adequacy of DZ HYP as the merged institution, in terms of liquidity and capital, in the third quarter of 2018.

The migration of business data inventories from the IT systems of former WL BANK to DZ HYP's IT systems, which commenced in the previous year, is being continued during the 2019 financial year. Key IT systems will be run in parallel to some extent until migration has been completed. The combination of risk positions, which is associated with the migration, will be concluded during the 2019 financial year, as planned.

Risks

Risks arise from unexpected adverse developments for the net assets, financial position and performance. Key risks for the financial performance of DZ HYP exist in the form of value drivers for income falling short of, or risk costs exceeding projections. In particular, DZ HYP's net assets, financial position or financial performance may be adversely affected by counterparty credit risk – which is why continuous risk monitoring of the portfolios is indispensable.

I) Objectives of risk management

Risk management at DZ HYP is an integral part of the strategic and operative management of the Bank as a whole. Assuming risks in a targeted and controlled manner, observing target returns, is an element of enterprise management within the DZ BANK Group, and hence, also within DZ HYP. The activities driven by DZ HYP's business model require the ability to identify, measure, assess, manage, monitor and communicate risks. In addition, maintaining an adequate level of equity backing for risk exposure is fundamentally important as a prerequisite for the Bank's continued operation. As a guiding principle for all business activities carried out by DZ BANK Group – and hence, also by DZ HYP – risk is as-sumed only to the extent required to achieve business policy objectives, observing the mission statement, and provided that the Bank has an adequate understanding and expertise for measuring and managing the risks assumed.

To implement this principle, DZ HYP's Management Board has defined a Risk Appetite Statement, which is in line with Group guidelines. DZ HYP defines risk appetite as the type and scope of risk an institution is willing to assume in order to implement its business model and achieve its business objectives, within the framework of its risk-bearing capacity. Essentially, this is determined by the maximum loss threshold defined by DZ BANK Group, the Liquidity Coverage Ratio, and the minimum level of excess liquidity.
Based on the risk policy guidelines and the business strategy, a Risk Strategy Framework was prepared, and risk strategies were determined for the material risks the Bank is exposed to. Each of these risk strategies comprises the business activities exposed to risk, the risk management objectives (including provisions concerning risk acceptance and avoidance), and the measures designed to achieve these objectives. These strategies were newly developed in the context of the merger, and discussed with the Supervisory Board.

a) Responsibilities

The regulatory organisational requirements and the allocation of risk management responsibilities are set out, in particular, in the Minimum Requirements for Risk Management (Mindestanforderungen an das Risikomanagement – "MaRisk") and the German Regulation on Remuneration in Financial Institutions (Institutsvergütungsverordnung – "InstVergV"). DZ HYP considers these requirements, adapting its relevant processes to the specific needs of its business model and considering the specific requirements to the Group waiver. DZ HYP has also developed and implemented a risk management and risk control framework that fulfils the needs arising in the market and competitive environment, as well as the requirements arising from the Bank's integration in the DZ BANK Group. This forms the basis that ensures the proper operation and efficiency of the risk management process.

DZ HYP has assigned the relevant tasks to the following bodies and committees:

Supervisory Board

The entire Supervisory Board decides on personnel matters and remuneration of the Management Board, the Rules of Procedure and Schedule of Responsibilities for the Management Board. The Supervisory Board also decides on transactions requiring approval, such as the acquisition or disposal of participating interests in the event of changes exceeding € 500,000 in the carrying amount of such interests, the conclusion of rental or lease contracts involving annual rent or lease payments exceeding € 500,000 as well as on the establishment or disposal of business lines, establishing branches and representative offices, the purchase, disposal or charges of property assets, and on material issues related to loans or participations that are not explicitly assigned to the Risk Committee of the Supervisory Board. The Bank's strategic and operational planning are also presented to the Supervisory Board. To fulfil its duties, the Supervisory Board has constituted the following committees from amongst its members: a Risk Committee, an Audit Committee, as well as committees for personnel matters (Nomination Committee and Remuneration Oversight Committee).

Risk Committee

The Risk Committee is responsible for risk management. In addition, the Supervisory Board has assigned responsibility for the Bank's risk appetite statement and the risk strategies derived therefrom (in accordance with MaRisk) to the Risk Committee. The Committee advises the plenary meeting of the Supervisory Board on the Company's current and future total risk appetite, and supports the Supervisory Board in monitoring implementation of this strategy by the Bank's top management.

The Risk Committee monitors whether terms and conditions for client business are in line with the Company's business model and risk structure. Where necessary, the Committee requests proposals and monitors their implementation. The Committee verifies whether the incentives created by the remuneration system take the Company's risk, capital and liquidity structure into account, as well as the probability and timing of income. It also determines the type, scope, format and frequency of information on strategy and risks, to be submitted by the Management Board. The Committee accepts the Management Board's reports concerning risk exposure, participations and credit issues, analyses them and reports material findings to the plenary meeting of the Supervisory Board.

Moreover, pursuant to the MaRisk, the Risk Committee is one of the recipients of reports to be submitted to the supervisory body in the event of ad-hoc reporting that may be required. The Committee is also responsible for decision-making regarding those loan exposures, portfolio transactions and participating interests that – in line with the Internal Rules of Procedure – do not fall within the remit of the Management Board. Due to the utilisation of the Group waiver, decisions regarding large exposures (as defined in section 13 of the KWG) are the responsibility of DZ BANK's entire Board of Managing Directors.

Audit Committee

The Audit Committee's monitoring duties include, in particular, the accounting and financial reporting process, the effectiveness of the risk management system, the audit of the financial statements, as well as the independence of the external auditors. The Committee supervises the rectification of any deficiencies identified by the external auditors. Furthermore, the Supervisory Board has nominated the Audit Committee as the recipient of quarterly reporting in accordance with MaRisk. The Committee is also responsible for the approval of certain agreements related to the Bank's IT systems, and for instructing the external auditors with any tasks outside the scope of auditing.

Nomination Committee

The Nomination Committee supports the Supervisory Board; its tasks include identifying candidates for appointment to the Management Board, assessing the structure, size composition and performance of the Management Board and the Supervisory Board. Specifically, this entails appraising the skills, professional aptitude and experience of individual members of the Management Board and the Supervisory Board.

Remuneration Oversight Committee

The Remuneration Oversight Committee monitors whether remuneration systems for the Management Board and for the Bank's employees are appropriate – particularly for those employees whose activities have a material impact on the Bank's overall risk profile, and for the heads of Risk Controlling and Compliance. The Committee supports the Supervisory Board in monitoring whether remuneration systems for the Bank's staff are appropriate, and in assessing the impact of remuneration systems on the management of risk, capital and liquidity. Furthermore, the Remuneration Oversight Committee prepares the Supervisory Board's resolutions concerning the remuneration for members of the Management Board.

Management Board

The Management Board – as the highest decision-making body – is responsible for the internal management of DZ HYP. Management Board resolutions are taken during weekly meetings. Concerning DZ HYP's risk governance, the Management Board has the sole power of representation and management authority, in accordance with sections 77 and 78 of the German Public Limited Companies Act (Aktiengesetz – "AktG"). The Management Board is the central body responsible for managing and monitoring risks of the entire Bank at a portfolio level, as well as for the allocation of risk capital. The Management Board decides upon individual loan exposures in line with its lending authority. The Management Board also decides upon the strategy to be adopted for asset/liability management, and determines the Bank's liquidity costs to be taken into account for its lending business. Accordingly, the heads of front-office and back-office departments, as well as the heads of Finance and Risk Controlling, take part in Management Board meetings.

In addition, DZ HYP is integrated into the committee structures of DZ BANK Group and the Cooperative Financial Network, where DZ HYP's Management Board members or other employees are represented.

b) Functions

Risk Planning

Planning, as a bank-wide exercise, comprises the planning of income and costs, as well as the risks associated with DZ HYP’s individual business activities. Within this planning process, risk limits and earnings projections are determined, taking into consideration the risk-bearing capacity of DZ BANK Group. Due to the use of the waiver option, resolutions on risk limits are passed by the Board of Managing Directors of DZ BANK.

Risk Management

A 'three lines of defence' model has been established for the structural organisation of the risk management and control framework. This model clearly differentiates responsibilities between the various units, and addresses potential conflicts of interest. The first line of defence is the operative management in the front-office units. The units involved are responsible for recognising risks at an early stage, assessing them and implementing suitable measures, taking the existing framework conditions into account. The second line of defence is responsible for establishing and developing risk management standards. It also monitors compliance with these standards by the first line of defence, and submits corresponding reports to the Management Board and the Supervisory Board. As the third line of defence, and independent of individual processes, Internal Audit examines and assesses risk management and risk control processes employed by the first and second lines of defence. In this capacity, the third line of defence reports directly to the Management Board, the Supervisory Board, and the Audit Committee.

Risk Controlling
Within the second line of defence, the departments within the Chief Risk Officer's area of responsibility assume a special role in terms of risk management and risk control. This applies especially to Risk Controlling, which assumes overarching responsibility for identifying, measuring, assessing, managing and limiting risks, as well as for risk monitoring and communication.

The purpose of the annual risk inventory carried out within the DZ BANK Group is to identify the relevant types of risk the DZ BANK Group is exposed to, and to assess their materiality. Where required due to specific events, the Group also performs a risk inventory during the course of a financial year, to be able to recognise any material changes to the risk profile where necessary. A materiality analysis is carried out for any types of risk that may occur in principle, given the business activities of DZ BANK Group entities. In a next step, all types of risk classified as material are evaluated as to what extent risk concentrations exist.

Credit risk, market risk, liquidity risk, operational risk, investment risk, reputational risk, as well as business risk have been identified as material for DZ HYP. These types of risk are explained in sections II to VII. With the exception of liquidity risk, economic capital – referred to as the risk capital requirement – is determined for these types of risk; for risk types measured by DZ BANK, the so-called risk contribution is used accordingly. Exposure to reputational risk is mapped to business risk.

Risk is generally determined using a value-at-risk (VaR) figure based on a one-year holding period and a confidence interval of 99.90 per cent. To account for types of risk for which capital requirements cannot yet be (sufficiently) determined, the Bank has set aside a capital buffer. As soon as adequate measures to quantify such risks become available (and the exposure can be included in the risk capital requirement or risk contribution, respectively), it will be possible to release this buffer.

In contrast to the other types of risk, economic capital is not allocated for liquidity risk: this is because the allocation of aggregate risk cover will not prevent an imminent insolvency. Methods and procedures used for managing liquidity risk are outlined in section III b).

Within the framework of an annual suitability check, the suitability of risk measurement methods for all risk types classified as material is examined. Measures are taken to adjust the management toolbox where necessary. Risk inventories, suitability checks and the capital buffer process are harmonised in terms of content and timing.

Risk Controlling is responsible for ongoing reporting and – together with back-office units – for monitoring risk on a portfolio level. Credit Risk Controlling is responsible for quantifying the risk capital requirement, using a credit portfolio model to determine Expected Loss (EL) and Credit Value-at-Risk (CVaR) on a monthly basis. For this purpose, default probabilities required are mapped using CRR-compliant ratings to the extent possible. In principle, Expected Loss is determined by mapping probability of default and expected loss severity, after the realisation of collateral. Expected losses on the level of individual transactions are incorporated into the calculation parameters for new business, in order to prevent a creeping erosion of capital. Key factors used to determine credit risk, employing the credit portfolio model, are lending volume, concentration effects (relative to sectors, countries, or counterparties), eligible collateral, and the credit quality structure of the portfolio. Measurement captures default risk from the lending business as well as trading activities. The risk capital requirement determined in this way (plus any capital buffer required) is compared to the maximum loss threshold for credit risk, and is being monitored.

An Overall Risk Report is prepared on a monthly basis; in accordance with MaRisk requirements, this report comprises a presentation of the Bank's aggregate risk situation, the material types of risk, as well as the regulatory and economic capital adequacy. The Overall Risk Report is discussed by the Management Board on a monthly basis; it is discussed by the Supervisory Board and the Risk Committee on a quarterly basis. The Report is also submitted to Heads of Division of DZ HYP and DZ BANK. Furthermore, Risk Controlling also carries out daily risk reporting and limit monitoring on the market risks and existing liquidity risks to which DZ HYP is exposed, in accordance with MaRisk. These reports are submitted to the Management Board, the units involved in managing the Bank, and DZ BANK; in addition, the key findings are regularly reported to the Supervisory Board, or to the Risk Committee of the Supervisory Board.

Internal Audit
As an independent unit, Internal Audit examines whether the demands on the internal controlling systems, the risk management and risk controlling systems, and the necessary reporting, are adequately met.

Compliance
DZ HYP's Compliance Office reports directly to the Management Board. The Compliance Office combines the compliance function in accordance with the MaRisk and the German Securities Trading Act (WpHG): it serves as the Central Unit for the prevention of money laundering and fraud, and holds responsibility for data protection, IT security, and business continuity planning. The Compliance Office has sufficient resources in order to fulfil its various tasks. For the purposes of MaRisk compliance, the Bank has established a Compliance Board (comprising members of the Management Board and Division Heads) as well as a Compliance Committee (comprising representatives from the divisions). During the course of regular meetings, the existing legal monitoring is reviewed; views and opinions concerning Compliance issues and risks are exchanged whenever needed.

c) Ongoing regulatory developments

In close cooperation with DZ BANK, DZ HYP analyses and evaluates the requirements resulting from ongoing regulatory developments. Given the classification of DZ BANK as an institution with systemic relevance on a national level, the ECB assumed the direct supervision of DZ BANK and the DZ BANK Group in November 2014. Therefore, DZ HYP generally has to comply with regulatory requirements for "significant" institutions. In particular, DZ BANK Group – and hence, DZ HYP – must comply with the "Principles for effective risk data aggregation and risk reporting" (BCBS 239), published in January 2013 by the Basel Committee on Banking Supervision. Besides requirements for the organisational structure and workflows of banks' risk management function, these rules – which were incorporated into the MaRisk in October 2017 – also include specific regulatory requirements concerning the IT architecture and data management in banks. DG HYP and WL Bank already and individually launched corresponding implementation projects, in 2015 and 2016 respectively, and combined these projects during the course of the merger. All steps taken to implement the requirements under BCBS 239 are being closely coordinated with DZ BANK's activities in this context. DZ HYP is also looking at new requirements concerning outsourcing and risk culture, which were also published as part of the MaRisk amendments in October 2017.

The focus during the year under review was additionally on requirements under CRR II/CRD V, which include new regulations regarding the interest rate risk in the banking book (IRRBB), the Leverage Ratio and the NSFR. Furthermore, a project was launched to prepare for new regulatory requirements concerning the definition of default, as well as the estimation of risk parameters in the IRBA, which will come into force in 2021. DZ HYP also implemented requirements from the Guidelines on Connected Clients, as well as from the German Regulation on the Creditworthiness Assessment for Real Estate Loans to Consumers (Immobiliar-Kreditwürdigkeitsprüfungsleitlinien-Verordnung – "ImmoKWPLV"). Implementation of the ECB Non-Performing Loans Guideline (including supplementary regulatory expectations regarding risk provisioning) is ongoing, in coordination with DZ BANK.

d) Requirements pursuant to section 27 of the German Pfandbrief Act

DZ HYP's risk management and risk control framework fulfils all requirements under section 27 of the German Pfandbrief Act (Pfandbriefgesetz – "PfandBG"). The TXS-Pfandbrief application is used to determine the market risk exposure of cover assets pools, based on a coverage concept using present values, as set out in the Present Value Cover Regulation ("PfandBarwertV") promulgated by BaFin. Stress scenarios simulating the impact of standardised interest rate shocks on the present value of cover assets pools are used to quantify the market risk exposure.

BaFin has prescribed some structural parameters for these interest rate shock scenarios, as well as for the maximum impact these scenarios may have on the present value of the cover assets pools. A report on the present values and DZ HYP's liquidity status is prepared on a daily basis and submitted to Treasury.

In addition, a quarterly report, which covers the more extensive PfandBG requirements regarding historical and future performance and credit risk exposure of the cover assets pools, is submitted to the Management Board.

Internal rules regarding the commencement of business in new products or markets comply with the requirements of the MaRisk as well as with those under section 27 of the PfandBG.

e) Internal control and risk management system related to the financial reporting process

As an issuer of publicly-traded securities (as defined in section 264d of the HGB), DZ HYP is obliged, pursuant to section 289 (4) of the HGB, to outline the key features of the internal control and risk management system it has implemented with regard to the financial reporting process.

Organisation
DZ HYP's accounting and financial reporting system is predominantly assigned to the Finance division (which is independent from the business divisions); it comprises financial accounting and asset accounting. Securities accounting as well as loan accounting are assigned to the various back-office units within DZ HYP. Payroll administration has been outsourced to ZALARIS Deutschland AG, Henstedt-Ulzburg.

Strategy
The internal control and risk management system implemented for the accounting process consists of accounting-related and other control objectives. Accounting-related control objectives are designed to ensure the proper functioning and reliability of internal and external accounting and financial reporting systems. Key objectives in this context are the completeness and accuracy of documentation, timely recording, the reconciliation of balances across the IT systems used, and compliance with accounting rules. Other control objectives relate to ensuring the efficiency of business activities as well as to compliance with applicable laws and regulatory requirements related to accounting and financial reporting.

Integrated business process control mechanisms have been installed, in order to fulfil the strategy outlined above. This includes checks of completeness and accuracy, applying the principle of dual control. Errors are also mitigated through the separation of functions, access restrictions, work instructions, and plausibility checks. The bank regularly draws upon support by external experts for implementing new legal regulations. New product processes always require evidence, prior to the launch of a new product, that the new product can be implemented in the accounting and financial reporting system, in an orderly manner that is in line with applicable rules. Internal Audit regularly carries out process-independent checks concerning accounting and financial reporting.

Overall, the Bank has implemented a control and risk management system with regard to the financial reporting process. This system comprises measures to identify and assess material risks (and related risk mitigation measures) to ensure the proper preparation of the financial statements.

II) Credit risk

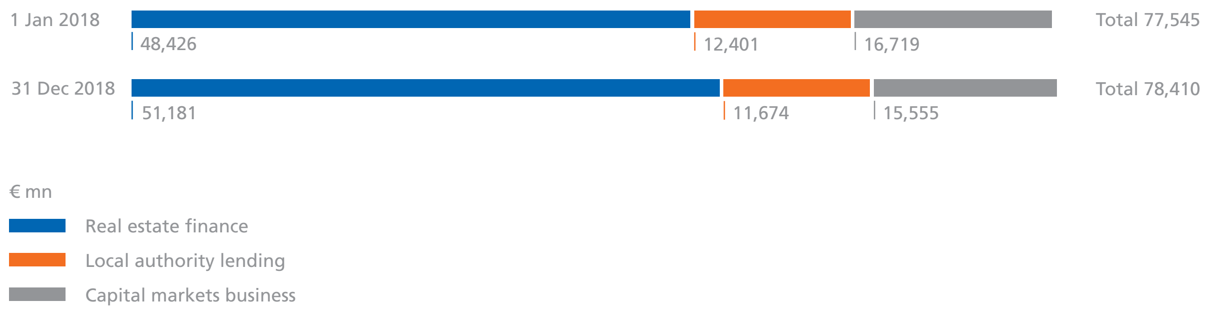
Credit risk is defined as the risk of losses incurred as a result of the default of counterparties (borrowers, issuers, other counterparties) or guarantors as well as from impairment due to a decline in creditworthiness of borrowers or by market turbulence. Both traditional lending business (real estate finance and local authority lending, including financial guarantees and loan commitments) as well as capital markets activities may be exposed to credit risk. In the context of credit risk, capital markets activities relate to products such as securities, promissory note loans (Schuldscheindarlehen), derivative and money market transactions.

Credit risk in real estate finance and local authority lending is defined as the risk that a client is unable to settle claims arising from loans taken out by him and due claims for payments or the risk of losses from contingent liabilities and committed credit lines.

Credit risk from capital markets activities is distinfurther guished, into replacement risk and issuer risk, for example. Replacement risk from derivatives is defined as the risk of a counterparty defaulting during the term of a transaction (with a positive market value), in which case DZ HYP would have to incur only additional expenditure (equivalent to this market value, at the time of default) in order to enter into an equivalent transaction with another counterparty. Issuer risk denotes the threat of losses from the default of issuers of tradable bonds or losses from the default of underlying instruments of derivatives (such as credit derivatives).

DZ HYP's lending volume increased by 1 per cent in the 2018 financial year, to € 78.4 million. Real estate lending is predominantly collateralised by land charges and mortgages (98 per cent). The following chart breaks down lending volume by DZ HYP's three types of business:

LENDING VOLUME BY BUSINESS DIVISION



a) Lending process

The front and back offices for the real estate finance business are located in DZ HYP's decentralised Real Estate Centres; for certain client groups, these functions are at DZ HYP's head offices in Hamburg and Münster. Key workflow stages include the credit rating, which is identified using rating procedures that comply with the CRR, and also client, property and project assessments. In this context, DZ HYP benefits from the client proximity of advisors and surveyors, as well as from the Bank's integration into the Cooperative Financial Network. The loan application is authorised on the basis of lending volume and risk classification, observing the separation of functions prescribed by MaRisk.

Market coverage, credit analysis and the processing of exposures in local authority lending and capital markets business are centralised in Hamburg and Münster, and are being handled by specialist front-office and back-office teams. Likewise, the existing portfolio of mortgage backed securities (MBS) is also looked after centrally in Hamburg by a specialist back-office department. The bank no longer enters into new business in this type of product.

b) Limit system

DZ HYP has limit systems in place for the internal management and monitoring of credit and country risks, thus ensuring compliance with the strategic requirements of DZ HYP and the DZ BANK Group. Treasury has access to the respective limits and their utilisation at any time, for the purposes of intraday monitoring. Back-office units monitor the utilisation of individual business partner and country limits on a daily basis, as part of their monitoring processes, and initiate escalation procedures in the event of any limit transgressions. These procedures are designed to restore limit compliance, or to approve transgressions, in line with delegated authority, taking the strategy adopted by DZ HYP/ DZ BANK Group into account.

c) Credit rating

As an IRBA institution, DZ HYP complies with regulatory requirements regarding methods, process flows, management and monitoring procedures as well as data recording and data processing systems used in the credit business in order to measure and manage risks.

