

## **Aareal Bank's bad luck of being a property bank**

*Börsen-Zeitung*, 14 Nov 2008/page 17

By Carsten Steevens, *Börsen-Zeitung*, 14 Nov 2008

Aareal Bank has not reported losses in any quarter since the onset of the financial markets crisis in mid-2007. The Wiesbaden-based property finance house, which was created in June 2002 following the split of former DePfa Group and has been included in the MDAX index of second-line issues for six years now, relies on a well-balanced business model incorporating the two segments Structured Property Financing and Consulting/Services. "We generate steady profits, in spite of the financial markets crisis, and our results are within projections. Can you name any other bank who is able to say that?", asks Wolf Schumacher, Aareal Bank's Chairman of the Management Board (cf. *Börsen-Zeitung* of 12 November). Yet the share price has lost more than three quarters in the course of this year alone, with Aareal Bank's market capitalisation plunging from EUR 1.3 billion to just EUR 260 million.

### Collective liability

Quite apparently, the bank finds itself in the unlucky position of being a property specialist during a financial crisis of epic proportions. The origins of this crisis – which has worsened sharply since mid-September – can be traced to the troubles in the US property market, triggered by defaults of borrowers with weak credit standing. Aareal Bank is under 'collective liability', having to face widespread suspicion that any property bank is bound to fall victim to the crisis. Of course, cases such as Hypo Real Estate, Aareal Bank's German competitor which had to be rescued, do not improve perceptions. According to Schumacher, Aareal Bank's share price is burdened by other issues which are outside the bank's influence.

Yet despite its resilience during times of crisis, and the performance of its financial indicators over the past quarters, Aareal Bank has not managed to convince investors. Schumacher complains that comments seen to date have not sufficiently appreciated the soundness and robustness Aareal Bank's business model. Presenting the bank's nine-month results last Tuesday, Schumacher reiterated that the bank's operating business performs within budget, its capitalisation is adequate, and its funding is sound.

The financial markets crisis – including the collapse of Lehman Brothers, the fourth largest US investment bank, and the forced nationalisation of Icelandic banks – has hardly had any direct impact on Aareal Bank: the property specialist quantified the direct burden on income as a result of the financial markets crisis during the third quarter at EUR 10 million. As the interim report as at 30 September points out, this is an achievement of the bank's "cautious risk policy".

### No State support sought right now

At present, Aareal Bank sees no need to apply for support from Germany's recently-established Financial Markets Stabilisation Fund ("SoFFin"). Nevertheless, should the bank perceive competitive disadvantages, as a result of its domestic and international competitors who received government support benefiting from better ratings and cheaper funding, allowing them to generate more new business, the bank might seek capitalisation support from the German Federal Government after all. In contrast to some of its German competitors, as CEO Schumacher puts it, Aareal Bank does not face distress, which would force it to seek government aid under the EUR 480 billion financial sector rescue package.

## Own crisis resolved

It was only at the end of March 2007 – three months before the outbreak of the financial markets crisis – that Aareal Bank declared its strategic realignment as completed, which it had embarked upon in response to its own crisis, involving billions of bad debt and losses for two years in a row, launching a growth programme at the time. This spring, however, the bank had to postpone its target of Group return on equity after taxes of 13%, from 2009 to 2010. Given the deterioration of the financial markets crisis over recent weeks, in conjunction with economic slowdown in Aareal Bank's key business regions of Europe, North America, and Asia/Pacific, even this delayed target looks questionable. Analysts expect allowance for credit losses to start rising again in the next year at the latest.

## Dividend cut?

This week Aareal Bank withdrew its target of matching the previous year's operating profit of EUR 159 million in 2008. As a result, the property bank's shareholders – Bayerische Beamten-Lebensversicherung, Swiss Life, plus four other financial institutions have pooled their interests in Aareal Holding Verwaltungsgesellschaft, holding a 37.2% stake – might have to contend themselves with a lower dividend distribution. In any case, a dividend payment does look likely. As Schumacher explained last Tuesday, the bank would find it "very hard to imagine" having to post a loss for the full year 2008. Aareal Bank paid a dividend of 50 cents per share for the 2006 and 2007 financial years, having distributed no dividends for the three preceding years.

According to a research note by UniCredit, the cancellation of the forecast for 2008 did not come as a big surprise, given the financial markets crisis. The Italian bank thus maintained its optimistic view for the Aareal Bank share price: UniCredit's analysts reiterated their 'buy' recommendation, pointing out that the property bank steers a steady course in the prevailing environment. Looking at analyst coverage recorded by Bloomberg, the majority are positive, with 16 'buy' votes against one 'hold' and four 'sell' recommendations. Share price targets updated in November range between EUR 10 (Deutsche Bank) and EUR 20 (Keefe, Bruyette), with Bloomberg indicating the 12-month consensus forecast at EUR 14.66. On Thursday, the Aareal Bank share price was up 1.8%, at EUR 6.06, against a slightly falling MDAX index.