



from left:

Thomas Ortmanns

Member of the Management Board

Dagmar Knopek

Member of the Management Board

Marc Hess

Member of the Management Board

Hermann J. Merkens

Chairman of the Management Board

Christiane Kunisch-Wolff

Member of the Management Board

Christof Winkelmann

Member of the Management Board

Letter from the Management Board

*Dear shareholders,
Business associates and staff members,*

The 2019 financial year was another challenging year – not only for the banking sector as a whole, but also for Aareal Bank. The past year was once again marked by persistently low interest rates alongside considerable political and economic uncertainty. As in previous years, we focused on implementing new regulatory requirements, and prepared early for further foreseeable regulatory changes. Thus, Aareal Bank has confronted these challenges and can look back at another successful financial year in which we not only generated good results, but also set the strategic course for the future.

The financial indicators clearly confirm: commercially, the 2019 financial year was yet another in an impressively long series of successful years for our enterprise. We achieved all our targets in the past financial year, whilst further improving the foundations for a continuation of our positive performance over the past years. Therefore, we are proud of what the entire Aareal Bank Group team achieved and managed in the financial year under review.

Aareal Bank Group's operating profit of € 248 million in 2019 was down only slightly on the adjusted figure for the previous year (€ 261 million), in spite of integration costs incurred for Düsseldorfer Hypothekbank (DHB), in what continued to be a very challenging market and competitive environment (including the positive non-recurring effect of € 55 million from the acquisition of DHB, the previous year's figure was € 316 million). Operating profit was thus within the projected target range, despite expenses of approximately € 50 million being incurred for the accelerated reduction of risk exposures. The other operating indicators were also in line with the forecasts: net interest income, which was stable despite the persistently low level of interest rates, remained within the projected range. This was also the case for loss allowance – higher than in the previous year as a result of accelerated de-risking in the second half of 2019 – as well as for the further marked improvement in net commission income and moderately higher administrative expenses.

Aareal Bank not only developed its operating business further in line with projections during the past year. It also continued to target an improved starting position for the years ahead. As such, we delivered accelerated de-risking – announced at mid-year 2019 – i.e. the accelerated reduction of risk exposures on the credit side and in the securities portfolios, at reasonable expense. Our risk exposure to Italy was thus reduced by one-third, and total NPL volume was even down by around 40 per cent from its mid-year high. Moreover, the de-risking exercise had a positive impact on our capitalisation, as well as improving average loan-to-value ratios in our credit portfolio. We have thus significantly strengthened the structure of the assets side of our balance sheet. Considering all these positive effects, the accelerated de-risking carried out so far has – in our opinion – been a major success.

Aareal Bank countered the decline in the portfolio related to de-risking through continued dynamic new business origination, totalling € 7.7 billion for the year as a whole. Hence, the portfolio volume of € 26.7 billion as at year-end remained within the target corridor of € 26 billion to € 28 billion. We surpassed our margin target, which underlines our ability to allocate new business flexibly to attractive markets, whilst adhering to unchanged high quality standards at the same time.

We also recorded a successful year outside the banking business, with our software subsidiary Aareon remaining on a growth trajectory during the year under review: for 2019, Aareon once again reported a marked increase in sales revenue compared to the previous year, exceeding the € 250 million threshold for the first time. Sales revenues from digital products continued their especially dynamic development, soaring by 20 per cent. Despite announced growth investments at Aareon having been launched in the second half of the year, the subsidiary's earnings contribution also continued to rise.

With solid business in the Structured Property Financing segment and dynamic growth at Aareon, Aareal Bank Group's fundamental operating business trends are still intact, giving us a good starting position to master the challenges lying ahead, and adding to the crucial strategic decisions taken in the past months for the period following the end of the current "Aareal 2020" programme for the future. In the years ahead, the Group will develop the individual business activities in a targeted manner under the motto of "Aareal Next Level" – with an unchanged general strategic orientation – and strengthen their independent profiles, aiming to accelerate the Group's overall growth whilst creating value for the shareholders and other stakeholders in a market, competitive and regulatory environment holding ever-growing challenges.

Whilst the emphasis in property financing is on securing the market position in an adverse environment, the Group is targeting the development of new potential in both the Bank's business with the housing sector and related industries, and at Aareon. Aareon, in particular, is expected to significantly increase its growth momentum, developing a strong independent value proposition as a software company with a standalone market position. For this purpose, Aareon will consistently implement its growth programme, presented in 2019, which is designed to double results over the medium term – predominantly through an expansion of digital businesses. Targeted M&A activities are expected to generate additional growth.

To strengthen the independent profiles of the individual business activities and to enhance external perception of their respective economic success, we will change our segment reporting as of the first quarter of 2020, shifting to three instead of the present two segments: Structured Property Financing, banking business with the housing sector and related industries, and Aareon.

The new segment reporting will externally reflect our refined strategy, with which we will raise our Company to a new development level over the medium term. Within the Bank, numerous Group-wide measures and initiatives will be carried out in the next months – all of which are based on "Aareal Next Level". Assuming a more positive environment compared to the current situation, the measures and initiatives undertaken will permit return on equity before taxes of around 12 per cent over the medium term.

Aareal Bank Group believes the market and competitive environment will remain challenging in the current year. It also expects ongoing political and economic uncertainty. No relief is to be expected either from regulatory pressures or from the low interest rate environment. On the whole we expect operating profit in 2020 to be in line with the previous year's level, along with stable consolidated net income. From today's perspective, we should even be able to achieve the latter when economically viable opportunities arise for a continued selective, accelerated de-risking.

As a result of the spread of the coronavirus and the efforts to combat it, considerable volatility and serious implications can currently be observed on the capital markets, but also in the overall economic environment. At present, it is impossible to assess if and to what extent these may influence the business and earnings development, hence they are not included in our forecasts.

Despite all of this, we are confident that we will once again manage to successfully steer your Company through a challenging environment in 2020 and beyond, consistently creating value for all stakeholders based on a solid operating business and a convincing strategy.

We thank you for the trust you have placed in the path we have pursued to date. The Management Board of Aareal Bank Group, its executives and staff, will devote all their energy to uphold this trust. I hope you will stay with us in the future too!

Yours sincerely, 

Hermann J. Merkens
Chairman of the Management Board