The rating environment was expanded to include further procedures used by former WL BANK during the course of the merger. Also within the framework of the merger, rating systems are being systematically harmonised and incorporated, in line with a schedule agreed upon with the regulators, in order to ensure that going forward, DZ HYP will continue to employ tailor-made rating procedures matching the risk profiles of various client groups. ECB has approved the rating systems for the purpose of calculating equity requirements under the Foundation IRB approach; they safeguard an adequate assessment of counterparty credit risk and support internal management. Models are developed and validated in line with DZ BANK's requirements; rating procedures are validated at least once a year.

For real estate financings, these rating procedures adequately incorporate the special characteristics of commercial and residential real estate developers, commercial housing enterprises, special purpose entities, commercial and private real estate investors, as well as open-ended and closed-end real estate funds and retail customers, considering the specific risks involved.

Given its extensive real estate expertise, DZ HYP has assumed the lead – within the Cooperative Financial Network – for the conception, regular maintenance and development of rating procedures for commercial real estate finance in Germany. In this context, the Bank is also responsible for compliance with CRR standards, which the ECB monitors regularly, in its capacity as supervisor. Having been approved by the regulatory authority, these rating procedures fulfil the highest standards; thanks to this high quality level, the procedures are also employed by numerous cooperative banks.

DZ HYP also offers CRR-compliant rating procedures – whose IRBA eligibility was approved during the course of regular supervisory audits – for other client segments, such as banks, sovereigns, or large SMEs. DZ BANK is responsible for methodological development regarding these segments, whereby the National Association of German Cooperative Banks (BVR) is also involved. DZ HYP regularly validates the adequacy of these procedures for its own portfolios, by way of internal validation processes.

DZ HYP also applies a CRR-compliant rating procedure to assess the credit quality of local authorities. Given the regulatory exemption for capital requirements concerning exposures to European local authorities, no regulatory approval is required here.

Due to cost/benefit considerations, for a low number of special cases, DZ HYP applies a simplified rating procedure where no IRBA approval has been applied for.

A breakdown of DZ HYP's total lending volume by type of business and by rating class is provided below:

LENDING VOLUME*) BY RATING CLASS

€ mn	Total 31 Dec 2018	Total 1 Jan 2018	Real estate lending as at 31 Dec 2018	Loans to local authorities 31 Dec 2018	Capital markets business 31 Dec 2018
Investment grade (rating class 2A or better)	**73,243**	72,481	47,743	11,672	13,828
Non-investment grade (rating classes 2B-3E)	**4,952**	4,805	3,365	2	1,585
Defaulted rating classes (4A or worse)	**126**	144	72	–	54
Unrated	**89**	115	1	–	88

*) including disbursement commitments

A new rating is prepared for each client at least once a year, or on an event-driven basis.

d) Intensified handling and management of problem loans

DZ HYP uses an individual risk management system ("ERM") for the purposes of early warning, in a similar way as employed by the parent company DZ BANK. Cases with early warning indicators are assigned to a so-called 'yellow list'. Loans with regard to which a subsequent loss cannot be excluded are kept on a 'watch list'. Where there is a clear negative trend, coupled with an existing requirement for recognising specific risk provisions, the cases are included on the 'default list', which also includes all exposures subject to recovery without specific provisions required.

The processing rules and requirements on the transfer from one ERM list to another are subject to defined criteria. Exposures which are subject to an ongoing threat of elevated risk remain within the responsibility of staff within the respective division, whereby the centralised intensified handling team is also involved. Problem loans that are judged to have a favourable outlook are passed on to the Restructuring department for further processing. As a basis for a restructuring decision, a concept is submitted that must comprise a differentiated analysis and assessment of the overall situation of the exposure and a cost-benefit analysis, as well as usually a comprehensive restructuring plan. Loan exposures are transferred to work-out if restructuring has failed or if this is deemed to be fruitless from the outset. A detailed report on problem exposures is submitted to the Management Board on a monthly basis.

Non-performing loans are managed using the following indicators:

- » the NPL ratio (defined as the share of non-performing loans in total lending volume);
- » the provisioning ratio (defined as the share of aggregate provisions for loan losses and loss allowance in total lending volume); and
- » the risk coverage ratio (defined as the share of aggregate provisions for loan losses and loss allowance in aggregate non-performing loans).

Selected indicators used for internal management of credit risk developed as follows during the year under review:

CREDIT RISK INDICATORS

€ mn	Total 31 Dec 2018	Total 1 Jan 2018	Change in %
Lending volume*	**78,410**	77,545	1.1
NPL volume	**126**	144	-12.5
NPL ratio (%)	**0.2**	0.2	-
Loss allowance	**211**	180	17.2
Provisioning ratio (%)	**0.3**	0.2	50.0
Risk coverage ratio (%)	**168**	125	34.4

*) including disbursement commitments

e) Provisions for loan losses / loss allowance

The Bank has accounted for all identifiable credit risks, in accordance with prudent commercial judgement, by recognising provisions in the amount of expected losses. Provisions for loan losses comprise write-downs and provisions for credit risks and inherent default risks, for all receivables carried on the balance sheet as well as for off-balance sheet transactions.

Specific provisions are recognised when the Bank has reason to doubt the performance of a receivable, due to the difficult financial circumstances of a borrower, or in the event of insufficient collateralisation; or if there are indications that the borrower will be unable to pay interest on a sustainable basis. The same applies to contingent receivables. Specific provisions must be recognised in accordance with the requirements of German commercial law, especially observing the principle of prudence.

Regarding the calculation of specific provisions, DZ HYP was generally required to use different methods for the sub-portfolios of former DG HYP and WL BANK. DZ HYP is currently working at streamlining the calculation methods, which will be continued throughout 2019. There are no material differences between the different methods, in terms of the amounts of risk provisions determined. At both locations, existing receivables (including any pro-rata interest and pending items) are compared to revalued collateral as at the valuation date; the uncovered portion determined in this way is written down in full. The inventory of specific provisions is regularly monitored; reports are submitted to the Management Board as part of the monthly ERM reporting package and the quarterly risk report for the Bank as a whole.

Portfolio loss allowances and provisions for loan commitments as at 31 December 2017 were measured in line with expected 12-month credit losses, in accordance with IAS 39. Since 1 January 2018, this measurement was changed to the stage concept pursuant to IFRS 9, whereby the Bank recognises loss allowance in the amount of 12-month expected credit losses for lending transactions where credit risk has not increased significantly compared to a defined threshold value since initial recognition (stage 1 lending transactions), and in the amount of lifetime expected credit losses for lending transactions where credit risk has increased significantly compared to the defined threshold value since initial recognition (stage 2 lending transactions). The new loss allowance accounting policy was designed to provide the reader of financial statements with a more accurate, fair and true view of the assets and liabilities of the Bank. In addition, this change in accounting policies ensures that loss allowance accounting processes remain streamlined for HGB and IFRS purposes, as was previously the case under IAS 39 regulations. A material portion of changes which occurred in the financial year under review was thus attributable to a changeover from regulatory to economic parameters.

Amounts carried for the various types of provision/allowance developed as follows:

CREDIT RISK PROVISIONING INDICATORS

€ mn	Total 31 Dec 2018	Total 1 Jan 2018	Change in %
Specific allowance for credit losses	12,503	13,380	-6.6
Portfolio-based allowance for credit losses	33,435	36,919	-9.4
General risk provisions (section 340f of the HGB)	159,345	122,110	30.5
Other provisions	5,602	7,899	-29.1
Total risk provisioning	210,885	180,308	17.0

The reductions in specific and portfolio-based allowance, and in provisions, were largely due to conversion effects under IFRS 9, as outlined above. In addition, write-downs had to be reversed due to recoveries of previously non-performing loan exposures. This shows a further improvement in the quality of the loan portfolio, thanks to successful restructuring and workout measures. This was offset by an allocation to general risk provisions in accordance with section 340f of the HGB.

f) Concentration risks

The Management Board is informed about economic capital requirements for credit risks, as part of the overall internal risk report. In addition, internal reporting provides a more in-depth analysis of the portfolio structure in terms of concentration risks, using key risk criteria such as country, sector, property type, credit rating class, or the volume of loans extended to a single business partner. These reports contain details concerning individual exposures as well as on any specific provisions.

Real Estate Finance

The share of domestic loans in DZ HYP's total real estate financing portfolio currently stands at 97.3 per cent. The share of international financings rose to 4.9 per cent in 2018, whereby the target markets of Austria, France, the United Kingdom and the Netherlands account for 85.8 per cent of international loans.

A breakdown of real estate lending volumes by property type is provided below:

REAL ESTATE LENDING VOLUME BY TYPE OF PROPERTY

€ mn	Total 31 Dec 2018	Total 1 Jan 2018	Change in %
Residential	15,394	14,732	4.5
Multi-storey apartment buildings (multi-family homes)	13,869	13,525	2.5
Office	8,437	7,973	5.8
Retail	7,916	7,208	9.8
Hotels	2,371	2,031	16.7
Logistics	1,047	947	10.6
Other	1,180	714	65.3
Not allocated to any property type	967	1,296	-25.4
Total	51,181	48,426	5.7

Originated loans to local authorities

Risk monitoring in the area of public-sector clients focuses on regional concentration risks in particular. The broad portfolio diversification was maintained in 2018, with 57 per cent of the aggregate portfolio attributed to the German federal states of North-Rhine Westphalia (27 per cent), Hesse (15 per cent) and Lower Saxony (15 per cent).

Capital markets business

DZ HYP is exposed to noticeable concentration risks in the public finance portfolio in particular. In the event of any material loan defaults or bail-ins affecting these holdings, DZ HYP might be forced to draw upon DZ BANK's obligation to equalise losses, as provided for in the control and profit transfer agreement.

The regional breakdown of the securities portfolio is analysed below:

CAPITAL MARKETS BUSINESS (EXCLUDING MBS): REGIONAL DISTRIBUTION OF SECURITIES HOLDINGS

Country	31 Dec 2018 (€ mn)	1 Jan 2018 (€ mn)	Change in %
Germany	8,405	9,053	-7.2
EU peripheral countries*	4,087	4,302	-5.0
Other EU member states	1,149	1,173	-2.0
Other third countries	939	1,001	-6.2
Supranationals	433	442	-2.0
Total	**15,013**	15,971	**-6.0**

*) Italy, Portugal and Spain

The portfolio is continuously monitored and examined for risks. During the financial year under review, a particular focus was on the portfolio of exposures to countries at the European periphery, which is subject to persistent uncertainty on international financial markets due the political and economic crisis in Italy. Furthermore, the portfolio of exposures to the United Kingdom was a focal point of checks, given the UK's impending exit from the EU (Brexit). Such analyses cover the entire economic environment (including the labour market, the real estate market and gross domestic product, for example). As a result, Brexit-related risks from the MBS exposure to the UK have sufficiently been taken into consideration within internal stress scenarios. The monitoring of credit risk and collateral for individual exposures has not yielded any signs of material risks. Given its predictable new business activities in the United Kingdom, DZ HYP does not anticipate any material impact on its operating business from a potential Brexit. The following table shows the entire underlying exposure:

UK EXPOSURE

€ mn	Total 31 Dec 2018	Total 1 Jan 2018	Change in %
MBS	270	414	-34.8
Mortgage loans	279	283	-1.4
Bank bonds	129	129	–
Derivatives	78	38	105.3
Total	**756**	864	**-12.5**

III) Market price risk

Market price risk is the impact of interest rate fluctuations on the money and capital markets, and changes in exchange rates. DZ HYP is largely exposed to market price risk in the form of interest rate risk, currency risk, as well as spread and migration risk. These risks are measured, and limits applied, at Group level, using data provided by DZ HYP on a daily basis. Market price risk is quantified via the risk capital requirement (for interest rate risk and currency risk) as well as risk contributions (for spread and migration risks).

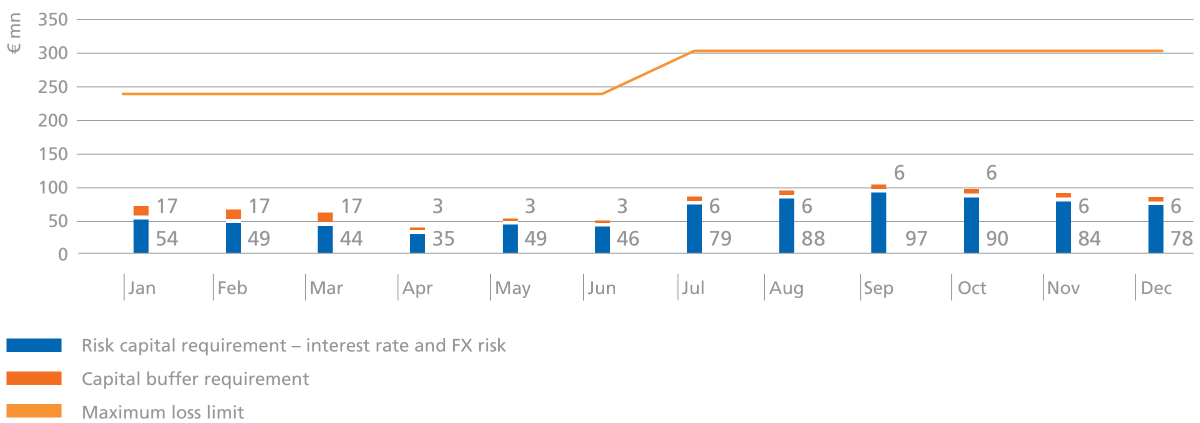
DZ HYP uses various hedging tools in its dynamic management of interest rate risk and currency risk for the Bank as a whole. This consists mainly of interest-rate swaps, cross-currency swaps and caps. Each derivative hedge forms part of the overall management of the entire banking book.

Market Risk Controlling informs the Management Board (as well as the Treasury) on the day-to-day limit utilisation in terms of the risk capital requirement at Group level, and of sensitivity limits implemented. A multi-level escalation plan, comprising escalation paths and measures to be taken, has been implemented to deal with the breach of defined thresholds. No escalation was required in the financial year under review.

To quantify market price risk, the Bank calculates interest rate sensitivity parameters (i.e. theoretical present value changes given simulated changes in interest rates) on a daily basis. Interest rate sensitivity during the year under review was characterised by low fluctuations at a low level. Interest rate sensitivity limits were always complied with. In line with the procedures applied to other types of risk, the risk classification procedure is examined for appropriateness on an annual basis, and adjusted if necessary. The Bank regularly calculates scenarios based on parameters set by DZ BANK. These also include those defined by BaFin (in Circular 09/2018) for the purposes of monitoring interest rate risk exposures of investments.

During the course of 2018, DZ HYP's limit utilisation for market price risk was low following the merger. The corresponding limit (defined by the maximum loss threshold) was raised from € 241 million (the limit applicable to former DG HYP) to € 305 million in the course of the merger.

RISK CAPITAL REQUIREMENT FOR INTEREST RATE AND CURRENCY RISK, PLUS CAPITAL BUFFER REQUIREMENT FOR REAL ESTATE RISK*



* Figures for 2018 – DG HYP only for the first half of the year

During the course of 2018, DZ HYP's limit utilisation for spread and migration risks declined following the merger. The corresponding limit (defined by the contribution alert trigger) was raised from € 900 million (the limit applicable to former DG HYP) to € 1,375 million in the course of the merger.

Capital buffer amounts – as part of market price risk – are only being maintained for real estate risk, i.e. for potential fluctuations in the value of the Bank's own property holdings.

DZ HYP's Treasury management is in line with the Bank's business model. In particular, the primary focus of Treasury management is on managing profit and loss for the period, in order to protect margins from client business. Treasury's business activities are not regarded as a profit centre.

Real estate loans with term exceeding ten years are subject to statutory termination rights pursuant to section 489 of the German Civil Code (BGB). The effect of these optional risks are reflected in a separate risk model. Contractual early redemption rights are adequately taken into account via notional lifetimes which are validated statistically.

IV) Liquidity risk

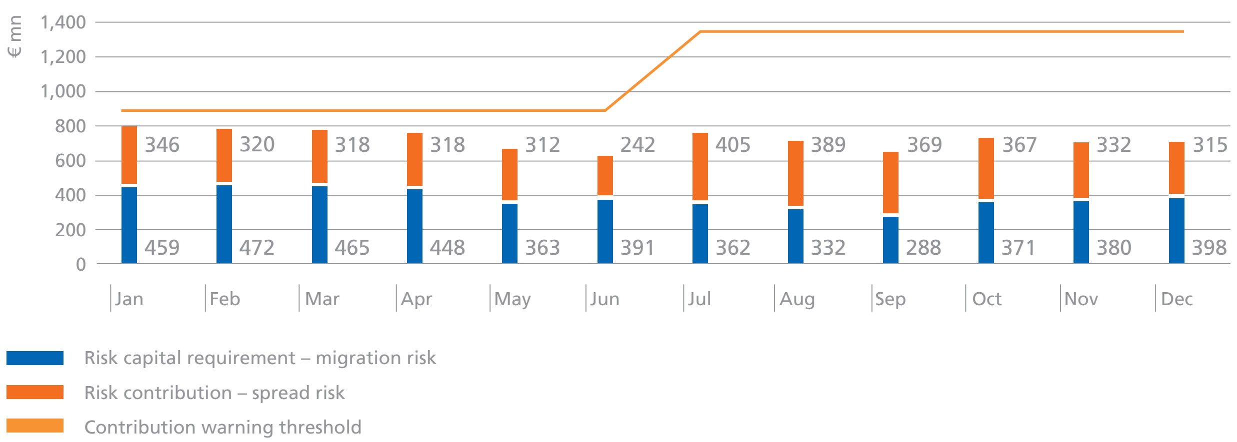
Liquidity risk comprises the threat that DZ HYP is actually unable to borrow the funds required to maintain payments. Liquidity risk can thus be understood as the risk of insolvency. In this regard, liquidity risk arises from a mismatch in the timing and amount of cash inflows and outflows and is affected to a significant degree by other types of risk, such as market price risk or reputational risk. The Bank's liquidity situation is determined daily, in line with the regulatory and business requirements and in coordination with DZ BANK.

Based on the management of economic liquidity, Market Price Risk and Liquidity Risk Controlling provides Treasury with a differentiated overview on each business day, indicating future liquidity flows (comprising cash flows as well as a gap analysis of principal repayments and fixed interest mismatches) resulting from the individual positions in the portfolio. Where a comparison of liquidity data against defined limits gives rise to escalation, this follows a pre-defined process flow which may invoke emergency liquidity planning. No escalation was required in 2018.

In order to determine Group liquidity risk exposure and DZ HYP's contribution thereto, DZ HYP's liquidity data is transmitted to DZ BANK's Risk Control Unit daily, where this is used to determine limit utilisation.

Additionally, an overview of excess liquidity post-stress scenarios is submitted to Management Board meetings. Liquidity is managed on the basis of this overview, with the dual objectives of securing the Bank's long-term liquidity and achieving compliance with CRR requirements. A suitable liquidity controlling system is already in place in line with the requirements of MaRisk for measuring and reporting on liquidity risk (BTR 3.1 and

RISK CAPITAL REQUIREMENT – SPREAD AND MIGRATION RISK*



* Figures for 2018 – DG HYP only for the first half of the year

3.2). A limit system is implemented on a daily basis and integrated into the risk monitoring process. The results from the scenario analyses – which comply with the requirements set out in the relevant sections of MaRisk – are fed into the risk analysis process.

The first step in determining risk indicators is to calculate a liquidity run-off profile, based on the contractually-agreed terms of all financial instruments with an impact on liquidity. The base case scenario maps the development of current and future liquidity reserves, in connection with expected business activities. Potential changes to the liquidity run-off profile, and to liquidity reserves, in the event of a crisis affecting markets or the Bank are simulated for four stress scenarios:

- a serious crisis threatening the DZ BANK Group;
- a one-notch rating downgrade of DZ BANK Group;
- a global economic crisis; and
- a combination of a crisis affecting the market as well as the Company.

Expected liquidity is indicated by the liquidity run-off profile in the base case scenario. In the stress scenario, liquidity is defined by the worst daily value among the four scenarios. Using expected liquidity for each record date, the minimum excess liquidity indicator is determined, which expresses the adequacy of economic liquidity. Throughout 2018, this indicator remained above the limit of zero. The set of scenarios is complemented by inverse stress tests carried out on a quarterly basis.

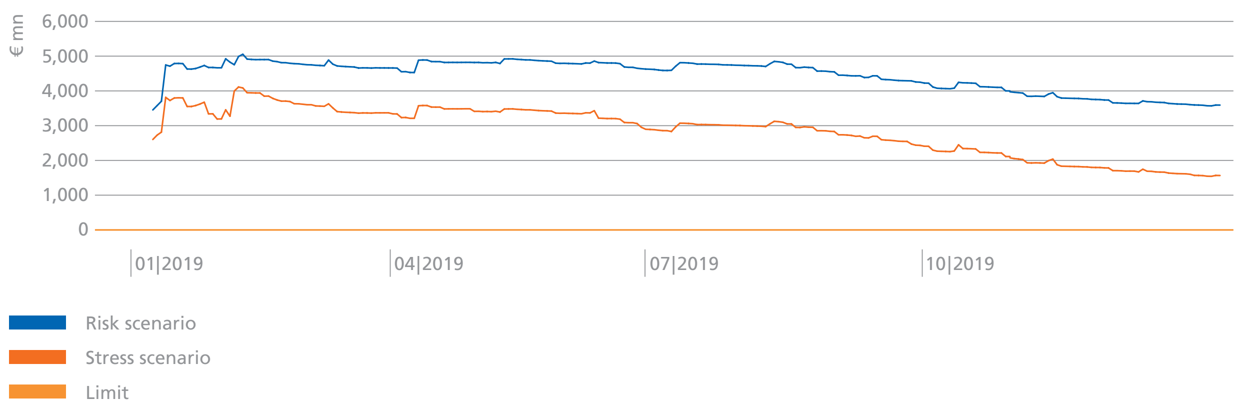
The liquidity risk model and the emergency concept are reviewed annually, within the framework of an adequacy check, and adjusted if necessary.

One or more independent credit rating agencies may assign ratings for DZ HYP. The purpose of a rating is to assess DZ HYP's credit quality, informing investors about the repayment probability of capital invested in DZ HYP. Refinancing risk denotes the risk of a loss which may be incurred as a result of a decline of DZ HYP's liquidity spread (which forms part of the spread on DZ HYP's own issues): with a wider liquidity spread, covering any future liquidity requirements would incur additional cost. DZ HYP minimises refinancing risk through the management of the liquidity run-off profile.

During 2018, DZ HYP's funding activities comprised the use of unsecured liquidity facilities (largely provided by the Bank's Group parent DZ BANK), as well as the issuance of Mortgage Pfandbriefe and Public-Sector Pfandbriefe (which were predominantly purchased by counterparties outside the Cooperative Financial Network).

DZ HYP defines market liquidity risk as the threat of losses which may be incurred due to unfavourable changes in market liquidity – for example, due to a deterioration in market depth, or in the event of market disruptions, in which case the Bank may only be able to sell assets held at a discount, and active risk management may be restricted. Since the impact of market liquidity risk is evident in changed spreads and volatility levels, this is implicitly reflected in risk calculations.

DEVELOPMENT OF EXPECTED LIQUIDITY PER 31 DEC 2018



For the purposes of regulatory monitoring of the Bank's liquidity situation, part 6 of the CRR defines the calculation of the (short-term) Liquidity Coverage Ratio (LCR), which is designed to ensure the resilience of banks through a 30-day liquidity stress scenario. The indicator is defined as the ratio of available highly liquid assets to net cash outflows over the next 30 days, subject to defined stress conditions. A minimum Liquidity Coverage Ratio (LCR) of 100 per cent has been mandatory for banks since 1 January 2018.

The waiver under Article 7 of the CRR does not cover the requirements under part 6; therefore, DZ HYP must comply with the corresponding requirements at a single-entity level. Accordingly, the Bank reports its single-entity LCR, in accordance with the CRR, to the supervisory authorities on a monthly basis. An additional LCR indicator is determined for DZ HYP, based on the require-ments of Delegated Regulation 2015/61/EU. This indicator remained above 100 per cent throughout the 2018 financial year.

in per cent	December 2018	September 2018	June 2018 (DG HYP only)	March 2018 (DG HYP only)
LCR month-end	305	460	958	619

The (long-term) Net Stable Funding Ratio (NSFR) is designed to restrict banks' ability to enter into mismatches between the maturity structure of assets vs. liabilities. The NSFR relates the amount of stable funding (equity and liabilities) to the required amount of stable funding (as required by the lending business). For this purpose, funding sources and assets are weighted, depending upon their degree of stability (or the ability to liquidate them, respectively), using inclusion factors defined by the supervisory authorities. In contrast to the Liquidity Coverage Ratio, compliance with the Net Stable Funding Ratio is only expected to be mandatory from 2019 onwards. Within the scope of internal reporting, DZ HYP already provides the NSFR parameter, in line with applicable calculations; NSFR figures were above 100 per cent throughout 2018.

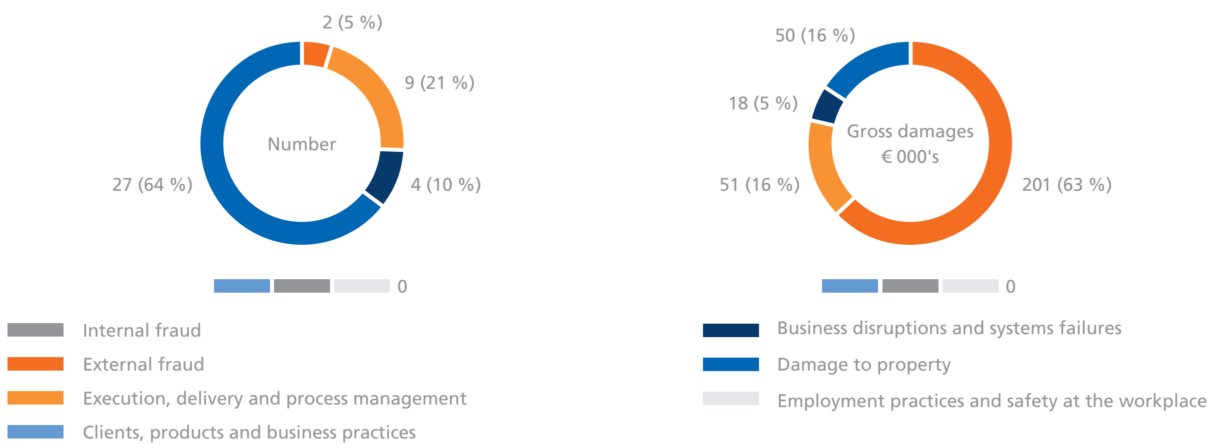
V) Operational risk

Closely aligned to the definition by banking regulators, DZ BANK Group defines operational risk as the risk of losses resulting from human behaviour, technical faults, weaknesses in processes or project management procedures, or from external events. This definition includes legal risk.

Capital requirements for the operational risk are determined at Group level, as part of the process to determine regulatory capital requirements, applying the standardised approach as set out in the CRR. Due to the waiver, DZ HYP does not carry out its own determination; instead, DZ HYP's data is incorporated into Group calculations. Moreover, economic capital for operational risk is determined at Group level, using a portfolio model, and incorporated into internal management, both on a Group and single-entity level.

DZ HYP has continued to maintain the system for collecting and recording loss data, which was already in use at its two predecessor institutions, DG HYP and WL BANK, since the merger. Incoming loss reports involving gross damages of € 1,000 or higher are collected systematically in a database arranged according to predefined categories: they are subsequently used as indicators for further improving the operating processes, and hence for reducing operational risks. Losses incurred by DZ HYP are incorporated into DZ BANK's economic model, enhancing the database.

OPRISK LOSSES 2018



A total of 42 loss events (2017: 28 for DG HYP/48 for WL BANK) with aggregate net damages of € 319,000 (2017: € 7,711,000 for DG HYP/€ 501,000 for WL BANK) were recorded during the year under review. In principle, the incidents are analysed for any cues how such losses can be avoided in future (for example, by changing business processes), and any changes required are implemented. Given the merger, it is fair to assume a higher probability of losses occurring. The loss data reported did not provide any indication of elevated risk, however.

Scenario-based risk self-assessments were once again conducted in 2018. Using risk scenarios, material potential risks were determined, in accordance with the CRR, for all first-level risk categories and mapped in the form of scenarios. The scenarios deemed to be most likely were potential threats from hacker attacks, outsourcing, or the non-availability of buildings. The results of DZ HYP's assessments are incorporated into the economic risk model developed by DZ BANK at Group level.

In order to be able to identify operational risks in good time, an early warning system used by DZ HYP regularly records a total of 173 risk indicators (aligned with the CRR event categories, including system failures, fraud, staff fluctuation) and analyses results by way of a traffic light system. As in the previous year, the risk indicator system did not yield any indications of particular operational risks during 2018. Throughout the year, the vast majority of risk indicators were in 'green' status. 'Amber' signals were given in isolated cases only; as a rule, these were returned to 'green' in the following month. There were no 'red' status alerts.

DZ HYP has outsourced certain activities and processes to external service providers. The outsourcing unit is predominantly responsible for determining, as part of the outsourcing risk analysis, whether an outsourced activity or process is material, and for assessing the risk involved. Other relevant organisational units (such as the Legal department) are involved in this process. This risk analysis is reviewed and updated once a year. DZ HYP's material outsourcing arrangements include the outsourcing of IT and network operations to T-Systems International GmbH, Frankfurt/Main, and to Ratiodata IT-Lösungen & Services GmbH, Münster. The use of the waiver option relieves DZ HYP of some obligations under regulatory reporting; the remaining parts of reporting duties are either outsourced – under a corresponding agreement – to DZ BANK, or handled by various departments of DZ HYP. Furthermore, DZ HYP is integrated into DZ BANK's risk measurement, monitoring and management structure (including the measurement of liquidity risk and Group-wide market price risk), via corresponding outsourcing arrangements. From an organisational perspective, DZ HYP's Risk Controlling unit is responsible for measuring operational risks, whilst the Central Outsourcing Management unit within DZ HYP's Finance division is responsible for coordinating outsourcing control. Both units report regularly, at DZ HYP's Management Board meetings, on losses sustained, on the activities for further developing the quantification approach, as well as on the status of outsourcing control.

VI) Equity investment risk

Equity investment risk is defined as the risk of losses due to negative changes in value affecting the part of the investment portfolio that is not taken into account for other types of risk. Investments are held for strategic considerations; they are of minor importance to DZ HYP.

The risk capital requirements for DZ HYP's equity investment risk are calculated by DZ BANK, in line with the measurement of equity investment risk by DZ BANK. For this purpose, risk capital requirements are measured using a value-at-risk concept based on a variance/covariance approach, with a one-year holding period. Risk drivers are the market values of investments, volatility of such market values and correlation among them. Market value fluctuations are predominantly derived from exchange-listed reference assets.

VII) Reputational risk

Reputational risk is defined as the risk of losses caused by events which damage the confidence of, in particular, clients, shareholders, labour market participants, the general public or regulatory authorities in the Bank, or the products and services it offers. Reputational risk may be caused by other risk having materialised, but also by other publicly available information concerning DZ BANK Group or DZ HYP.

The Bank's fundamental strategic objectives for dealing with reputational risk have been incorporated in a separate risk strategy. This strategy defines the following key objectives, which also apply on a Group-wide level:

- to avoid losses from reputational events, through preventive measures;
- to mitigate reputational risks, through preventive as well as responsive measures;
- to strengthen awareness of reputational risk within the Bank – including by appointing persons responsible for this risk type, and by establishing a Group-wide framework and reporting structure for reputational risks.

As a matter of principle, reputational risk continues to be implied for risk measurement and capital backing purposes through business risk. Moreover, liquidity risk management explicitly covers the threat of funding problems as a result of potential reputational damage.

VIII) Business risk

DZ HYP defines business risk as the threat of losses arising from unexpected fluctuations in the Bank's results which cannot be offset by cutting costs; assuming an unchanged business strategy, such fluctuations usually materialise on a short-term horizon (within a one-year period) due to changed external circumstances (e.g. in the business or product environment, or due to customer behaviour). DZ HYP models this risk using a so-called earnings volatility approach. An additional capital buffer requirement to cover the option resulting from the termination right under section 489 of the BGB is added to the earnings volatility approach.

IX) Summary

Managing DZ HYP's opportunities and risks is an integral part of the strategic planning process at DZ BANK Group. High-performance management and control tools are deployed across all risk areas; these tools are continuously fine-tuned and developed. DZ HYP's expected performance is appropriate in terms of the risks assumed. Hence, there are no indications for any threats to DZ HYP's continued existence.

ECB and EBA hold the view that any profit and loss transfer agreements prevent the inclusion of ordinary shares (including the associated premium) as common equity tier 1 (CET1) capital. Given its control and profit transfer agreement with DZ BANK AG, DZ HYP is also affected by this. Reasons given by the regulators include the lack of discretion available to DZ HYP regarding distributions on ordinary shares. During a transitional period from 2018 until the end of 2020, affected capital instruments will remain fully eligible for inclusion as CET1 capital. As part of the CRR revision, there are plans to add a provision to Article 28 (3) of CRR II that, subject to certain prerequisites, the existence of a profit and loss transfer agreement is not detrimental to inclusion. For instance, the subsidiary will need to have the opportunity of strengthening its reserves prior to distributing profits to the parent company. The planned amendment will remedy the concerns held by regulators. Since DZ HYP will be able to fulfil said criteria, it will be possible to restore the status quo. CRR II has almost been finalised: political 'trilogue' negotiations between the EU Commission, the Council and the Parliament have already been concluded; the final set of rules is likely to come into effect in the second quarter of 2019. However, the exact date of first-time application of the new provision in Article 28 (3) of CRR II has yet to be determined. It is fair to assume that this will be applicable by the end of 2020 at the latest, to prevent an inclusion gap.

REPORT ON EXPECTED DEVELOPMENTS

This forecast and other parts of the Annual Report include expectations and forecasts that relate to the future. These forward-looking statements, in particular those regarding DZ HYP's business and earnings growth, are based on forecasts and assumptions, and are subject to risks and uncertainties. As a result, the actual results may differ materially from those currently forecast. There are many factors that impact on DZ HYP's business, and which are beyond the Bank's control. These factors primarily include changes to the general economic situation and the competitive arena, and developments on the national and international real estate and capital markets. In addition, results can be impacted by borrowers defaulting or by other risks, some of which are discussed in detail in the risk report. In this context, DZ HYP would like to point out that despite discernible progress made, no sustainable solution has been found for the global issue of high sovereign debt; ongoing reforms are needed. After the merger of WL BANK and DG HYP to form DZ HYP was completed in the year under review, with retroactive economic effect from 1 January 2018, the forecasts and target/actual comparisons described in this section relate to the merged institution in full. The corresponding planning was prepared in May 2018.

Quality of forecasts

DZ HYP's financial performance in the 2018 financial year was in line with the merged entity's projections, especially in terms of new business volume in Real Estate Finance, which outperformed expectations. Average interest margins were slightly below the budgeted figures. Net interest income came in slightly above budget. The net commission result, on the other hand, was lower than forecast, as commission income from the lending business was lower than expected. The aggregate of net interest income and the net commission result was 0.4 per cent above forecast levels. Thanks to the macroeconomic environment in Germany, which remains positive for real estate, risk provisioning was once again significantly lower than the projected figure, which was determined on the basis of standard risk costs. Overall, the quality of DZ HYP's forecasts for the year under review proved to be robust and reliable. The fact that results once again exceeded forecasts overall also underlines the conservative stance on which the Bank's projections are based.

Forecast period

Based on the strategic business orientation as part of a five-year plan, DZ HYP derives its operative planning on an annual basis, focusing on the subsequent financial year. As a rule, the Bank's forecast is based on the one-year operative planning horizon; in certain cases it also refers to the results of the five-year plan.

Business environment and assumptions underlying the forecast

In an environment shaped by global risks, the German economy has been impressively stable since 2013. This has mainly been driven by private consumption, which benefits from higher nominal disposable income – driven in particular by the positive labour market development and the associated increase in salaries. Looking ahead to the next year, it is fair to assume that disposable income will increase further. This means that the upswing in the German economy is likely to continue on the whole in 2019, despite an interruption in the autumn quarter of 2018 due to registration problems in the automotive industry and a slight dip in global economic momentum.

DZ HYP expects the German real estate market to remain resilient and stable in this environment during 2019. As the ECB's monetary policy remains supportive even after the conclusion of its bond-buying programme, and given the high investment pressure faced by institutional investors (including those from abroad), the Bank continues to envisage a high volume of investments on the German real estate market. The robust labour market is likely to sustain good demand for office space. Rising wages will support the retail sector, and will help private households to pay rising residential rents. At the same time, this means that pressure on yields will remain strong, with risk premiums, which are already lower than they were in previous years, set to shrink further.

Nonetheless, political risks may challenge the German economy, which has been resilient so far: these may include a scenario in which policymakers fail to push through structural reforms – in France and Italy, for example – as well as risks associated with Brexit and the associated potential trade restrictions, or possible setbacks to free trade (for example the trade disputes between the US and China) and geopolitical risks. In this environment, the ECB will continue with its supportive monetary policy by taking indirect measures even after the end of its bond-buying programme (for example, new rounds of supplying banks with central bank money which they can then use to buy bonds) and will continue to respond as necessary at all times. It is also fair to assume that if needed, the ECB would also resume direct purchases of sovereign and corporate bonds.

DZ HYP's business model, which is focused on the German real estate market, shows different degrees of sensitivity to these potential threats. Implications are thus possible – at least indirectly, e.g. due to falling demand, financial market volatility, or price bubbles.

Expected development of DZ HYP

Based on these framework conditions, and adhering to its unchanged risk strategy, DZ HYP plans to avoid cyclical peaks in the long-term business it pursues, to the extent possible. Moreover, the Bank does not calculate any performance contributions from unhedged interest rate or foreign exchange positions in its projections. Therefore, any changes to the relevant market parameters do not materially influence the Bank's results planning. Key value drivers for DZ HYP's future financial performance are thus the Bank's planned business volume, net credit margins, commissions earned and risk costs incurred in new business, as well as any write-downs which may be necessary in the non-strategic portfolios. Given DZ HYP's strengthened market position, the Bank has conservatively accounted for these factors in its planning calculations.

The Basel Committee on Banking Supervision (BCBS) finalised its revised "Basel III: Finalising post-crisis reforms" framework for the calculation of risk-weighted assets and capital floors on 7 December 2017. Simulations show that the amended regulations will only have a minor direct impact upon DZ HYP's calculation of risk-weighted assets under the IRB approach. However, the capital floor is expected to lead to increased capital requirements under the revised Credit Risk Standard Approach, due to higher capital requirements for commercial real estate finance. These regulations will take effect from 2022, with a phase-in period until 2027. Since this period provides sufficient scope for profit retention, DZ HYP – in coordination with its Group parent, and supported by the existing Group waiver – assumes that the revision of the framework will not lead to any restrictions concerning its planning calculations.

Assuming these assumptions will materialise, DZ HYP will once again engage in a sufficient level of new real estate finance business in 2019. Given margins which are expected to be slightly lower, volumes are also anticipated to fall short of the figures seen in the year under review. The aim is to strike a good balance between profitability targets and equity requirements, whilst closely adhering to the relevant regulatory requirements.

Given the expected portfolio increase in real estate lending, net interest income is likely to slightly exceed current levels.

Depending on the relevant deal flow and the product mix, the net commission result will remain below the current figures.

The future development of administrative expenses will not least be driven by increasing regulatory requirements, which exert additional pressure on staff and IT costs. Overall, the Bank's administrative expenses will decrease considerably in the future thanks to the merger, which has already been implemented to a large extent.

Provisions for loan losses are calculated using individual standard risk costs which are commensurate with the Bank's business model; the long-term forecast projects a mid-range double-digit million euro figure. Overall, the expected acute default risks are conservatively accounted for.

The MBS portfolio is intensively monitored by means of a detailed risk management system, regular analyses of individual exposures, and comprehensive stress testing. The development of material risk factors indicates stabilisation at the current levels. The persistent default risks this portfolio is exposed to were identified within the scope of a five-year forecast, and adequately incorporated in the Bank's projections.

The merged Bank is pursuing a successful path – with new business aligned toward our clients' requirements. The Bank is consistently reducing capital markets transactions which are not related to client business.

The merger of DG HYP and WL BANK to form DZ HYP has created a leading real estate finance bank and Pfandbrief issuer in Germany – with products and services and a distribution approach aligned to client segments, alongside customised offers, catering to the segments of Commercial Real Estate Finance, Housing Sector, Public Sector, and Retail Customers/Private Investors. The systematic broadening and deepening of primary banking relationships, combined with a full range of products and services, will support cooperative banks in their continuous expansion of market share, strengthening them sustainably.

ABOUT 690,000 KILOMETRES TO REACH DZ HYP

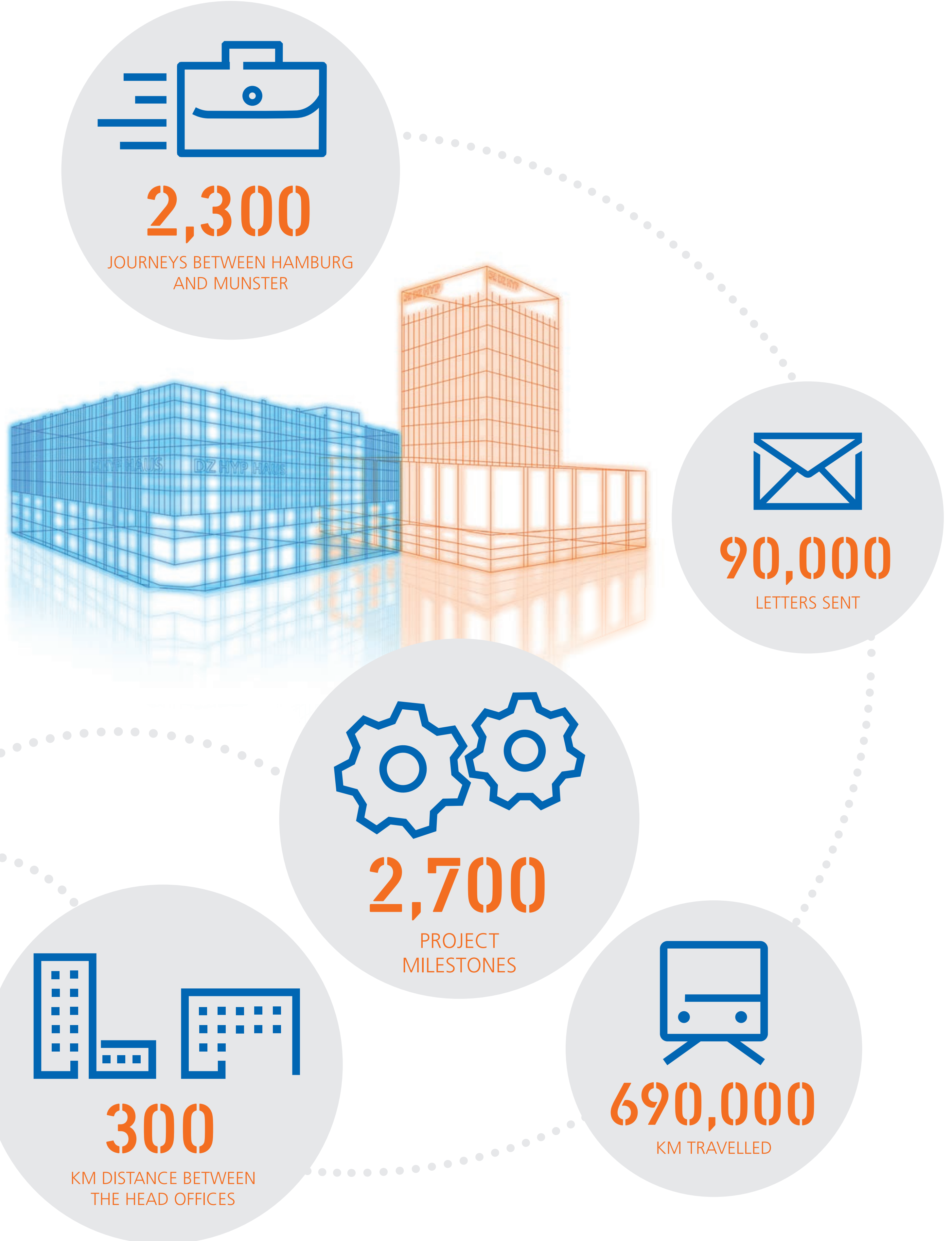
Facts and figures prove the laborious work processes

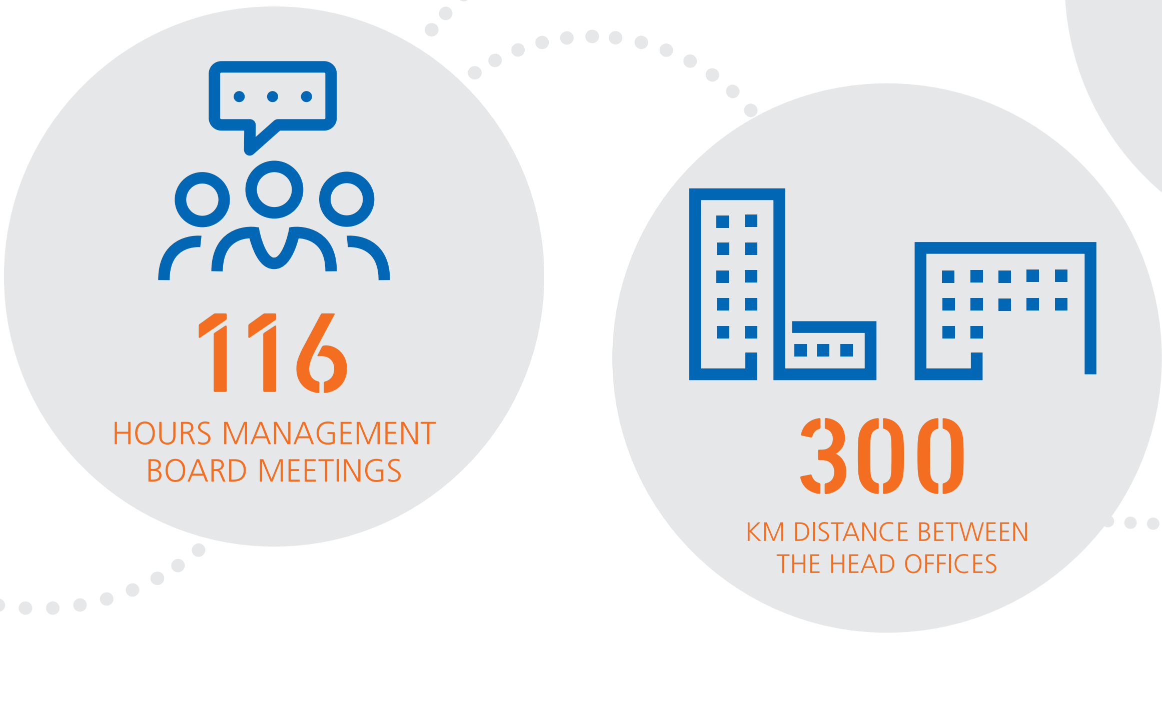
Newsflow on Day 1 was positive throughout.

Until year-end 2018, numerous DZ HYP employees undertook the journey of just under 300 kms between both head offices approximately 2,300 times – for reasons directly linked to the merger. All in all, this amounts to approximately 690,000 kilometres travelled for the merger. This figure gives a first indication of the amount of work done before and after Day 1.

About 90,000 letters were sent to all clients and partners, informing them about the merger. Since then, cooperative banks, commercial real estate investors, housing companies, and public-sector clients have been successfully working together with DZ HYP. The migration processes within the scope of the merger are still fully underway. A few important milestones of the approximately 2,700 defined in the merger project are scheduled to be reached within 2019.

All in all, after 130 project manager jour fixes and 116 hours Management Board meetings, countless e-mails, telephone and video conferences, carried out leading up to the start, and after the positive feedback from the press, one can say: it was a lot of work, but worth the effort.





EMPLOYEES

Cultures coming together at DZ HYP

In addition to structural and technical requirements, cultural integration following the merger of DG HYP and WL BANK is also a challenge for the Bank's human resources work. DZ HYP pursues a long-term concept using various formats. These are intended to ensure that employees cope well with the changes that need to be made, and can make a gradual contribution to the integration of the two institutions. The first and foremost task lies in familiarising all employees with the orientation of DZ HYP and convincing them to unite behind common goals. Even during the merger process, interested employees were invited to dialogue events with the Management Board in the year under review, allowing them to engage in informal discussions about the merger – and the changes that it would entail – in a small group setting. In addition, the Bank organised the very first conference for all executive staff.

As well as pursuing a joint approach, it is also important to support the people affected by the changes. As individual needs vary and can include professional or procedural backup, or support in the form of personnel resources, DZ HYP offers various measures to support the individuals affected. These include coaching and training sessions for executives, change workshops and seminars for employees and technical and process-related support, as well as events designed to transcend company boundaries and allow the new teams to get to know each other.

Introduction of a uniform HR support concept

The Human Resources department pursues a uniform personnel support concept: the Human Resources Business Partner (HRBP) concept, which has been established in the Hamburg office (formerly DG HYP) for many years. As part of the uniform alignment of the Bank's HR work, this concept has also been launched at the Münster office (formerly WL BANK). The aim is to bring human resources work more closely into line with value creation in the units it supports. The HRBP concept helps employees to contribute to business success and create added value for customers. The areas in question are provided with close support in tackling the individual challenges facing them.

Future-proof HR initiatives

In order to meet the demands of a working world that is changing at an ever faster pace, several new programmes were launched in 2018 to secure the Bank's future viability.

New employer/works council agreements on "Working hours" and "Employee appraisals"

In order to standardise the applicable regulations, a new employer/works council agreement on working hours came into force for the Hamburg office on 1 November 2018. The aim was to promote flexible working arrangements that give employees a degree of autonomy. Within a defined framework, employees can decide when and how they want to complete their work. Since the agreement came into force, the recording of working time has been voluntary. In addition, employees can now enjoy mobile, digital working arrangements, as well as the opportunity to save hours up for additional days of annual leave, or take a sabbatical of up to three months. To support modern management, a format for employee appraisals that is both workable and state-of-the-art has also been developed at the Hamburg office. It ensures that managers and their employees enter into a dialogue based on partnership at least once a year: instead of featuring a formalised assessment that reviews the employee's past performance, the emphasis is on their individual strengths and potential instead. Similar solutions are also planned for the Münster office in 2019.

New employee portal and digitalisation of travel expense reports

The employee portal introduced in 2018 is a key element of the Bank's future-proof HR work. It is based on state-of-the-art SAP technology and features functions such as time management, salary statements and the management of personal details or evaluations for managers. The introduction of the new employee portal has resulted in the end-to-end digitalisation of the travel expense report process. Since the portal was launched, employees have been able to create their own travel expense reports which are then approved by their managers, speeding up the process considerably.

Promoting women: statutory quotas and corporate initiative

In accordance with statutory requirements, the Supervisory Board and Management Board of DZ HYP are obliged to set targets for the proportion of women on the Supervisory Board, the Management Board, and the two management levels below the Management Board – as well as target dates for achieving such targets. Against this background, in accordance with section 111 (5) of the AktG, in 2017 DG HYP's Supervisory Board set a target quota of 22 per cent for the share of women on the Supervisory Board, and a target quota of 0 per cent for the share of women on the Management Board. The target date for implementation of these quotas was 31 July 2018. Both targets were reached by the end of the deadline. In accordance with section 111 (5) of the AktG, on 18 June 2018 DG HYP's Supervisory Board set a target quota of 22 per cent for the share of women on the Supervisory Board, and a target quota of 0 per cent for the share of women on the Management Board. The target date for implementation of these quotas is 31 July 2020. These objectives also apply to the merged bank, effective from the merger.

Promotion of up-and-coming young talents as a key element of HR work

DZ HYP offers tailor-made vocational training and career advancement programmes to school leavers, university students and graduates. The Münster office has been training bank clerks since 1989. The trainees rotate through all of the relevant departments over a period of two and a half years. Since the merger, some parts of the Hamburg office have also been included in the programme. For the theoretical part of their vocational training, the trainees attend blocks of lessons at the GenoKolleg cooperative vocational college in Münster.

In addition to conventional vocational training, the Münster office has also been offering dual study programmes for Bachelor and Master of Arts degrees in Banking & Finance, with an integrated two-year vocational training component, since 2012. The programme features alternating practical and theoretical phases at ADG Business School in Montabaur. Several school cooperation projects, participation in vocational training fairs and in internship programmes organised by the Chambers of Commerce and Industry (IHK) promote contact with individuals who are potentially interested in completing their training at DZ HYP. A total of four trainees and two dual students are recruited every training year.

DZ HYP's 18-month graduate trainee programme was developed and launched in 2010. One trainee, who will focus on commercial real estate finance, was recruited in Hamburg in 2018. In the Münster office, one trainee was recruited to the Back Office – Housing Sector, Retail Customers/Private Investors. Three participants of the previous trainee programme cycle successfully completed their course in the year under review and were given permanent employment contracts. "Trendence und Absolventa", the leading online jobs portal for young academics, once again awarded DZ HYP its seal of quality in 2018 for its "career-promoting trainee programme".

DZ HYP Real Estate Academy continued

The DZ HYP Real Estate Academy is an integral part of the Bank's specialist training programme. It functions in partnership with the IRE|BS Real Estate Business School, Regensburg, one of the most renowned further training establishments in the real estate sector. The fifth year of the programme was successfully concluded in 2018, with participants also including ten employees from cooperative banks. The Real Estate Academy offers comprehensive training and an in-depth insight into the various areas of the real estate industry. The curriculum consists of twelve and a half days of lectures in total, split into three modules, plus a demanding project exercise at the end of the programme which is executed in and presented by small teams.

Coordinated human resources policies within the DZ BANK Group

The HR strategy adopted by the DZ BANK Group in 2017 is being implemented in close cooperation between the individual companies. In the year under review, for example, HR managers came together in Group-wide workshops to address the topic of digital change and made intensive use of the opportunities for best practice-sharing and knowledge transfer. Also when implementing statutory requirements such as the German Regulation on Remuneration in Financial Institutions 3.0 (Institutsvergütungsverordnung 3.0), there is close and effective coordination at Group level to ensure uniform standards.

Cooperation with the Works Council

The constructive cooperation between DZ HYP and the Works Council continued during the year under review. The joint development of a reconciliation of interests and a social compensation plan as part of the merger, the work on the "remuneration system for employees not subject to a collective pay scale agreement" and the conclusion of two employer/works council agreements on working hours and employee appraisals are particularly worthy of mention. DZ HYP would like to thank the Works Council for the good and constructive cooperation.

STAFFING INDICATORS

	2018*)	2017*)	2017 DG HYP	2017 WL BANK
Total**)	**873**	877	480	397
Fluctuation rate (%)	**4.4**	3.4	4.2	2.4
Share of voluntary resignations (%)	**2.5**	1.9	1.9	1.9
Years of service	**13.7**	13.3	14.3	12.1
Number of training days per employee	**1.1**	2.3	2.0	2.6
Employment basis (%)*)**				
Full-time employees	**77.9**	79.7	81.3	77.7
Part-time employees	**22.1**	20.3	18.7	22.3
Share of women (%)	**45.8**	44.0	40.7	48.0
Average age	**45.3**	44.9	47.1	42.2

*) Consolidated
**) Annual average
***) Average values

FINANCIAL STATEMENTS

77 Financial Statements
78 Balance Sheet
80 Profit and Loss Account
81 Statement of Changes in Equity
82 Cash Flow Statement
83 Notes to the Financial Statements
83 General Notes
89 Notes to the Balance Sheet
100 Notes to the Profit and Loss Account
101 Coverage
108 Other Information on the Annual Financial Statements

BALANCE SHEET

AS AT 31 DECEMBER 2018
ASSETS

	€ 000's	Note	€ 000's	31 Dec 2018 € 000's	1 Jan 2018 € 000's	DG HYP 31 Dec 2017 € 000's
CASH FUNDS				570	650,822	649,919
a) Cash on hand			66		31	–
b) Balances with central banks			504		650,791	649,919
of which: with Deutsche Bundesbank	504				(650,791)	(649,919)
LOANS AND ADVANCES TO BANKS		(4)		4,356,777	4,215,329	2,291,190
a) Mortgage loans			20,327		20,892	16,563
b) Loans to local authorities			319,045		386,908	109,714
c) Other loans and advances			4,017,405		3,807,529	2,164,913
of which: payable on demand	2,853,062				(1,948,678)	(515,794)
LOANS AND ADVANCES TO CUSTOMERS		(4)		60,039,766	58,256,184	27,233,956
a) Mortgage loans			42,889,984		39,953,321	17,956,504
b) Loans to local authorities			14,726,537		15,690,434	6,682,468
c) Other loans and advances			2,423,245		2,612,429	2,594,984
DEBT SECURITIES AND OTHER FIXED-INCOME SECURITIES		(6)		11,082,874	11,585,635	6,350,993
a) Bonds and debt securities			(10,464,426)		10,861,856	(5,809,621)
aa) Public-sector issuers			6,938,658		7,270,035	3,967,517
of which: securities eligible as collateral with Deutsche Bundesbank	6,086,953				(6,449,571)	(3,223,227)
ab) Other issuers			3,525,768		3,591,821	1,842,104
of which: securities eligible as collateral with Deutsche Bundesbank	2,874,215				(2,743,198)	(1,068,384)
b) Own bonds issued			618,448		723,779	541,372
Nominal amount	616,366				(713,608)	(540,258)
PARTICIPATIONS		(6)		911	911	524
INVESTMENTS IN AFFILIATED COMPANIES		(6)		1,566	1,566	1,566
TRUST ASSETS		(7)		41,902	62,445	61,753
of which: trustee loans	23,802				(44,345)	(43,653)
INTANGIBLE FIXED ASSETS		(6)		2,232	1,988	1,255
a) Concessions, industrial property rights and similar rights and assets, as well as licences in such rights and assets			1,845		1,812	1,231
b) Advance payments made			387		176	24
TANGIBLE FIXED ASSETS		(6)		174,424	165,816	139,990
OTHER ASSETS		(8)		29,594	38,068	12,028
PREPAID EXPENSES		(10)		160,624	177,614	82,801
a) From new issues and lending			159,447		176,050	81,787
b) Other			1,177		1,564	1,014
TOTAL ASSETS				75,891,240	75,156,378	36,825,975

AT 31 DECEMBER 2018
LIABILITIES AND EQUITY

	€ 000's	Note	€ 000's	31 Dec 2018 € 000's	1 Jan 2018 € 000's	DG HYP 31 Dec 2017 € 000's
LIABILITIES TO BANKS		(13)		26,916,136	25,641,260	17,675,294
a) Outstanding Registered Mortgage Pfandbriefe (Hypotheken-Namenspfandbriefe)			2,126,657		2,283,271	928,033
b) Outstanding Registered Public Pfandbriefe (öffentliche Namenspfandbriefe)			1,087,054		1,379,265	790,862
c) Other liabilities			23,702,425		21,978,724	15,956,399
of which: payable on demand	79,764				(399,784)	(37,802)
LIABILITIES TO CUSTOMERS		(13)		19,533,904	21,226,493	7,432,117
a) Outstanding Registered Mortgage Pfandbriefe (Hypotheken-Namenspfandbriefe)			6,528,140		6,706,990	1,387,943
b) Outstanding Registered Public Pfandbriefe (öffentliche Namenspfandbriefe)			10,705,969		12,203,103	5,301,386
c) Other liabilities			2,299,795		2,316,400	742,788
of which: payable on demand	507,059				(602,945)	(566,081)
Registered Mortgage Pfandbriefe and Registered Public Pfandbriefe surrendered to lenders as collateral for borrowings	–				(5,113)	(5,113)
SECURITISED LIABILITIES BONDS ISSUED		(13)		26,487,437	25,236,966	9,491,631
a) Mortgage Pfandbriefe (Hypothekenpfandbriefe)			20,483,690		18,533,324	7,706,760
b) Public Pfandbriefe (öffentliche Pfandbriefe)			3,624,599		3,629,920	1,207,803
c) Other debt securities			2,379,148		3,073,722	577,068
TRUST LIABILITIES		(7)		41,902	62,445	61,753
of which: Trustee loans	23,802				(44,345)	(43,653)
OTHER LIABILITIES		(14)		169,953	207,029	143,967
PREPAID EXPENSES		(10)		186,666	201,652	110,487
a) From new issues and lending			186,664		201,628	110,487
b) Other			2		24	–
PROVISIONS				245,161	221,484	163,750
a) Provisions for pensions and similar obligations			172,447		155,467	121,315
b) Provisions for taxes			10,666		259	–
c) Other provisions			62,048		65,758	42,435
SUBORDINATED LIABILITIES		(15)		80,750	174,718	42,718
FUND FOR GENERAL BANKING RISKS				467,000	422,000	297,000
EQUITY				1,762,331	1,762,331	1,407,258
a) Subscribed capital		(16)	(784,990)		(784,990)	(725,000)
aa) Share capital			149,990		149,990	90,000
ab) Silent partnership contributions			635,000		635,000	635,000
b) Capital reserves			884,196		884,196	589,113
c) Retained earnings			(93,145)		(93,145)	(93,145)
ca) Legal reserves			945		945	945
cb) Other retained earnings			92,200		92,200	92,200
TOTAL EQUITY AND LIABILITIES				75,891,240	75,156,378	36,825,975
CONTINGENT LIABILITIES		(17)				
Liabilities from guarantees and indemnity agreements				376,424	452,347	438,227
OTHER COMMITMENTS		(18)				
Irrevocable loan commitments				5,770,066	5,840,788	3,468,647

PROFIT AND LOSS ACCOUNT

FOR THE PERIOD FROM 1 JANUARY TO 31 DECEMBER 2018

	€ 000's	Note	€ 000's	2018 € 000's	2017 € 000's	DG HYP 2017 € 000's
INTEREST INCOME FROM		(26)				
a) Lending and money market transactions			1,693,698		1,757,286	859,438
b) Fixed-income securities and debt register claims			309,372		308,885	210,305
				2,003,070	2,066,171	1,069,743
INTEREST EXPENSES		(26)		1,482,293	1,587,679	796,255
				520,777	478,492	273,488
CURRENT INCOME FROM PARTICIPATIONS				156	123	123
INCOME FROM PROFIT-POOLING, PROFIT TRANSFER AND PARTIAL PROFIT TRANSFER AGREEMENTS				2,544	2,185	2,185
COMMISSION INCOME			31,776		40,245	39,122
COMMISSION EXPENSES			59,135		55,845	4,909
NET COMMISSION RESULT				-27,359	-15,600	34,213
OTHER OPERATING INCOME		(27)		27,973	21,539	17,629
GENERAL ADMINISTRATIVE EXPENSES						
a) Personnel expenses						
aa) Wages and salaries			78,372		70,989	43,657
ab) Compulsory social security contributions and expenses for pensions and other employee benefits			18,859		13,950	7,987
			97,231		84,939	51,644
of which: pension expenses	8,620				(3,776)	(2,257)
b) Other administrative expenses			191,938		138,570	73,917
				289,169	223,509	125,561
AMORTISATION/DEPRECIATION AND WRITE-DOWNS OF INTANGIBLE AND TANGIBLE FIXED ASSETS				5,002	4,282	3,046
OTHER OPERATING EXPENSES		(28)		20,047	24,181	21,306
WRITE-DOWNS AND VALUATION ALLOWANCES OF LOANS AND ADVANCES AND SPECIFIC SECURITIES, AS WELL AS ADDITIONS TO LOAN LOSS PROVISIONS				68,691	22,817	5,949
INCOME FROM WRITE-UPS TO PARTICIPATING INTERESTS, SHARES IN AFFILIATED COMPANIES, AND INVESTMENT SECURITIES				38,469	69,391	1,626
ALLOCATION TO THE FUND FOR GENERAL BANKING RISKS				45,000	100,200	40,000
RESULT FROM ORDINARY ACTIVITIES				134,651	181,141	133,402
INCOME TAXES		(29)	59,664		89,493	67,168
OTHER TAXES NOT DISCLOSED UNDER 'OTHER OPERATING EXPENSES'			3,680		359	145
				63,344	89,852	67,313
PROFITS TRANSFERRED UNDER PROFIT TRANSFER AGREEMENTS				55,000	75,200	50,000
PROFITS TRANSFERRED UNDER PARTIAL PROFIT TRANSFER AGREEMENTS				16,307	16,089	16,089
NET INCOME				–	–	–

STATEMENT OF CHANGES IN EQUITY

	31 Dec 2017	1 Jan 2018	1 Jan 2018 after adjustment	Net income/loss	Other changes	31 Dec 2018
	€ 000's	€ 000's	€ 000's	€ 000's	€ 000's	€ 000's
SUBSCRIBED CAPITAL	(725,000)	(59,990)	(784,990)	–	–	**(784,990)**
- Share capital	90,000	59,990	149,990	–	–	**149,990**
- Silent partnership contributions	635,000	–	635,000	–	–	**635,000**
CAPITAL RESERVES	(589,113)	(295,083)	(884,196)	–	–	**(884,196)**
- Premium at issuance	113,507	295,083	408,590	–	–	**408,590**
- Other payments	475,606	–	475,606	–	–	**475,606**
RETAINED EARNINGS	(93,145)	–	(93,145)	–	–	**(93,145)**
- Legal reserves	945	–	945	–	–	**945**
- Other retained earnings	92,200	–	92,200	–	–	**92,200**
- Net retained profit	–	–	–	–	–	**–**
EQUITY	1,407,258	355,073	1,762,331	–	–	**1,762,331**

CASH FLOW STATEMENT

€ mn		2018	2017	2017 DG HYP
	NET INCOME FOR THE PERIOD (NET INCOME/LOSS INCLUDING INTERESTS OF OTHER SHAREHOLDERS AND BEFORE TAX)	131	133	133
+/-	Amortisation/depreciation, write-downs and write-ups on loans and advances, and non-current assets	3	-95	11
+/-	Increase/decrease in provisions	24	19	16
+/-	Other non-cash expenses/income	53	104	43
-/+	Profit/loss from the disposal of non-current assets	-1	-2	-2
-/+	Other adjustments (net balance)	-3	-3	-2
-/+	Increase/decrease in loans and advances to banks	-142	7	-341
-/+	Increase/decrease in loans and advances to customers	-1,820	-652	627
-/+	Increase/decrease in securities (excluding financial assets)	103	-523	-486
-/+	Increase/decrease in other assets from operating activities	46	-25	-16
+/-	Increase/decrease in liabilities to banks	1,270	2,230	1,792
+/-	Increase/decrease in liabilities to customers	-1,676	-1,834	-1,026
+/-	Increase/decrease in securitised liabilities	1,252	388	-599
+/-	Increase/decrease in other liabilities from operating activities	-71	30	2
+/-	Interest expenses/income	-523	-481	-276
+/-	Income tax expenses/income	0	22	0
+	Interest and dividend payments received	2,015	2,089	1,093
-	Interest paid	-1,496	-1,616	-824
+/-	Income tax payments	-47	-9	-11
=	CASH FLOW FROM OPERATING ACTIVITIES	-882	-218	134
+	Receipts from the disposal of financial assets	1,208	2,564	1,372
-	Payments for investments in financial assets	-784	-1,468	-667
+	Receipts from the disposal of property and equipment	0*)	0*)	0*)
-	Payments for investments in tangible fixed assets	-12	-12	-1
-	Payments for investments in intangible fixed assets	-2	-1	0*)
=	CASH FLOW FROM INVESTING ACTIVITIES	410	1,083	704
-	Dividends paid to shareholders of parent company	-68	-106	-80
-	Dividends paid to other shareholders	-16	-17	-17
+/-	Changes in cash funds due to other capital movements (net balance)	-94	-91	-91
=	CASH FLOW FROM FINANCING ACTIVITIES	-178	-214	-188
	CASH FUNDS AT THE BEGINNING OF THE PERIOD	651	0*)	0*)
+/-	Cash flow from operating activities	-882	-218	134
+/-	Cash flow from investing activities	410	1,083	704
+/-	Cash flow from financing activities	-178	-214	-188
	CASH FUNDS AT THE END OF THE PERIOD	1	651	650

*) Values less than €0.5 million

The cash funds correspond to the balances sheet item "Cash funds" and include cash on hand and balances with central banks.

NOTES TO THE FINANCIAL STATEMENTS

GENERAL NOTES

Taking effect on 1 January 2018 (merger record date), WL BANK AG Westfälische Landschaft Bodenkreditbank with its registered office in Münster (Westphalia) ("WL BANK") was merged with the former Deutsche Genossenschafts-Hypothekenbank Aktiengesellschaft ("DG HYP") whose registered office was in Hamburg.

In connection with the Commercial Register entries related to the merger, which took place on 27 July 2018, DG HYP was renamed "DZ HYP AG" ("DZ HYP" in short), with dual registered offices in Hamburg and Münster (Westphalia), through an amendment to the Articles of Incorporation. DZ HYP acquires the Commercial Register number of DG HYP (HRB 5604). In addition, the Bank holds a second Commercial Register number from Münster (HRB 17424).

(1) General information on the preparation of financial statements

The financial statements of DZ HYP for the financial year 2018 have been prepared in accordance with the provisions of the German Commercial Code (Handelsgesetzbuch – "HGB"). Furthermore, the financial statements are prepared in accordance with the Regulation on the Accounting of Credit Institutions and Financial Services Institutions (Verordnung über die Rechnungslegung der Kreditinstitute und Finanzdienstleistungsinstitute - "RechKredV") and the German Banking Act (Kreditwesengesetz - "KWG"); they fulfil the requirements of the German Stock Corporation Act (Aktiengesetz - "AktG") and the German Pfandbrief Act (Pfandbriefgesetz - "PfandBG").

Given the non-materiality of all subsidiaries, even if considered in aggregate, in accordance with section 290 (5) in conjunction with section 296 (2) of the HGB, the company has not prepared consolidated financial statements.
All amounts have been quoted in euros, in accordance with section 244 of the HGB.

(2) Accounting policies

Disclosures on the recent merger
The registration of the merger of WL BANK and DG HYP and the immediate subsequent change of the company name of DG HYP into DZ HYP was registered in the Commercial Registers on 27 July 2018. With regard to the law of obligations, the merger forming DZ HYP took place with retroactive effect as at 1 January 2018 (merger record date) in line with the merger agreement.
Any and all business transactions and other asset changes of WL BANK in the period between 1 January 2018 and 27 July 2018 (so-called "for-the-account phase") were allocated to DG HYP (DZ HYP after change of name) for accounting purposes, and are therefore fully included in these financial statements. The aggregated transfer of all assets and liabilities of WL BANK to DG HYP, including any and all rights and obligations attached thereto, took effect for accounting purposes by applying the valuation procedure option (carrying amounts taken over from acquired entity) provided under section 24 of the German Transformation Act (Umwandlungsgesetz - "UmwG"). Effective 1 January 2018, the Bank took over the carrying amounts from the audited annual financial statements dated 31 December 2017 of the former WL BANK, which have been given an unqualified audit opinion. In line with section 17 (2) of the UmwG, WL BANK's closing balance sheet dated 31 December 2017 was used as the basis to transfer former WL BANK's assets and liabilities to the accounting system of DZ HYP.

Merger-related changes and comparability
Given the aforementioned merger effective 1 January 2018, and to improve comparability within the meaning of section 265 (2) of the HGB, in these financial statements, the Bank decided to (a) include the post-merger balance sheet values as at 1 January 2018 in the balance sheet 2018 (i.e. the balance sheet also comprises the values increased by the assets and liabilities acquired from WL BANK), and to (b) include the summarised values disclosed in the profit and loss accounts 2017 of former DG HYP and WL BANK in the

profit and loss account for 2018.

The figures of the former DG HYP (as disclosed in DG HYP's annual financial statements dated 31 December 2017) are disclosed as a third column, headed "Former DG HYP – 31 December 2017" in the balance sheet, or "Former DG HYP – 2017" in the profit and loss account and cash flow statement. In the notes, previous-year figures of former DG HYP (as disclosed by DG HYP in its notes dated 31 December 2017) are generally not disclosed again in order to improve readability. In the notes, previous-year figures of former DG HYP (as disclosed by DG HYP in its notes dated 31 December 2017) are only disclosed if required by law.

Material changes in accounting policies

These annual financial statements of DZ HYP as at 31 December 2018 are generally based on the same accounting policies as were applied in the annual financial statements of the former DG HYP as at 31 December 2017. However, given that the assets and liabilities transferred – as part of the merger in line with the valuation procedure option from WL BANK's closing balance sheet as at 1 January 2018 – were partly disclosed according to different accounting policies, various adjustments to these items were necessary to align them with the accounting policies applied at the former DG HYP in order to prepare these interim condensed financial statements as at 30 June 2018 (necessary and permissible deviation from the generally applicable principle of accounting continuity at WL BANK). In particular the following merger-related adjustments were made during the preparation of these interim condensed financial statements:

» Application of uniform valuation parameters for pension obligations: DZ HYP used Dr Klaus Heubeck's 2018 G actuarial tables (revised version from 2 October 2018) as the uniform calculation basis applicable as at 31 December 2018 (DG HYP and WL BANK used Dr Klaus Heubeck's 2005 G actuarial tables as uniform calculation basis as at 31 December 2017); future salary increases of 2.5 per cent p.a. (in line with DG HYP's former approach applied until 31 December 2017, whereas WL BANK was using an increase of 3.0 per cent p.a. up until 31 December 2017); pension increases of 1.75 per cent p.a. (also applied by both former entities up until 31 December 2017); the discount rate of 3.21 per cent applied by DZ HYP is based on the average market interest rate for the last 10 years and a notional remaining term of 15 years as established by Deutsche Bundesbank (as at 31 December 2017, a discount rate of 3.68 per cent was applied by both former entities).

» Adjustment of portfolio items to reflect the value changes due to spot rate fluctuations for cross-currency swaps and foreign exchange forwards, which – together with the respective FX underlying transactions – fulfil the requirements of section 340h of the HGB (special coverage) to the disclosure items used at DZ HYP. Regarding foreign exchange forwards, these adjustments are disclosed in the foreign exchange compensation item under other assets or other liabilities (at former WL BANK, such FX differences were disclosed in the compensation item of the respective underlying transaction). Regarding cross-currency swaps, these adjustments are disclosed under loans and advances to banks, or liabilities to banks (at former WL BANK, these adjustments were disclosed under other receivables or other liabilities).

» Uniform use of hedging relationships: at the former WL BANK, various hedging relationships were recognised in line with HGB requirements, while the former DG HYP did not recognise any hedging relationships. According to the new uniform DZ HYP policy for the recognition of hedging relationships, applicable as from 1 January 2018, hedging relationships within the meaning of the HGB shall (exclusively) be recognised for two specific accounting cases: interest rate hedging for securities held as liquidity reserve, and hedging of structured products (which have to be accounted for separately) using stand-alone opposing derivatives. Given that these two specific accounting cases did not occur in the existing or new business, no hedging relationships have been recognised since 1 January 2018. Given that it does not fulfil the requirements of DZ HYP's new policy, the legacy portfolio of WL BANK's hedging relationships was dissolved, with the resulting effects recognised directly in equity, as part of the other merger-related adjustments made to the Group's accounting policies. The previously recognised hedging derivatives and underlying transactions of the dissolved legacy portfolio were considered in the fair value measurement (verlustfreie Bewertung) of the banking book.

» Given the merger, the following changes in the fair value measurement of the interest-related banking book ("interest rate book") applied as from 31 December 2018: until 31 December 2017, DG HYP maintained a (single) interest rate book (given that DG HYP only applied a single management approach for the interest rate risks associated with the banking book). However, effective 31 December 2018, DZ HYP was obliged to perform provision testing within the meaning of IDW RS BFA 3 for two interest rate books, given that the interest rate risks of the Hamburg banking book and the Münster banking book were still managed separately at the lower (primary) management level in 2018 for system-related reasons.

Compared to the financial statements dated 31 December 2017, there were additional changes to the Bank's accounting methods, which were not, or not exclusively, attributable to the merger:

» Among these changes was the measurement of loss allowance (specific allowances, portfolio loss allowances as well as provisions for loan commitments), which have so far been recognised in line with IAS 39. The Bank introduced IFRS 9 as at 1 January 2018 – including for the purposes of German commercial law – and thus has applied the respective loss allowance provisions since that date. This relates, in particular, to the introduction of the two-stage approach in line with IFRS 9, according to which the Bank shall recognise loss allowance in the amount of 12-month expected credit losses for lending transactions where credit risk has not increased significantly compared to a defined threshold value since initial recognition (stage 1 lending transactions), and in the amount of lifetime expected credit losses for lending transactions where credit risk has increased significantly compared to the defined threshold value since initial recognition (stage 2 lending transactions). Furthermore, DZ HYP now uses individual economic parameters to evaluate stage 1 and stage 2 loss allowance instead of the supervisory parameters that have partly been used so far. The new loss allowance accounting policy was designed to provide the reader of financial statements with a more accurate, fair and true view of the assets and liabilities of the Bank. In addition, this change in accounting policies ensures that loss allowance accounting processes remain streamlined for HGB and IFRS purposes. These changes led to a decline in loss allowance of € 3.6 million (income recognised in the profit and loss account item "Write-downs and valuation allowances of loans and advances and specific securities, as well as additions to loss allowance").

» Another change in accounting policies applies to the accounting method for repurchased liabilities, which was indirectly associated with the merger. Such realisation effects had only a minor impact at former DG HYP, and were disclosed within net interest income. However, after the merger with former WL BANK, these items increased by € 29.8 million, and are therefore material. Given that former WL BANK's accounting method for repurchased liabilities was better streamlined with the overall bank management, DZ HYP took over this approach (realisation effects are included in cross-compensation according to section 340f (3) of the HGB). Therefore, as from 1 January 2018, realisation effects resulting from repurchased liabilities are included in cross-compensations at DZ HYP.

Loans and advances to banks/to customers

Loans and advances to banks and customers are recognised at nominal value, in accordance with section 340e (2) of the HGB. Where their stated value differs from the amount disbursed, or cost, the amount of the difference is reported under prepaid expenses or deferred income, and amortised in interest income over the term of the transaction.

Loans and advances which are fully classified as current assets are valued strictly at the lower of cost or market. All existing individual lending risks are covered by specific loss allowances.

Specific provisions are recognised when the Bank has reason to doubt the performance of a receivable, due to the difficult financial circumstances of a borrower, or in the event of insufficient collateralisation; or if there are indications that the borrower will be unable to pay interest on a sustainable basis. The same applies to contingent receivables. Specific provisions must be recognised in accordance with the requirements of German commercial law, especially observing the principle of prudence.

Regarding the calculation of specific provisions, DZ HYP was generally required to use different methods for the sub-portfolios of former DG HYP and WL BANK. DZ HYP is currently working at streamlining the calculation methods, which will be continued throughout 2019.

For instance, since the introduction of IFRS 9 (1 January 2018), specific provisions for the sub-portfolios of former DG HYP are based either on a "run-down" or a "survival scenario", whereas the sub-portfolios of former WL BANK are subject to an exclusive run-down approach. Furthermore, interest receivables were considered in specific provision calculations only for the sub-portfolios of former DG HYP. Expected future cash flows from the asset serving as collateral (based on the net collateral value) are discounted to the reference date, weighted, and compared with the residual claim. A specific provision will be recognised for the portion of the loan receivable not covered by the weighted present value of the net collateral value.

Inherent default risks and country risks are covered by portfolio-based loss allowances, which are derived using a model similar to the IFRS 9 impairment loss model. Additional loss allowances were set aside in accordance with section 340f of the HGB.

When recognising loss allowances, DZ HYP applies the option to cross-compensate all income and expense items in line with section 340f (3) as well as section 340c (2) of the HGB.

Debt securities and other fixed-income securities
Bonds and debt securities held as fixed assets are measured at amortised cost; if impairments are expected to be permanent, DZ HYP recognises a write-down to the lower observable closing rate ("gemildertes Niederstwertprinzip"). Other bonds and debt securities are allocated to the liquidity reserve. These items are measured at the lower of cost and fair value ("strenges Niederstwertprinzip").

The vast majority of bonds and debt securities held as fixed assets are used in coverage calculations as ordinary or extended cover. The difference between cost and redemption amount is disclosed in net interest income during the remaining term. Reclassifications from the liquidity reserve to fixed assets are made in accordance with IDW RH HFA 1.014.

The fair value of liquid debt securities and other fixed-income securities is generally determined on the basis of external market prices. If a valid market price for securities already held cannot be determined as at the balance sheet date, due to a lack of transaction volume, spread curves are used to determine the relevant price on the basis of the discounted cash flow method; this applies to only a limited number of items at DZ HYP. Future cash flows from interest and principal were discounted to their present value as at the balance sheet date, using market interest rates in line with the risks and maturities concerned. If specific parameters needed for valuation purposes cannot be observed on the market, and cannot be derived from market data, DZ HYP applies parameters estimated within the DZ BANK Group.

The valuation of securities held as fixed assets, or included in the liquidity reserve, is generally based on an individual approach.

Participations and interests in affiliated companies
Investments and shares in affiliated companies are measured at amortised cost, or at the lower fair values in case of permanent impairments.

Intangible and tangible fixed assets
According to section 253 (1) and (3) of the HGB, intangible and tangible fixed assets are measured at cost less depreciation, amortisation and impairment losses. Depreciation and amortisation are recognised monthly on a straight-line basis, taking the expected useful life into account. Low-value assets disclosed under intangible and tangible fixed assets with cost of between € 250 and € 800 (after deducting any pre-tax amounts) are recognised in the balance sheet in the year of acquisition, and amortised/depreciated immediately. Assets with cost of less than € 250 are recognised through profit or loss in the year of acquisition.

Standard software is reported under intangible assets, as prescribed by accounting standard HFA 11 issued by the Main Committee of the IDW (IDW RS HFA 11).

Liabilities
Liabilities are recognised at their settlement amount in accordance with section 253 (1) s. 2 of the HGB. The difference between the nominal value and the initial carrying amount of liabilities is recognised under prepaid expenses or deferred income, and amortised over the term of the transaction.

Zero bonds are shown at their issue value, plus pro-rata interest in line with the yield at the time of issue.

Liabilities classified as structured products (as defined in Accounting Standard 22 issued by the Auditing and Accounting Board of the IDW) are accounted for as uniform liabilities, since such products at DZ HYP exclusively contain interest rate derivative components, which do not have to be accounted for separately.

Provisions
Provisions for pensions are recognised in accordance with actuarial principles and determined on the basis of the projected unit credit method, using Dr Klaus Heubeck's 2018 G actuarial tables (revised version from 2 October 2018). The calculation of the provisions takes into account future salary increases of 2.5 per cent p.a. as well as pension increases of 1.75 per cent p.a. DZ HYP uses the average market interest rate for the last 10 years and a notional remaining term of 15 years as established by Deutsche Bundesbank in accordance with section 253 (2) of the HGB (3.21 per cent).

Due to amended legal requirements, the calculation of pension provisions was adapted in 2016. The assessment period of the applied average interest rate was extended from 7 to 10 years. The positive difference according to section 253 (6) s. 1 of the HGB (i.e. the shortfall in pension provisions due to the change in the period used to determine average values to the last 10 years) stood at € 22.9 million as at year-end 2018.
DZ HYP recognises tax provisions for current taxes in accordance with tax regulations.
Other provisions are recognised for contingent liabilities or for impending losses from executory contracts in the amount of the expected settlement amounts, exercising prudent commercial judgement.
In accordance with section 253 (2) of the HGB, provisions with a remaining term of more than one year are discounted using the average market interest rate of the last seven years, in line with maturities. Income or expenses from discounting or accumulating provision items are recognised in other operating income/expenses.

Derivative financial instruments and fair value measurement of banking book
Financial derivatives are accounted for separately in auxiliary ledgers. These instruments are used to hedge against the interest rate and currency risk exposure of on-balance sheet transactions. Therefore, each derivative forms part of the overall management of the banking books in Hamburg and Münster. Segregated sub-portfolios (valuation units) are not managed on an individual basis. Accordingly, section 254 of the HGB is not applicable.

Current interest payments are amortised and recognised in net interest income.

In connection with the early redemption of hedged items recognised on the balance sheet, we also generally terminate derivative financial instruments early. Any resulting gains are usually recognised in net interest income. Where interest rate swaps can be allocated to individual securities, income realised upon closing out swaps is recognised in line with the recognition of income of the underlying transaction, in the net financial result, or in the net risk provisioning balance, respectively.

In accordance with Statement IDW RS BFA 3 (as amended) issued by the Banking Committee of the Institute of Public Auditors in Germany (IDW), the fair value measurement (verlustfreie Bewertung) of interest-related banking books ("interest rate books") is based on the present value. Interest rate books comprise both the interest-related underlying transaction as well as the interest-related derivative. Effective 31 December 2018, DZ HYP was obliged to carry out provision tests within the meaning of IDW RS BFA 3 for two interest rate books. This was due to the fact that the interest rate risks of the Hamburg banking book and the Münster banking book were still managed separately at the lower (primary) management level in 2018 for system-related reasons. As at 31 December 2018, the two provision tests resolved that no provisions pursuant to section 249 (1) sentence 1 alternative 2 of the HGB have to be recognised for either interest rate book, since the present value of the interest rate book was higher than the carrying amount of the interest rate book, less general administrative and risk costs in both cases.

Profit and loss account

Interest rate option premiums paid and received are disclosed under other liabilities, or other assets, and recognised through profit or loss in net interest income at maturity.

Prepayment fees charged for loan repayments or extensions during the fixed-interest term of a loan are fully recognised in net interest income.

Income and expenses from the valuation of the lending business and securities held in the liquidity reserve are recognised on an offset basis in accordance with section 32 of the RechKredV in conjunction with section 340f (3) of the HGB. Expenses from financial investments are offset against the corresponding income items in accordance with section 33 of the RechKredV in conjunction with section 340c (2) of the HGB.

(3) Currency translation

Assets and liabilities from foreign exchange transactions are translated in line with section 340h in conjunction with section 256a of the HGB and the Statement IDW RS BFA 4 issued by the Banking Committee of the Institute of Public Auditors in Germany (IDW). Book receivables, securities, liabilities and unsettled spot transactions as well as foreign exchange forwards and cross-currency swaps denominated in foreign currencies entered into for FX hedging purposes are translated into euro, using the ECB reference rate on the balance sheet date. Regarding foreign exchange forwards entered into in order to hedge interest-bearing balance sheet items, currency translations are made by splitting the forward rate into the spot rate and the swap rate in line with IDW RS BFA 4. Due to the specific coverage of all existing foreign currency items, all currency translation effects have been recognised in income. Currency translation effects (as well as any realised FX effects) are recognised in other operating income.

NOTES TO THE BALANCE SHEET

(4) Lending business

MORTGAGE LOANS	Principal € mn	Carrying amount € mn
to banks	20	20
to customers	42,807	42,890
Total	42,827	42,910

PORTFOLIO DEVELOPMENT (PRINCIPAL)	€ mn	€ mn
Balance at 31 Dec 2017		39,903
ADDITIONS DURING THE FINANCIAL YEAR 2018		9,199
through Disbursements	9,144	
Reclassifications	3	
Other additions	52	
DISPOSALS DURING THE FINANCIAL YEAR 2018		6,275
through Scheduled and unscheduled redemptions/repayments	5,329	
Reclassifications	946	
Other disposals	0	
BALANCE AT 31 DEC 2018		42,827

LOANS TO LOCAL AUTHORITIES	Principal € mn	Carrying amount € mn
to banks	317	319
to customers	14,615	14,727
Total	14,932	15,046

PORTFOLIO DEVELOPMENT (PRINCIPAL)	€ mn	€ mn
Balance at 31 Dec 2017		15,975
ADDITIONS DURING THE FINANCIAL YEAR 2018		706
through Disbursements	698	
Reclassifications	0	
Other additions	8	
DISPOSALS DURING THE FINANCIAL YEAR 2018		1,749
through Scheduled and unscheduled redemptions/repayments	1,749	
Reclassifications	0	
Other disposals	0	
BALANCE AT 31 DEC 2018		14,932

(5) Negotiable securities

Balance sheet item	Listed 31 Dec 2018 € 000's	Listed 1 Jan 2018 € 000's	Unlisted 31 Dec 2018 € 000's	Unlisted 1 Jan 2018 € 000's	Carrying amount of negotiable securities not valued at the lower of cost or market 31 Dec 2018 € 000's	Carrying amount of negotiable securities not valued at the lower of cost or market 1 Jan 2018 € 000's
Debt securities and other fixed-income securities	10,494,826	11,023,686	588,048	561,949	1,157,589	2,201,078

As at 31 December 2018, the Bank did not recognise an extraordinary write-down in the aggregate amount of € 78.6 million (1 January 2018: € 89.0 million) for negotiable securities held as fixed assets with a carrying amount of € 1,157.6 million (1 January 2018: € 2,201.1 million) and a fair value of € 1,079.0 million (1 January 2018: € 2,112.1 million) not measured at the lower of cost or market, due to the expected temporary nature of the impairment. This assessment is based on the observation that the euro area has become more stress-resistant due to the crisis mechanisms established in the recent past, and that the effects of individual stabilisation measures are becoming (or have become) increasingly evident (such as bond acquisition programmes or low-interest rate policies).

As at 31 December 2018, the hidden burdens and reserves in the Bank's portfolio of negotiable securities amounted to a total of € 1,020.8 million (1 January 2018: € 1,274.2 million). The aggregate hidden reserves were affected by changes in the swap curve (decline in overall market interest rate levels over recent years) in the amount of € 1,860.7 million (1 January 2018: € 2,061.2 million) and by the poorer credit rating for some securities compared to the date of acquisition, affecting hidden reserves with € -839.9 million (1 January 2018: € -787.0 million). While DZ HYP enters into opposing primary and derivative interest rate transactions to neutralise swap curve developments and the resulting positive valuation effects for securities as part of the interest rate risk management (overall bank management) (i.e. DZ HYP does not profit from such valuation changes), the Bank fully carries the negative credit risk-related valuation changes for securities. According to its current assumptions, DZ HYP does not expect any disruptions of interest or principal payments; after an isolated consideration, the Bank did not recognise any impairments in connection with credit risk-related valuation losses. Please refer to the Bank's management report (chapter "net assets") for further information on the securities portfolio.

(6) Breakdown of, and statement of changes in fixed assets

	Purchase or production cost					
	Former DG HYP 31 Dec 2017 € 000's	Addition by merger € 000's	1 Jan 2018 € 000's	Additions € 000's	Reclassifications € 000's	Disposals € 000's
I. INTANGIBLE ASSETS						
1. Software	20,777	1,529	22,306	1,048	213	86
2. Advance payments made on intangible assets	24	152	176	758	–213	334
	20,801	1,681	22,482	1,806	–	420
II. TANGIBLE FIXED ASSETS						
1. Land and buildings	179,398	27,891	207,289	11,591	–	–
2. Office furniture and equipment **)	4,986	6,379	11,365	805	–	998
	184,384	34,270	218,654	12,396	–	998
					Additions	
III. FINANCIAL ASSETS						
1. Participations	524	387	911		–	
2. Investments in affiliated companies	1,566	–	1,566		–	
3. Investment securities	5,858,779	4,947,065	10,805,844		949,955	
	5,860,869	4,947,452	10,808,321		949,955	

	Depreciation and amortisation				Carrying amounts		
	in the financial year € 000's	Reclassifications € 000's	Disposals € 000's	Total € 000's	31 Dec 2018 € 000's	1 Jan 2018 € 000's	Former DG HYP 31 Dec 2017 € 000's
I. INTANGIBLE ASSETS							
1. Software	1,228	–	86	21,636	1,845	1,812	1,231
2. Advance payments made on intangible assets	–	–	–	–	387	176	24
	1,228	–	86	21,636	2,232	1,988	1,255
II. TANGIBLE FIXED ASSETS							
1. Land and buildings	2,461	–	–	47,211	171,669*)	162,538	138,338
2. Office furniture and equipment **)	1,312	–	989	8,417	2,755	3,277	1,652
	3,773	–	989	55,628	174,424	165,815	139,990
		Disposals					
III. FINANCIAL ASSETS							
1. Participations		–			911	911	524
2. Investments in affiliated companies		–			1,566	1,566	1,566
3. Investment securities		1,421,539			10,334,260	10,723,613	5,733,627
		1,421,539			10,336,737	10,726,090	5,735,717

*) of which: owner-occupied properties: € 67.6 million; used by third parties: € 104.0 million.
**) fully used for the Bank's own operations.

(7) Trust business

	31 Dec 2018 € 000's	1 Jan 2018 € 000's
Assets held in trust comprise:		
- Loans and advances to customers	23,802	44,345
- Participations	18,100	18,100
	41,902	**62,445**
Trust liabilities are carried vis-à-vis:		
- Banks	14,960	17,574
- Customers	26,942	44,871
	41,902	**62,445**

(8) Other assets

Other assets of € 29.6 million (1 January 2018: € 38.1 million) mainly include the cash collateral for the restructuring fund (€ 21.6 million), reinsurance coverage claims of € 3.2 million, as well as claims against VR WERT Gesellschaft für Immobilienbewertungen mbH, Hamburg (profit transfer 2018) of € 2.5 million.

(9) List of investments pursuant to sections 285 no. 11 and 340a of the HGB

Minimum stake of 20% Name/registered office	Equity interest per cent	Equity € 000's	Result 2018 € 000's
VR WERT Gesellschaft für Immobilienbewertungen mbH, Hamburg	100.0	50	2,544*)
VR HYP GmbH, Hamburg	100.0	25	– **)
VR REAL ESTATE GmbH, Hamburg	100.0	25	– **)
TXS GmbH, Hamburg	24.5	200	616**)

*) Control and profit and loss transfer agreement with DZ HYP.
**) Result for the financial year 2017.

(10) Prepaid expenses and deferred income

	31 Dec 2018 € 000's	1 Jan 2018 € 000's	31 Dec 2017 DG HYP € 000's
PREPAID EXPENSES			
Sub-item a) From new issues and lending comprises:			
Difference between the nominal amount and the higher disbursement amount of receivables	43,766	32,401	12,920
Difference between the nominal amount and the lower issuing amount of liabilities	88,580	89,001	20,837
LIABILITIES AND EQUITY			
Sub-item a) From new issues and lending comprises:			
Difference between the nominal amount and the lower disbursement amount of receivables	22,795	29,872	18,190

(11) Open-market transactions

	31 Dec 2018 € 000's	1 Jan 2018 € 000's
Open-market transactions entered into with the European Central Bank	1,588,293	1,600,000

(12) Securities repurchase agreements

	31 Dec 2018 € 000's	1 Jan 2018 € 000's
Carrying amount of securities pledged under repo agreements Securities	2,931,252	1,237,208
Repurchase amount	3,073,542	1,304,469

(13) Breakdown of, and statement of changes in debt securities and borrowed funds

	Principal € mn	Carrying amount € mn
REGISTERED MORTGAGE PFANDBRIEFE		
to banks	2,098	2,126
to customers	6,436	6,528
MORTGAGE PFANDBRIEFE	20.398	20,484
	28,932	**29,138**
REGISTERED PUBLIC PFANDBRIEFE		
to banks	1,073	1,087
to customers	10,460	10,706
PUBLIC PFANDBRIEFE	3,605	3,625
	15,138	**15,418**
OTHER DEBT SECURITIES	**2,364**	**2,379**
BORROWED FUNDS		
from banks	18,094	18,151
from customers	1,711	1,736
	19,805	**19,887**
TOTAL	**66,239**	**66,822**

DEVELOPMENT (PRINCIPAL)

	Balance on 1 Jan 2018	Additions	Disposals	Reclassifications and other adjustments	Balance on 31 Dec 2018
	€ mn	€ mn	€ mn	€ mn	€ mn
Mortgage Pfandbriefe and Registered Mortgage Pfandbriefe	27,317	4,506	2,891	–	28,932
Public Pfandbriefe and Registered Public Pfandbriefe	16,901	151	1,940	26	15,138
Other debt securities	3,053	98	787	–	2,364
Borrowed funds	18,748	5,008	3,951	–	19,805
Total	**66,019**	**9,763**	**9,569**	**26**	**66,239**

(14) Other liabilities

This item amounts to € 170.0 million (1 January 2018: € 207.0 million) and mainly comprises liabilities from tax allocations of € 78.1 million, liabilities from profit transfers of € 55.0 million, as well as € 16.3 million in profits to be transferred under partial profit transfer agreements in connection with silent capital contributions.

(15) Subordinated liabilities

	31 Dec 2018 € 000's	1 Jan 2018 € 000's
SUBORDINATED		
other debt securities	67,000	157,000
borrowed funds	13,750	17,718
	80,750	**174,718**
INTEREST EXPENSES 2018	4,693	7,019

Pursuant to the CRR, subordinated liabilities in the amount of € 40.4 million qualify as tier 2 capital in the determination of own funds for regulatory purposes. Early repayment obligations are not provided for in all cases. There are no provisions or plans for a conversion of such funds to capital, or into another form of debt.

Subordinated liabilities carry an average interest of 5.64 per cent, and have original maturities of between 10 and 20 years.

Disclosures on subordinated liabilities amounting to 10.0 per cent or more of the aggregate amount of subordinated liabilities:

Amount € mn	Currency	Coupon *) %	Maturity
25.0	EUR	6.61	21 Mar 2022
10.0	EUR	6.14	5 Sep 2023

*) as at 31/12/2018

(16) Equity

DZ HYP reported equity of € 1,762.3 million as at 31 December 2018 (1 January 2018: € 1,762.3 million; former DG HYP as at 31 December 2017: € 1,407.3 million).

The € 355.1 million increase in equity compared to 31 December 2017 reflects the capital increase carried out in connection with the merger of WL BANK and DG HYP.

As part of the merger process with WL BANK, the General Meeting of Shareholders of former DG HYP resolved to increase subscribed capital (share capital) from € 90,000,000.00 by up to € 59,991,402.86, via issuance of up to 2,332,999 shares. The conversion ratio of 1:13.991 was agreed upon in the merger agreement, and approved by the merger auditor. The capital increase by issuance of 2,332,942 no-par value bearer shares (the number of issued shares was 57 below the permissible maximum number), with a notional value of € 25.7142857143 per share (total share capital increase of € 59,989,937.14), was entered into the Commercial Register of the Hamburg District Court on 27 July 2018. The new shares carry full dividend rights from 1 January 2018. The portion of WL BANK's net assets (total book value of € 355,083,712.81) in excess of the share capital increase was allocated to the capital reserve in accordance with section 272 (2) no. 1 of the HGB (premium for share issues) following deduction of additional cash payments (WL BANK shareholders received additional cash payments of € 11,349.25), i.e. the capital reserve was increased by € 295,082,426.42.

After the capital increase, the share capital amounts to € 149,989,937.14 and is divided into 5,832,942 notional no-par value shares ("unit shares"). No shareholder of the former WL BANK objected to the merger, meaning that no repurchase of shares to DZ HYP were made after the share issuance.

DZ BANK AG Deutsche Zentral-Genossenschaftsbank, Frankfurt am Main, has given notice pursuant to section 20 (4) of the German Stock Corporation Act (Aktiengesetz – "AktG") that it holds a majority shareholding. With effect from 31 December 2012, DZ BANK issued an unrestricted letter of comfort for DG HYP (DZ HYP after change of company name). According to the still-valid unrestricted letter of comfort, except in the event of political risk, DZ BANK has undertaken to ensure (in total for the consolidated entity DZ HYP) that DZ HYP is able to meet its contractual obligations.

Silent partnership contributions in the amount of € 635.0 million are open-ended and comply with the provisions of section 10 (4) of the KWG on the balance sheet date. The silent partnership contributions are partial profit transfer agreements within the meaning of section 292 (1) no. 2 of the AktG. Pursuant to the transitional regulations of the CRR, € 254.0 million of the silent capital contributions are considered as tier 1 capital. The remaining € 381.0 million is included in tier 2 capital.

(17) Contingent liabilities

Contingent liabilities of € 376.4 million (1 January 2018: € 452.3 million) comprise mainly guarantees for commercial real estate loans, € 168.1 million of which are extended to DZ BANK. DZ HYP's credit risk management is responsible for monitoring contingent liabilities.

(18) Other commitments

Irrevocable loan commitments of € 5,770,1 million (1 January 2018: € 5,840.8 million) are related primarily to mortgage financing, and were decreased by € 2.4 million in provisions for contingent losses.

(19) Obligations

DZ HYP is a member of the BVR Institutssicherung GmbH (BVR-ISG) and the deposit insurance scheme of the National Association of German Cooperative Banks (Bundesverband der Deutschen Volksbanken und Raiffeisenbanken – "BVR"). According to the articles of association of the deposit insurance scheme of the BVR, the institutions merging into DZ HYP, i.e. WL BANK and DG HYP, issued letters of indemnity to BVR. As a result, DG HYP is liable to contingent liabilities in the amount of € 34.8 million.

According to BVR-ISG’s articles of association, the merging institutions WL BANK and DG HYP, now constituting DZ HYP, have undertaken to make special contributions and payments to BVR-ISG in proportion to the volume of the covered deposits. Pursuant to section 27 (4) of the German Deposit Guarantee Act (Einlagensicherungsgesetz), BVR-ISG may generally raise, as a statutory deposit guarantee scheme, special contributions and payments of a maximum amount of up to 0.5 per cent of the covered deposits of the credit institutions allocated to it within a given settlement year.

(20) Relationships with affiliated enterprises and subsidiaries

AFFILIATED COMPANIES

	31 Dec 2018 € 000’s	1 Jan 2018 € 000's	31 Dec 2017 DG HYP € 000's
Loans and advances to			
- banks	2,105,454	1,728,678	1,526,644
- customers	41,982	43,019	34,642
Other assets	7,489	6,175	2,610
Liabilities to			
- banks	21,120,949	19,104,107	16,135,550
- customers	720,278	823,529	303,341
Other liabilities	152,703	187,397	134,027
Other provisions	–	80	–
Subordinated liabilities	18,000	108,000	–

Subsidiaries

As at the reporting date, liabilities to subsidiaries amounted to € 30,000 (1 January 2018: € 9,000; former DG HYP as at 31 December 2017: € 9,000); loans and advances to subsidiaries amounted to € 1,000 (1 January 2018: € 0; former DG HYP as at 31 December 2017: € 0).

(21) Related-party transactions

There were no related-party transactions entered into – at terms not in line with prevailing market terms – which would give rise to a disclosure duty pursuant to section 285 no. 21 of the HGB.

(22) Breakdown of maturities for loans and advances, and liabilities

		31 Dec 2018 € 000’s	1 Jan 2018 € 000's
ASSETS			
Loans and advances to banks			
Remaining term	**- payable on demand**	2,853,205	1,948,836
	- up to three months	1,164,646	1,845,896
	- between three months and one year	25,674	157,402
	- between one year and five years	254,593	183,688
	- more than five years	58,659	79,507
		4,356,777	**4,215,329**
Loans and advances to customers			
Remaining term	**- payable on demand**	209,541	405,992
	- up to three months	1,338,799	1,372,423
	- between three months and one year	3,952,433	3,471,395
	- between one year and five years	18,031,401	17,845,615
	- more than five years	36,507,592	35,160,759
		60,039,766	**58,256,184**
Debt securities and other fixed-income securities maturing in the following year		859,021	717,816
LIABILITIES			
Liabilities to banks			
Remaining term	**- payable on demand**	79,764	399,785
	- up to three months	4,545,813	3,015,642
	- between three months and one year	2,383,421	3,605,590
	- between one year and five years	9,939,007	10,235,356
	- more than five years	9,968,131	8,384,887
		26,916,136	**25,641,260**
Liabilities to customers			
Remaining term	**- payable on demand**	507,059	602,944
	- up to three months	1,046,171	902,565
	- between three months and one year	940,411	954,208
	- between one year and five years	3,626,837	4,150,434
	- more than five years	13,413,426	14,616,342
		19,533,904	**21,226,493**
Certificated liabilities maturing in the following year		3,027,598	2,656,338

(23) Assets and liabilities in foreign currencies

	31 Dec 2018 € 000's	1 Jan 2018 € 000's
Assets include foreign-currency receivables in the total amount of	2,418,385	2,622,862
Liabilities and equity include foreign-currency liabilities in the total amount of	672,285	749,186

(24) Forward contracts not reflected in the balance sheet

The following types of forward transactions based on foreign currencies, interest rates or other underlying instruments were outstanding as at the balance sheet date:

	Nominal amounts by residual term			Total		Fair value			
						31 Dec 2018		1 Jan 2018	
€ mn	≤ 1 year	> 1 – 5 yrs	> 5 yrs	31 Dec 2018	1 Jan 2018	positive	negative	positive	negative
Interest rate instruments *)	12,674	37,985	70,326	120,985	116,715	3,549	5,477	4,030	6,215
Currency-related instruments	66	1,225	873	2,164	2,366	95	164	114	150
Credit-related transactions	-	21	58	79	76	7	-	8	-
Total	**12,740**	**39,231**	**71,257**	**123,228**	119,157	**3,651**	**5,641**	4,152	6,365

*) Including interest rate swaps with identical foreign currency

The breakdown of the carrying amounts of forward contracts not reflected on the balance sheet by balance sheet items pursuant to section 285 no. 19 of the HGB is as follows:

	Carrying amount 31 Dec 2018 € mn	Carrying amount 1 Jan 2018 € mn	Balance sheet item Assets	Carrying amount 31 Dec 2018 € mn	Carrying amount 1 Jan 2018 € mn	Balance sheet item liabilities
Interest-based transactions	432	310	Loans and advances to banks, loans and advances to customers, prepaid expenses, other assets	459	389	Liabilities to banks, liabilities to customers, deferred income, other liabilities
Currency-based transactions	40	65	Loans and advances to banks, loans and advances to customers, prepaid expenses, other assets	75	67	Liabilities to banks, liabilities to customers, deferred income, other liabilities
Rating-based transactions	4	4	Loans and advances to banks, prepaid expenses	2	3	Provisions

The forward transactions identified above are used to manage interest rate, currency and counterparty credit risk exposure. As a rule, counterparties are OECD banks, OECD financial services institutions or OECD central governments. In addition, borrowers also appear as counterparties (market value € 37.7 million) in connection with loan agreements.

Interest rate and currency swaps are valued using present values, determined by discounting cash flows to their present value as at the balance sheet date using interest rates in line with the credit risk and maturities concerned, as indicated by individual yield curves prevailing on the balance sheet date. Furthermore, credit adjustments are applied in the valuation of such trades, to reflect default risks and closing costs. Structured products are divided into components for valuation purposes.

Options are valued using option pricing models. These are applied on the basis of generally recognised assumptions regarding valuation parameters; in particular, the value and volatility of the underlying instrument, the agreed exercise price (interest rate), the remaining lifetime of the contract, as well as the risk-free interest rate for that lifetime. Regarding the valuation of foreign exchange forwards, the respective cash flows are translated into euro using the corresponding foreign currency rate, and discounted using the market interest rate appropriate to the risk level and maturity.

Credit derivatives are valued on an individual basis, predominantly on the basis of the default probability of the reference obligations concerned. Provisions have been recognised in the amount of € 2.4 million (01/01/2018: € 2.9 million) for the three total return swaps held since 2006 and 2007, respectively, in order to hedge the immediate counterparty risk exposure.

Market values are determined without consideration of netting agreements. The market values of derivatives are offset by compensating market values of the related hedged balance sheet items at overall bank level. Cash collateral was provided for derivatives, as part of the bank's collateral management, in the amount of € 1,981.6 million (01/01/2018: € 2,126.9 million).

NOTES TO THE PROFIT AND LOSS ACCOUNT

(25) Breakdown of income by geographic markets within the meaning of section 34 (2) no. 1 of the RechKredV

The breakdown of interest income, current income from equities and other non-fixed income securities, commission income and other operating income is as follows:

in %	2018	2017
GERMANY	84.1	83.2
INTERNATIONAL	15.9	16.8

(26) Interest expenses and income

Interest payments made and received in connection with derivative transactions, which are used to manage the overall interest rate risk, are recognised on a net basis in interest income or expenses. In individual exceptional cases, derivative transactions may be terminated early; the resulting compensation payments are recognised in net interest income.

Negative interest rates on financial assets and financial liabilities, due to the prevailing low interest rate environment, are offset in the profit and loss account against the corresponding interest expenses and interest income items. Overall, interest income as disclosed in the profit and loss account comprised negative interest rates in the amount of € 8.7 million, which was considered insignificant (previous year DZ HYP: € 12.4 million). Interest expenses comprised positive interest rates of € 18.5 million (previous year DZ HYP: € 7.8 million).

(27) Other operating income

Other operating income of € 28.0 million (previous year DZ HYP: € 21.5 million) was mostly due to rental income totalling € 9.0 million, income from the reversal of provisions totalling € 8.2 million as well as service income totalling € 7.2 million.

(28) Other operating expenses

Other operating expenses totalling € 20.0 million (previous year DZ HYP: € 24.2 million) largely include expenses of € 15.9 million for the discounting of provisions for pensions and similar obligations, and expenses for buildings not directly used for Bank business of € 2.1 million.

(29) Income taxes

Income taxes (2018: € 59.7 million; previous year DZ HYP: € 89.5 million) mainly comprise tax levies of the controlling company, DZ BANK AG, Deutsche Zentral-Genossenschaftsbank, Frankfurt am Main, Germany, amounting to € 78.2 million for the year under review and previous years. Furthermore, income taxes include the compensation payments to minority shareholders of € 0.2 million according to section 16 of the KStG, for which DZ HYP has to carry the respective tax payments, as well as one-off tax effects, which are due to the merger, in the amount of € 18.7 million.

COVERAGE

(30) Coverage by balance sheet item

	Mortgage Pfandbriefe 31 Dec 2018 € mn	Mortgage Pfandbriefe 1 Jan 2018 € mn	Public Pfandbriefe 31 Dec 2018 € mn	Public Pfandbriefe 1 Jan 2018 € mn
ORDINARY COVER	31,985	30,335	18,378	19,518
LOANS AND ADVANCES TO CUSTOMERS	31,871	30,221	14,786	15,571
Loans secured by property mortgages	31,871	30,221	53*)	57*)
Loans to local authorities	–	–	14,733	15,514
LOANS AND ADVANCES TO BANKS	20	20	98	284
Loans secured by property mortgages	20	20	–	–
Loans to local authorities	–	–	98	284
DEBT SECURITIES	–	–	3,493	3,663
BANK BUILDINGS	94	94	–	–
EXTENDED COVER	1,176	1,590	36	17
LOANS AND ADVANCES TO BANKS	0	650	36	17
Monetary claims	0	650	36	17
DEBT SECURITIES	1,176	940	–	–
Total	33,161	31,925	18,414	19,535

*) Under a municipal guarantee

(31) Details pursuant to section 28 of the German Pfandbrief Act

Outstanding Pfandbriefe and related cover assets

	Nominal amount		Present value		Risk-adjusted present value *)	
a) Total amount of outstanding	31 Dec 2018 € mn	1 Jan 2018 € mn	31 Dec 2018 € mn	1 Jan 2018 € mn	31 Dec 2018 € mn	1 Jan 2018 € mn
Mortgage Pfandbriefe	28,902	27,287	30,210	28,327	28,368	26,699
Cover assets pool	33,161	31,925	36,668	35,224	34,499	33,146
of which: derivatives	–	–	–	–	–	–
Excess cover	4,259	4,638	6,458	6,897	6,131	6,447
Excess cover %	14.7	17.0	21.4	24.3	21.6	24.1

*) When calculating the risk-adjusted present value, the dynamic method pursuant to section 5 (1) no. 2 of the Present Value Cover Regulation (PfandBarwertV) was used.

Ref a) Maturity structure	Mortgage Pfandbriefe 31 Dec 2018 € mn	1 Jan 2018 € mn	Cover assets pool 31 Dec 2018 € mn	1 Jan 2018 € mn
<= 6 months	1,625	1,322	1,566	2,165
> 6 months and <= 12 months	1,171	1,490	1,364	1,486
> 12 months and <= 18 months	1,634	1,112	1,297	1,355
> 18 months and <= 2 years	650	1,224	1,528	1,352
> 2 years and <= 3 years	2,123	2,295	2,990	2,968
> 3 years and <= 4 years	2,990	2,118	3,105	3,208
> 4 years and <= 5 years	2,642	3,017	2,844	2,906
> 5 years and <= 10 years	11,504	11,999	11,614	10,985
> 10 years	4,563	2,710	6,853	5,500
Total	28,902	27,287	33,161	31,925

Ref. a) Disclosure pursuant to section 6 of the German Pfandbrief Present Value Ordinance (Pfandbrief-Barwertverordnung – "PfandBarwertV")

Currency	Net present value in € 31 Dec 2018 mn	1 Jan 2018 mn
CHF	7.7	8.5
GBP	194.3	186.5
SEK	56.1	58.8
USD	43.3	57.8

Ref. a) additional indicators on Mortgage Pfandbriefe outstanding		31 Dec 2018	1 Jan 2018
Share of fixed-interest assets in total cover assets pool	%	91.0	89.0
Share of fixed-interest Pfandbriefe in liabilities to be covered	%	94.0	92.2
Total amount of assets breaching the limits as set in section 13 (1) of the PfandBG	€ mn	–	–
Average volume-weighted age of assets	in years	4.6	4.9
Average weighted loan-to-value ratio	%	54.0	50.3
Total amount of assets breaching the limits as set in section 19 (1) no. 2 of the PfandBG	€ mn	–	–
Total amount of assets breaching the limits as set in section 19 (1) no. 3 of the PfandBG	€ mn	–	–

b) Total amount of outstanding	Nominal amount 31 Dec 2018 € mn	1 Jan 2018 € mn	Present value 31 Dec 2018 € mn	1 Jan 2018 € mn	Risk-adjusted present value *) 31 Dec 2018 € mn	1 Jan 2018 € mn
Public Pfandbriefe	15,173	16,906	18,472	20,190	17,149	18,743
Cover assets pool	18,414	19,535	22,307	23,112	20,571	21,390
of which: derivatives	–	–	–	–	–	–
Excess cover	3,241	2,629	3,835	2,922	3,422	2,647
Excess cover %	21.4	15.5	20.8	14.5	20.0	14.1

*) When calculating stress scenarios, the static method is used for currencies and the dynamic method for interest rates.

Ref b) Maturity structure	Public Pfandbriefe 31 Dec 2018 € mn	1 Jan 2018 € mn	Cover assets pool 31 Dec 2018 € mn	1 Jan 2018 € mn
<= 6 months	641	596	883	856
> 6 months and <= 12 months	1,320	1,106	1,082	813
> 12 months and <= 18 months	928	595	823	725
> 18 months and <= 2 years	941	1,367	630	963
> 2 years and <= 3 years	1,101	1,917	1,316	1,430
> 3 years and <= 4 years	695	1,121	1,124	1,290
> 4 years and <= 5 years	875	741	1,096	1,099
> 5 years and <= 10 years	4,203	4,333	4,639	5,044
> 10 years	4,469	5,130	6,821	7,315
Total	15,173	16,906	18,414	19,535

Ref b) Disclosure pursuant to section 6 of the German Pfandbrief Present Value Ordinance ("Pfandbrief-Barwertverordnung")

Currency	Net present value in € 31 Dec 2018 mn	1 Jan 2018 mn
CAD	35.6	38.6
CHF	78.8	62.6
GBP	6.6	7.4
JPY	34.2	31.8
USD	67.4	76.6

Ref. b) Additional indicators on Public Pfandbriefe outstanding		31 Dec 2018	1 Jan 2018
Share of fixed-interest assets in total cover assets pool	%	95.0	94.0
Share of fixed-interest Pfandbriefe in liabilities to be covered	%	95.0	96.6
Total amount of assets breaching the limits as set out in section 20 (2) no. 2 of the PfandBG	€ mn	–	–

Assets included in cover for Mortgage Pfandbriefe

by loan amount	31 Dec 2018 € mn	1 Jan 2018 € mn
<= € 300,000	8,221	8,066
> € 300,000 and <= € 1 mn	2,285	2,152
> € 1 mn and <= € 10 mn	10,637	10,008
> € 10 mn	10,842	10,109
Total	31,985	30,335

by type of property	31 Dec 2018 € mn	1 Jan 2018 € mn
Housing properties	19,715	19,068
Commercial properties	12,270	11,267
Total	31,985	30,335

Assets included in cover for Mortgage Pfandbriefe, by country where real property collateral is located, and by type of property

€ mn	Year under review	Federal Republic of Germany	Belgium	France	United Kingdom	Netherlands	Austria	Poland	Sweden	Hungary	USA	Total portfolio
RESIDENTIAL PROPERTIES	31 Dec 2018	1,478	–	*) –	–	–	–	–	–	–	–	1,478
	1 Jan 2018	1,153	–	*) –	–	–	–	–	–	–	–	1,153
SINGLE AND DOUBLE FAMILY HOMES	31 Dec 2018	5,961	–	2	–	*) –	*) –	–	–	–	–	5,963
	1 Jan 2018	6,004	*) –	2	–	*) –	*) –	–	–	–	–	6,006
MULTI-FAMILY HOMES	31 Dec 2018	11,800	–	–	–	–	–	–	–	–	–	11,800
	1 Jan 2018	11,515	–	13	–	*) –	–	–	–	–	–	11,528
OFFICE BUILDINGS	31 Dec 2018	4,165	–	119	142	177	3	–	–	–	–	4,606
	1 Jan 2018	4,209	–	108	133	178	3	–	–	–	41	4,672
COMMERCIAL BUILDINGS	31 Dec 2018	3,661	–	85	38	104	–	37	55	44	–	4,024
	1 Jan 2018	3,583	–	77	39	98	–	53	57	45	–	3,952
INDUSTRIAL BUILDINGS	31 Dec 2018	45	–	–	–	–	–	–	–	–	–	45
	1 Jan 2018	59	–	–	–	–	–	–	–	–	–	59
OTHER COMMERCIAL PROPERTIES	31 Dec 2018	3,406	–	–	–	57	–	–	1	–	–	3,464
	1 Jan 2018	2,482	–	–	–	7	8	–	1	–	16	2,514
UNFINISHED NEW BUILDINGS NOT YET YIELDING RETURNS	31 Dec 2018	580	–	–	–	–	–	–	–	–	–	580
	1 Jan 2018	436	–	–	–	–	–	–	–	–	–	436
BUILDING PLOTS	31 Dec 2018	25	–	–	–	–	–	–	–	–	–	25
	1 Jan 2018	15	–	–	–	–	–	–	–	–	–	15
Total	31 Dec 2018	31,121	–	206	180	338	3	37	56	44	–	31,985
	1 Jan 2018	29,456	*) –	200	172	283	11	53	58	45	57	30,335

*) Values < € 0.5 million

Assets included in cover for Mortgage Pfandbriefe
Total amount of registered cover assets

	Assets pursuant to section 19 (1) no. 2 of the PfandBG									
	Equalisation claims pursuant to section 19 (1) no. 1 of the PfandBG		Total		of which: covered debt securities pursuant to art. 129 of the EU Regulation no. 575/2013		Assets pursuant to section 19 (1) no. 3 of the PfandBG		Total	
Sovereign borrowers	31 Dec 2018 € mn	1 Jan 2018 € mn	31 Dec 2018 € mn	1 Jan 2018 € mn	31 Dec 2018 € mn	1 Jan 2018 € mn	31 Dec 2018 € mn	1 Jan 2018 € mn	31 Dec 2018 € mn	1 Jan 2018 € mn
Federal Republic of Germany	–	–	–	650	–	–	1,176	940	1,176	1,590
Total	–	–	–	650	–	–	1,176	940	1,176	1,590

Overview of payments in arrears on cover assets for Mortgage Pfandbriefe

	Aggregate payments in arrears by at least 90 days		Total amount disclosed if applicable arrears equal at least 5% of total asset value	
	31 Dec 2018 € mn	1 Jan 2018 € mn	31 Dec 2018 € mn	1 Jan 2018 € mn
Federal Republic of Germany	1.9	2.1	6.5	4.7
France	–	–	0.1	0.1
Total	1.9	2.1	6.6	4.8

Assets included in cover for Mortgage Pfandbriefe
Forced sales/forced administration

	Commercial properties		Housing properties	
	2018 Number	2017 Number	2018 Number	2017 Number
No. 4a				
Forced sales pending	8	7	108	108
Forced administrations pending	4	3	26	37
of which: included in forced sales pending	4	3	19	32
Forced sales executed	2	4	58	60
No. 4b	Number	Number	Number	Number
Purchases of properties to prevent losses (foreclosed assets)	–	–	–	–
No. 4c	€ mn	€ mn	€ mn	€ mn
Total amount of interest arrears	0.11	0.07	0.40	0.33

Assets included in cover for Public Pfandbriefe
Share in total amount of Pfandbriefe outstanding (nominal)

	31 Dec 2018 € mn	1 Jan 2018 € mn	31 Dec 2018 € mn	1 Jan 2018 € mn
Total cover assets pool	18,414	19,535	121.36	115.55
of which: ordinary cover	18,378	19,518	121.12	115.45
of which: additional cover	36	17	0.24	0.10

Assets included in cover for Public Pfandbriefe

by loan amount	31 Dec 2018 € mn	1 Jan 2018 € mn
<= € 10 mn	6,931	7,267
> € 10 mn and <= € 100 mn	6,144	6,845
> € 100 mn	5,303	5,406
Total	**18,378**	**19,518**

Assets included in cover for Public Pfandbriefe, by country of domicile of the borrower and, in the case of full guarantee, of the guarantor

	Sovereigns		Regional public-sector entities		Local public-sector entities		Other		Total a.)	
a.) of which: due from € mn	2018	2017	2018	2017	2018	2017	2018	2017	2018	2017
Belgium	30	30	23	23	–	–	–	–	**53**	53
Federal Republic of Germany	215	26	1,776	1,891	10,795	11,531	1,010	1,361	**13,796**	14,809
France	40	–	7	7	20	20	21	21	**88**	48
Italy	690	690	200	180	80	118	–	–	**970**	988
Canada	–	–	280	269	5	6	–	–	**285**	275
Luxembourg	7	–	–	–	–	–	–	99	**7**	99
Austria	416	417	25	25	–	–	–	–	**441**	442
Portugal	280	280	–	–	–	–	–	–	**280**	280
Switzerland	–	–	226	218	–	–	–	–	**226**	218
Spain	50	83	980	1,026	137	172	–	–	**1,167**	1,281
EU institutions	–	–	–	–	–	–	288	182	**288**	182
Total	**1,728**	1,526	**3,517**	3,639	**11,037**	11,847	**1,319**	1,663	**17,601**	18,675

	Sovereigns		Regional public-sector entities		Local public-sector entities		Other		Total b.)		Total a.) and b.)	
b) of which: guaranteed by € mn	2018	2017	2018	2017	2018	2017	2018	2017	2018	2017	2018	2017
Belgium	–	–	53	54	–	–	–	–	**53**	54	**106**	107
Federal Republic of Germany	51	51	63	75	226	283	5	6	**345**	415	**14,141**	15,224
France	–	–	–	–	–	–	–	–	**0**	0	**88**	48
Italy	1	1	–	–	–	–	–	–	**1**	1	**971**	989
Canada	–	–	134	129	–	–	–	–	**134**	129	**419**	404
Luxembourg	–	–	–	–	–	–	–	–	**0**	0	**7**	99
Austria	20	20	–	–	–	–	–	–	**20**	20	**461**	462
Portugal	200	200	–	–	–	–	–	–	**200**	200	**480**	480
Switzerland	–	–	–	–	–	–	–	–	**0**	0	**226**	218
Spain	–	–	–	–	24	24	–	–	**24**	24	**1,191**	1,305
EU institutions	–	–	–	–	–	–	–	–	**0**	0	**288**	182
Total	**272**	272	**250**	258	**250**	307	**5**	6	**777**	843 *)	**18,378**	19,518

*) Totals do not include any guarantees due to promotion of export activities.

Assets included in cover for Public Pfandbriefe
Total amount of registered cover assets

	Equalisation claims pursuant to section 20 (2) no. 1 of the PfandBG		Assets pursuant to section 20 (2) no. 2 of the PfandBG: Total		Assets pursuant to section 20 (2) no. 2 of the PfandBG: of which: covered debt securities pursuant to art. 129 of the EU Regulation no. 575/2013		Total	
Sovereign borrowers	31 Dec 2018 € mn	1 Jan 2018 € mn	31 Dec 2018 € mn	1 Jan 2018 € mn	31 Dec 2018 € mn	1 Jan 2018 € mn	31 Dec 2018 € mn	1 Jan 2018 € mn
Federal Republic of Germany	–	–	36	17	–	–	36	17
Total	**–**	–	**36**	17	**–**	–	**36**	17

Overview of payments in arrears on cover assets for Public Pfandbriefe

	Aggregate payments in arrears by at least 90 days		Total amount disclosed if applicable arrears equal at least 5% of total asset value	
	31 Dec 2018 € mn	1 Jan 2018 € mn	31 Dec 2018 € mn	1 Jan 2018 € mn
Total	**–**	–	**–**	–

OTHER INFORMATION ON THE ANNUAL FINANCIAL STATEMENTS

(32) Audit and consulting fees within the meaning of section 285 no. 17 of the HGB

Auditors' fees are recognised in the consolidated financial statements of DZ BANK AG, Deutsche Zentral-Genossenschaftsbank, Frankfurt/Main.

(33) Executive bodies of DZ HYP

Supervisory Board

Uwe Fröhlich
Co-Chief Executive Officer of the Board of Managing Directors of DZ BANK AG Deutsche Zentral-Genossenschafts-bank, Frankfurt am Main
Member since 28/05/2018
– Chairman since 01/08/2018 –

Uwe Berghaus
Member of the Board of Managing Directors of DZ BANK AG Deutsche Zentral-Genossenschaftsbank, Frankfurt/Main
– Chairman until 31/07/2018 –

Dagmar Mines
Bank employee,
DZ HYP AG
– Deputy Chairwoman –

Thomas Müller
Spokesman of the Management Board
Volksbank Dresden-Bautzen eG
– Deputy Chairman –

Brigitte Baur
Deputy Chairwoman of the Management Board,
Volksbank Raiffeisenbank Nürnberg eG

Anja Franke
Bank employee,
DZ HYP AG

Ralph Gruber
Bank employee,
DZ HYP AG

Dr Holger Hatje
Chairman of the Management Board,
Berliner Volksbank eG

Olaf Johnert
Bank employee,
DZ HYP AG

Dr Reinhard Kutscher
Chairman of the Management Board,
Union Investment Real Estate GmbH

Ulrike Marcusson
Bank employee,
DZ HYP AG

Rainer Peters
Chairman of the Management Board,
Volksbank Halle/Westf. eG
since 28/07/2018

Johannes Röring
Chairman of the Management Board,
Stiftung Westfälische Landschaft,
since 28/07/2018

Martin Schmitt
Chairman of the Management Board,
Volksbank Kassel Göttingen eG

Michael Speth
Member of the Board of Managing Directors of DZ BANK AG Deutsche Zentral-Genossenschaftsbank, Frankfurt/Main

Heinrich Stumpf
Member of the Management Board,
Augusta-Bank eG
until 27/07/2018

Werner Thomann
Chairman of the Management Board,
Volksbank Rhein-Wehra eG
until 27/07/2018

Hans-Peter Ulepić
Spokesman of the Management Board,
Gladbacher Bank Aktiengesellschaft von 1922
since 28/07/2018

Thorsten Wenck
Bank employee,
DZ HYP AG

Holger Willuhn
Chairman of the Management Board,
Volksbank Mitte eG
until 27/07/2018

Hans Rudolf Zeisl
Chairman of the Management Board,
Volksbank Stuttgart eG

Management Board

Frank M. Mühlbauer
Chief Executive Officer
until 31/12/2018

Dr Georg Reutter
Chief Executive Officer

Dr Carsten Düerkop

Manfred Salber

(34) Remuneration of the executive bodies

	2018 € 000's	2017 € 000's
Supervisory Board	295	393
Management Board	2,770	2,472
Advisory Council	127	133
Former members of the Management Board or their surviving dependants	2,628	2,631
Provisions for current pensions and pension commitments for former members of the Management Board or their surviving dependants	34,778	33,012

(35) Loans to members of executive bodies

	31 Dec 2018 € 000's	1 Jan 2018 € 000's
Supervisory Board	32	330

(36) Offices held by members of the Management Board or members of staff in supervisory bodies of large limited companies

As at 31 December 2018, neither the members of the Management Board nor members of staff held any offices in supervisory bodies of large limited companies.

(37) Average number of employees

	Male	Female	2018 Total	Male	Female	2017 Total
TOTAL NUMBER OF EMPLOYEES	482	391	873	478	381	859
of which: full-time employees	466	214	680	464	218	682
part-time employees						
number	16	177	193	14	163	177
weighted	(13)	(111)	(124)	(12)	(103)	(115)

(38) Information about the parent company pursuant to section 285 no. 14 of the HGB

DZ BANK AG Deutsche Zentral-Genossenschaftsbank, Frankfurt/Main, prepares consolidated financial statements which incorporate the financial statements of DZ HYP. The consolidated financial statements of DZ BANK are published in the German Federal Gazette (Bundesanzeiger).

Report on material events after 31 December 2018

No events of particular importance materialised during the period from 1 January to 1 March 2019 which would have required a materially different presentation of DZ HYP's net assets, financial position and financial performance, had they occurred earlier.

Hamburg and Münster (Westphalia), 1 March 2019

DZ HYP AG

Dr Georg Reutter
Chief Executive Officer

Dr Carsten Düerkop

Manfred Salber

RESPONSIBILITY STATEMENT

To the best of our knowledge, and in accordance with the applicable reporting principles, the annual financial statements give a true and fair view of the assets, liabilities, financial position and profit or loss of the company, and the management report of the company includes a fair review of the development and performance of the business and the position of the company, together with a description of the principal opportunities and risks associated with the expected development of the company.

Hamburg and Münster (Westphalia), 1 March 2019

DZ HYP AG

Dr Georg Reutter
Chief Executive Officer

Dr Carsten Düerkop

Manfred Salber

INDEPENDENT AUDITOR'S REPORT

Translation of the German independent auditor's report concerning the audit of the annual financial statements prepared in German

To DZ HYP AG

Report on the audit of the annual financial statements and of the management report

Opinions

We have audited the annual financial statements of DZ HYP AG, Hamburg and Münster, which comprise the balance sheet as at 31 December 2018, and the profit and loss account, cash flow statement and statement of changes in equity for the financial year from 1 January to 31 December 2018, and notes to the financial statements, including the recognition and measurement policies presented therein. In addition, we have audited the management report of DZ HYP AG for the financial year from 1 January to 31 December 2018.

In our opinion, on the basis of the knowledge obtained in the audit,

» the accompanying annual financial statements comply, in all material respects, with the requirements of German commercial law applicable to institutions and give a true and fair view of the assets, liabilities and financial position of the Institution as at 31 December 2018 and of its financial performance for the financial year from 1 January to 31 December 2018 in compliance with German legally required accounting principles, and
» the accompanying management report as a whole provides an appropriate view of the Institution's position. In all material respects, this management report is consistent with the annual financial statements, complies with German legal requirements and appropriately presents the opportunities and risks of future development.

Pursuant to Sec. 322 (3) Sentence 1 HGB ["Handelsgesetzbuch": German Commercial Code], we declare that our audit has not led to any reservations relating to the legal compliance of the annual financial statements and of the management report.

Basis for the opinions

We conducted our audit of the annual financial statements and of the management report in accordance with Sec. 317 HGB and the EU Audit Regulation (No 537/2014, referred to subsequently as "EU Audit Regulation") and in compliance with German Generally Accepted Standards for Financial Statement Audits promulgated by the Institut der Wirtschaftsprüfer [Institute of Public Auditors in Germany] (IDW). Our responsibilities under those requirements and principles are further described in the "Auditor's responsibilities for the audit of the annual financial statements and of the management report" section of our auditor's report. We are independent of the Institution in accordance with the requirements of European law and German commercial and professional law, and we have fulfilled our other German professional responsibilities in accordance with these requirements. In addition, in accordance with Art. 10 (2) f) of the EU Audit Regulation, we declare that we have not provided non-audit services prohibited under Art. 5 (1) of the EU Audit Regulation. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinions on the annual financial statements and on the management report.

Key audit matters in the audit of the annual financial statements

Key audit matters are those matters that, in our professional judgment, were of most significance in our audit of the annual financial statements for the financial year from 1 January to 31 December 2018. These matters were addressed in the context of our audit of the annual financial statements as a whole, and in forming our opinion thereon; we do not provide a separate opinion on these matters. Below, we describe what we consider to be the key audit matters:

Valuation of commercial and private real estate finance exposures at risk of default

Reasons why the matter was determined to be a key audit matter

The valuation of exposures at risk of default in the commercial and private real estate finance loan portfolios and the resulting estimation of any necessary impairment losses constitutes a significant area of management judgment.

The identification of non-performing exposures and the calculation of the expected future cash flows is subject to uncertainty and involves various assumptions and factors, particularly in respect of the borrowers' financial position, expectations of future cash flows from the loan agreements and/or the financed properties and from the realization of collateral. Minimal changes in the assumptions can lead to significantly differing valuations and thus to higher impairment losses.

As part of the audit, the identification and valuation of commercial and private real estate finance exposures at risk of default were determined to be a key audit matter due to the relative magnitude of these real estate finance exposures and to the high level of judgment exercised in relation to the underlying assumptions.

Auditor's response

We assessed the design and operating effectiveness of the accounting-related internal control system with regard to the key lending processes. Our focus was on the processes for ongoing loan monitoring for the relevant real estate finance, for identifying impaired loans and for calculating individual impairments.

We also examined whether the specific loan loss provisions recognized in accordance with the Bank's calculation methods were appropriate and strictly applied. The calculation method was assessed in particular on the basis of our knowledge of the industry.

We also performed substantive procedures on a sample basis, assessing specific risk provisions in terms of necessity and adequacy in a test of details.

We selected the sample with a view to risk, applying in particular criteria such as amount of loan exposure and unsecured portion, listing on watchlists for potential and acute risks of default, and rating category.

We methodically assessed the significant assumptions concerning the estimated future cash flows from the loan agreements and financed properties and the realization of collateral applied during the impairment process. In doing so, we focused on assessing the borrowers' debt servicing ability as well as the expected cash flows from the realization of real estate collateral.
In order to assess borrowers' debt servicing capability, we validated, depending on the type of financing, the

documents provided by the Bank pertaining to the borrowers' financial situation, tenant lists, property data and financial plans and, if available, compared them with market data.

In order to assess the valuation of the real estate collateral, we used expert appraisals commissioned by the Institution. Applying our industry knowledge, we assessed the experts' work in particular with regard to whether their valuation was independent and appropriate.

We also performed analytical audit procedures specifically for the assessment of private real estate finance exposures at risk of default. These largely focused on changes in credit ratings and collateral values as well as on anomalies at the individual borrower level (e.g. implausible credit ratings in the face of non-performance).

Our procedures did not give rise to any reservations regarding the valuation of commercial and private real estate finance exposures at risk of default.

Reference to related disclosures

The Institution's disclosures about the valuation of commercial and private real estate finance exposures at risk of default are provided in the notes to the financial statements in note "(2) Accounting policies." Please see the "Net assets, financial position, and financial performance" and "Risk report section II c)" sections of the management report for further information about these exposures and about risk provisioning in the reporting year.

Other information

The other information comprises the sections of the annual report entitled "Letter from the Management Board," "Report of the Supervisory Board," "DZ HYP," "Responsibility Statement," and "Service," which were available as drafts on or before the date of this auditor's report. The Supervisory Board is responsible for the Report of the Supervisory Board. In all other respects, the executive directors are responsible for the other information.

Our opinions on the annual financial statements and on the management report do not cover the other information, and consequently we do not express an opinion or any other form of assurance conclusion thereon.

In connection with our audit, our responsibility is to read the other information and, in so doing, to consider whether the other information
- » is materially inconsistent with the annual financial statements, with the management report or our knowledge obtained in the audit, or
- » otherwise appears to be materially misstated.

If, based on the work we have performed, we conclude that there is a material misstatement of this other information, we are required to report that fact. We have nothing to report in this regard.

Responsibilities of the executive directors and the Supervisory Board for the annual financial statements and the management report

The executive directors are responsible for the preparation of the annual financial statements that comply, in all material respects, with the requirements of German commercial law applicable to institutions, and that the annual financial statements give a true and fair view of the assets, liabilities, financial position and financial performance of the Institution in compliance with German legally required accounting principles. In addition, the executive directors are responsible for such internal control as they, in accordance with German legally required accounting principles, have determined necessary to enable the preparation of annual financial statements that are free from material misstatement, whether due to fraud or error.

In preparing the annual financial statements, the executive directors are responsible for assessing the Institution's ability to continue as a going concern. They also have the responsibility for disclosing, as applicable, matters related to going concern. In addition, they are responsible for financial reporting based on the going concern basis of accounting, provided no actual or legal circumstances conflict therewith.

Furthermore, the executive directors are responsible for the preparation of the management report that, as a whole, provides an appropriate view of the Institution's position and is, in all material respects, consistent with the annual financial statements, complies with German legal requirements and appropriately presents the opportunities and risks of future development. In addition, the executive directors are responsible for such arrangements and measures (systems) as they have considered necessary to enable the preparation of a management report that is in accordance with the applicable German legal requirements, and to be able to provide sufficient appropriate evidence for the assertions in the management report.

The Supervisory Board is responsible for overseeing the Institution's financial reporting process for the preparation of the annual financial statements and of the management report.

Auditor's responsibilities for the audit of the annual financial statements and of the management report

Our objectives are to obtain reasonable assurance about whether the annual financial statements as a whole are free from material misstatement, whether due to fraud or error, and whether the management report as a whole provides an appropriate view of the Institution's position and, in all material respects, is consistent with the annual financial statements and the knowledge obtained in the audit, complies with the German legal requirements and appropriately presents the opportunities and risks of future development, as well as to issue an auditor's report that includes our opinions on the annual financial statements and on the management report.

Reasonable assurance is a high level of assurance, but is not a guarantee that an audit conducted in accordance with Sec. 317 HGB and the EU Audit Regulation and in compliance with German Generally Accepted Standards for Financial Statement Audits promulgated by the Institut der Wirtschaftsprüfer (IDW) will always detect a material misstatement. Misstatements can arise from fraud or error and are considered material if, individually or in the aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of these annual financial statements and this management report.

We exercise professional judgment and maintain professional skepticism throughout the audit. We also:

- » Identify and assess the risks of material misstatement of the annual financial statements and of the management report, whether due to fraud or error, design and perform audit procedures responsive to those risks, and obtain audit evidence that is sufficient and appropriate to provide a basis for our opinions. The risk of not detecting a material misstatement resulting from fraud is higher than for one resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal control.
- » Obtain an understanding of internal control relevant to the audit of the annual financial statements and of arrangements and measures (systems) relevant to the audit of the management report in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of these systems of the Institution.
- » Evaluate the appropriateness of accounting policies used by the executive directors and the reasonableness of estimates made by the executive directors and related disclosures.

» Conclude on the appropriateness of the executive directors' use of the going concern basis of accounting and, based on the audit evidence obtained, whether a material uncertainty exists related to events or conditions that may cast significant doubt on the Institution's ability to continue as a going concern. If we conclude that a material uncertainty exists, we are required to draw attention in the auditor's report to the related disclosures in the annual financial statements and in the management report or, if such disclosures are inadequate, to modify our respective opinions. Our conclusions are based on the audit evidence obtained up to the date of our auditor's report. However, future events or conditions may cause the Institution to cease to be able to continue as a going concern.
» Evaluate the overall presentation, structure and content of the annual financial statements, including the disclosures, and whether the annual financial statements present the underlying transactions and events in a manner that the annual financial statements give a true and fair view of the assets, liabilities, financial position and financial performance of the Institution in compliance with German legally required accounting principles.
» Evaluate the consistency of the management report with the annual financial statements, its conformity with [German] law, and the view of the Institution's position it provides.
» Perform audit procedures on the prospective information presented by the executive directors in the management report. On the basis of sufficient appropriate audit evidence we evaluate, in particular, the significant assumptions used by the executive directors as a basis for the prospective information, and evaluate the proper derivation of the prospective information from these assumptions. We do not express a separate opinion on the prospective information and on the assumptions used as a basis. There is a substantial unavoidable risk that future events will differ materially from the prospective information.

We communicate with those charged with governance regarding, among other matters, the planned scope and timing of the audit and significant audit findings, including any significant deficiencies in internal control that we identify during our audit.

We also provide those charged with governance with a statement that we have complied with the relevant independence requirements, and communicate with them all relationships and other matters that may reasonably be thought to bear on our independence and, where applicable, the related safeguards.

From the matters communicated with those charged with governance, we determine those matters that were of most significance in the audit of the annual financial statements of the current period and are therefore the key audit matters. We describe these matters in our auditor's report unless law or regulation precludes public disclosure about the matter.

Other legal and regulatory requirements

Further information pursuant to Art. 10 of the EU Audit Regulation

We were elected as auditor by the Annual General Meeting on 9 March 2018. We were engaged by the Audit Committee on 5 July 2018. We have been the auditor of DZ HYP AG without interruption since financial year 2002.

We declare that the opinions expressed in this auditor's report are consistent with the additional report to the Audit Committee pursuant to Art. 11 of the EU Audit Regulation (long-form audit report).
In addition to the financial statement audit, we have provided to the Institution and an entity controlled by it the following services that are not disclosed in the annual financial statements or in the management report:

» Agreed-upon procedures in accordance with International Standard on Related Services 4400
» Assurance engagements in accordance with International Standard on Assurance Engagements 3000
» Procedures in accordance with the instructions of the group auditor of DZ BANK with regard to the IFRS reporting packages prepared by DZ HYP as of 1 January 2018, 30 June 2018 and 31 December 2018
» Issuance of a comfort letter in accordance with IDW AuS 910
» Review of the half-year financial report in accordance with IDW AuS 900
» Voluntary audit of the annual financial statements of a controlled entity

German Public Auditor responsible for the engagement
The German Public Auditor responsible for the engagement is Mr Christian Mai.

Hamburg, 1 March 2019

Ernst & Young GmbH
Wirtschaftsprüfungsgesellschaft

Mai	Meyer
Wirtschaftsprüfer	Wirtschaftsprüfer
[German Public Auditor]	[German Public Auditor]

SERVICE

CORPORATE BODIES AND COMMITTEES, EXECUTIVES

Supervisory Board

Uwe Fröhlich
Co-Chief Executive Officer of the Board of Managing Directors, DZ BANK AG Deutsche Zentral-Genossenschaftsbank, Frankfurt am Main
– Chairman –

Dagmar Mines
DZ HYP AG, Hamburg
– Deputy Chairwoman –

Thomas Müller
Spokesman of the Management Board Volksbank Dresden-Bautzen eG, Dresden
– Deputy Chairman –

Brigitte Baur
Deputy Chairwoman of the Management Board, Volksbank Raiffeisenbank Nürnberg eG, Nuremberg

Uwe Berghaus
Member of the Board of Managing Directors, DZ BANK AG Deutsche Zentral-Genossenschaftsbank, Frankfurt am Main

Anja Franke
DZ HYP AG, Hamburg

Ralph Gruber
DZ HYP AG, Hamburg

Dr Holger Hatje
Bank director (retired), Berlin

Olaf Johnert
DZ HYP AG, Hamburg

Dr Reinhard Kutscher
Chairman of the Management Board, Union Investment Real Estate GmbH, Hamburg

Ulrike Marcusson
DZ HYP AG, Hamburg

Rainer Peters
Chairman of the Management Board, Volksbank Halle/Westf. eG, Halle (Westphalia)

Johannes Röring
Chairman of the Management Board, Stiftung Westfälische Landschaft, Vreden

Martin Schmitt
Chairman of the Management Board, Volksbank Kassel Göttingen eG, Kassel

Michael Speth
Member of the Board of Managing Directors, DZ BANK AG Deutsche Zentral-Genossenschaftsbank, Frankfurt am Main

Hans-Peter Ulepić
Spokesman of the Management Board, Gladbacher Bank Aktiengesellschaft von 1922, Mönchengladbach

Thorsten Wenck
DZ HYP AG, Hamburg

Hans Rudolf Zeisl
Chairman of the Management Board, Volksbank Stuttgart eG, Stuttgart

Updated: 31 March 2019

Advisory Board – Banks

Stefan Baumann
Member of the Management Board, Heidelberger Volksbank eG, Heidelberg

Ralf Baumbusch
Member of the Management Board, VR-Bank Ostalb eG, Aalen

Jürgen Dünkel
Member of the Management Board, VR-Bank Bayreuth-Hof eG, Bayreuth

Klaus Hatzel
Member of the Management Board, Volksbank Raiffeisenbank Rosenheim-Chiemsee eG, Rosenheim

Karl-Heinz Hempel
Member of the Management Board, Volksbank Raiffeisenbank Dachau eG, Dachau

Michael Hietkamp
Member of the Management Board, Volksbank Raiffeisenbank eG, Greifswald

Wolfgang Hillemeier
Chairman of the Management Board, Volksbank Rietberg eG, Rietberg

Wolfgang Hirmer
Spokesman of the Management Board, VR-Bank Langenau-Ulmer Alb eG, Langenau

Johannes Hofmann
Member of the Management Board, VR-Bank Erlangen-Höchstadt-Herzogenaurach eG, Erlangen

Thomas Jakoby
Member of the Management Board, Volksbank Münster eG, Münster

Rainer Jenniches
Chairman of the Management Board, VR-Bank Bonn eG, Bonn

Herbert Kohlberg
Member of the Management Board, Mainzer Volksbank eG, Mainz

Christoph Kothe
Member of the Management Board, Leipziger Volksbank eG, Leipzig

Armin Kühn
Member of the Management Board, VR Bank Enz plus eG, Remchingen

Thomas Ludwig
Member of the Management Board, Volksbank Raiffeisenbank Nordoberpfalz eG, Weiden

Florian Mann
Chairman of the Management Board, Raiffeisenbank Regensburg-Wenzenbach eG, Regensburg

Rainer Mellis
Spokesman of the Management Board, Volksbank Düsseldorf Neuss eG, Dusseldorf

Klaus Merz
Chairman of the Management Board, Volksbank Rhein-Lahn-Limburg eG, Diez

Walter Müller
Member of the Management Board, Volksbank Koblenz Mittelrhein eG, Koblenz

Thorsten Rathje
Member of the Management Board, Hamburger Volksbank eG, Hamburg

Manfred Resch
Member of the Management Board, Frankfurter Volksbank eG, Frankfurt/Main

Updated: 31 March 2019

Cornelia Rosenau
Member of the Management Board, Winterlinger Bank eG, Winterlingen

Ralf Schierenböken
Member of the Management Board, Volksbank eG Braunschweig Wolfsburg, Wolfsburg

Bernd Schmidt
Member of the Management Board, Kieler Volksbank eG, Kiel

Norbert Schmitz
Spokesman of the Management Board, VR-Bank Fläming eG, Luckenwalde

Volker Spietenborg
Member of the Management Board Volksbank Freiburg eG, Freiburg

Ulrich Tolksdorf
Chairman of the Management Board, vr bank Untertaunus eG, Idstein

Kai Wunderlich
Member of the Management Board, Volksbank Wittgenstein eG, Bad Berleburg

Advisory Board – Public Sector

Konrad Beugel
Finance and Economics Officer of the City of Erlangen, Erlangen

Dr Birgit Frischmuth
Senior Policy Advisor, Association of German Cities – Finance Department, Berlin

Dr Stefan Funke
Treasurer/Director of the District of Warendorf, Warendorf

Claus Hamacher
Councillor for Finance and Municipal Economy, Association of Cities and Municipalities in North-Rhine Westphalia, Dusseldorf

Markus Kreuz
Treasurer of the City of Hamm, Hamm

Dr Georg Lunemann
First Councillor and Treasurer, Landschaftsverband Westphalia-Lippe, Münster

Andreas Merkel
Treasurer of the City of Gaggenau, Gaggenau

Silke Meyn
First Councillor of the City of Oldenburg, Oldenburg

Dr Frank Nagel
Head of the Credit Department, Ministry of Finance of the State of Rhineland-Palatinate, Mainz

Alfons Reinkemeier
Treasurer of the City of Münster, Münster

Christian Schuchardt
Lord Mayor of the City of Würzburg, Würzburg

Updated: 31 March 2019

Advisory Board – Housing Sector

Karla Arndt
Member of the Management Board of Baugenossenschaft IDEAL eG, Berlin-Neukölln

Uwe Flotho
Member of the Management Board of Vereinigte Wohnstätten 1889 eG, Kassel

Franz-Bernd Große-Wilde
Chairman of the Management Board of Spar- und Bauverein eG, Dortmund

Peter Kay
Member of the Management Board of BGFG – Baugenossenschaft freier Gewerkschafter eG, Hamburg

Steffan Liebscher
Member of the Management Board of GEWOBA Nord Baugenossenschaft eG, Schleswig

Matthias Lüdecke
Chairman of the Management Board of Wohnungsverein Hagen eG, Hagen

Andreas Otto
Chairman of the Management Board of GWG Gifhorner Wohnungsbau-Genossenschaft eG, Gifhorn

Dr Wolfgang Pfeuffer
Spokesman of the Management Board of JOSEPH-STIFTUNG Kirchliches Wohnungsunternehmen, Bamberg

Peter Stammer
Executive Board member of Baugenossenschaft Familienheim, Heidelberg

Sybille Wegerich
Member of the Management Board of bauverein AG, Darmstadt

Jörn-M. Westphal
Managing Director of ProPotsdam GmbH, Potsdam

Management Board and distribution of responsibilities

Dr Georg Reutter
Chief Executive Officer

- Commercial Real Estate Investors Corporates & Cooperative Banks
- Commercial Real Estate Investors Institutional & International Customers
- Treasury
- Housing Sector & Private Investors
- Public Sector
- Retail Customers & Relationship Manager Cooperative Banks
- Communications, Marketing & Investor Relations
- Management Board Office & Committees

Dr Carsten Düerkop

- Finance
- Compliance
- Organisation & Operations
- IT
- Internal Audit
- Property Valuation
- Human Resources

Manfred Salber

- Back Office Commercial Real Estate Investors
- Back Office Housing Sector, Private Investors & Retail Customers
- Restructuring & Recovery
- Back Office Treasury & Public Sector
- Risk Controlling
- Legal

Updated: 31 March 2019

Senior General Managers

Jörg Hermes

Artur Merz

Markus Wirsen

Department Heads

Heike Bausch
Human Resources

Gerhard Decker
Property Valuation

Patrick Ernst
Treasury

Norbert Grahl
Back Office Commercial Real Estate Investors

Steffen Günther
Commercial Real Estate Investors Institutional & International Customers

Jörg Hermes
Finance

Axel Jordan
Commercial Real Estate Investors Corporates & Cooperative Banks

Markus Krampe
Public Sector

Artur Merz
Risk Controlling

Thomas Mirow
Restructuring & Recovery

Thomas Plum
Retail Customers & Relationship Manager Cooperative Banks

Peter Ringbeck
IT

Peter Ringbeck
Organisation & Operations

Frank Schneider
Compliance

Siegfried Schneider
Back Office Treasury & Public Sector

Jürg Schönherr
Housing Sector & Private Investors

Helge Trunk
Management Board Office & Committees

Peter Vögelein
Internal Audit

Carsten Hendrik Vollnberg
Legal

Markus Wirsen
Back Office Housing Sector, Private Investors & Retail Customers

Trustees

Dr Michael Labe
Judge at the Hamburg Higher Regional Court (Hanseatisches Oberlandesgericht Hamburg), Hamburg

Michael Führer
Deputy Trustee, Public Auditor and Tax Adviser, Münster

Björn Reher
Deputy Trustee, Public Auditor, Hamburg

Updated: 31 March 2019

DZ HYP ADDRESSES

Hamburg Head Office
Rosenstrasse 2
20095 Hamburg, Germany
Postfach 10 14 46
20009 Hamburg, Germany
Telephone: +49 40 3334-0

Münster Head Office
Sentmaringer Weg 1
48151 Münster, Germany
Mailing address:
48136 Münster, Germany
Telephone: +49 251 4905-0

Regional Centres

Berlin Regional Centre
Pariser Platz 3
10117 Berlin
Telephone: +49 30 31993-5101
(Commercial Real Estate Investors)
Telephone: +49 30 31993-5080
(Housing Sector)
Telephone: +49 30 31993-5086
(Retail Customers/Private Investors)

Dusseldorf Regional Centre
Ludwig-Erhard-Allee 20
40227 Dusseldorf, Germany
Telephone: +49 211 220499-30
(Commercial Real Estate Investors)
Telephone: +49 251 4905-3830
(Housing Sector)
Telephone: +49 211 220499-5832
(Retail Customers/Private Investors)

Frankfurt Regional Centre
CITY-HAUS I, Platz der Republik 6
60325 Frankfurt/Main, Germany
Telephone: +49 69 750676-21
(Commercial Real Estate Investors)
Telephone: +49 211 220499-5833
(Housing Sector)
Telephone: +49 69 750676-12
(Retail Customers/Private Investors)

Hamburg Regional Centre
Rosenstrasse 2
20095 Hamburg, Germany
Telephone: +49 40 3334-3778
(Commercial Real Estate Investors)
Telephone: +49 40 3334-4704
(Housing Sector)
Telephone: +49 40 3334-4706
(Retail Customers/Private Investors)

Munich Regional Centre
Türkenstrasse 16
80333 Munich, Germany
Telephone: +49 89 512676-10
(Commercial Real Estate Investors)
Telephone: +49 89 512676-42
(Housing Sector)
Telephone: +49 89 512676-41
(Retail Customers/Private Investors)

Stuttgart Regional Centre
Heilbronner Strasse 41
70191 Stuttgart, Germany
Telephone: +49 711 120938-0
(Commercial Real Estate Investors)
Telephone: +49 89 512676-42
(Housing Sector)
Telephone: +49 711 120938-38
(Retail Customers/Private Investors)

Regional Offices

Hanover Regional Office
Berliner Allee 5
30175 Hanover, Germany
Telephone +49 511 86643808

Heidelberg Regional Office
Konrad-Adenauer-Strasse 87
69207 Sandhausen
Telephone +49 6224 145151

Kassel Regional Office
Rudolf-Schwander-Str. 1
34117 Kassel, Germany
Telephone: +49 561 602935-23

Leipzig Regional Office
Schillerstrasse 3
04109 Leipzig, Germany
Telephone: +49 341 962822-92

Mannheim Regional Office
Augustaanlage 61
68165 Mannheim, Germany
Telephone: +49 621 782727-20

Münster Regional Office
Sentmaringer Weg 1
48151 Münster, Germany
Telephone: +49 251 4905-7314

Nuremberg Regional Office
Am Tullnaupark 4
90402 Nuremberg, Germany
Telephone +49 911 94009816

Schwäbisch Gmünd Regional Office
Maiglöckchenweg 12
73527 Schwäbisch Gmünd
Telephone +49 7171 8077230

Institutional Clients

Rosenstrasse 2
20095 Hamburg, Germany
Telephone: +49 40 3334-2159

DZ HYP AG

Rosenstraße 2
20095 Hamburg
Tel.: +49 40 3334-0

Sentmaringer Weg 1
48151 Münster
Tel.: +49 251 4905-0

dzhyp.de