"OUR ACTIONS WITH OUR MEMBERS, CUSTOMERS, EMPLOYEES AND SOCIETY ARE GUIDED BY OUR COMMITMENT TO ACTING RESPONSIBLY."

In a video interview, Dr. Louis Hagen, Chairman of the Münchener Hypothekenbank´s Board of Management, talks about the special importance of acting responsibly, and cooperative values. In addition, he gives some insight into the results of the 2017 business year, as well as the plans for the current year and challenges posed by digitalisation.

Click here to access the video.

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MANAGEMENT REPORT 2017
ECONOMIC REPORT

OVERALL ECONOMIC CONDITIONS

ECONOMIC DEVELOPMENT

The upturn in the global economy accelerated in 2017 as the global gross domestic product increased by 3.7 percent, which was higher than the International Monetary Fund (IMF) anticipated at the start of 2017. The gain showed that the economy was largely unaffected by the numerous political uncertainties that marked global events during the year under review. This applied, in particular, to global trade, which expanded substantially.

During the course of the year economic development within the euro area became increasingly dynamic resulting in a 2.4 percent increase in gross domestic product. The upswing was mainly driven by rising exports as global trade picked up and domestic demand remained strong.

The German economy also flourished as its gross domestic product increased by 2.2 percent in 2017, which was a stronger gain than in the previous year. The strongest drivers were private consumption followed by public-sector investments, and capital expenditures. In addition, the export sector grew notably to make a favourable contribution to the economy. Investments in construction also developed favourably and increased by 2.6 percent. The greatest gain of 3.1 percent was noted by investments in residential housing. Investments in construction within the public sector rose by 2.7 percent while investments in construction of commercial property increased by 1.4 percent.

The annual average rate of inflation rose to 1.8 percent, the highest rate noted since four years. Energy prices grew by 3.1 percent and were the primary reason behind the increase. Furthermore, food prices were notably more expensive than they had been in the previous year.

Development seen in the labour market also reflected the favourable economy as the annual average number of employed persons rose by over 600,000 to 44.3 million. The unemployment figure fell further as the average number of unemployed persons reported was 2.5 million, or more than 150,000 less than in 2016. The unemployment rate fell by 0.4 percentage points to 5.7 percent.

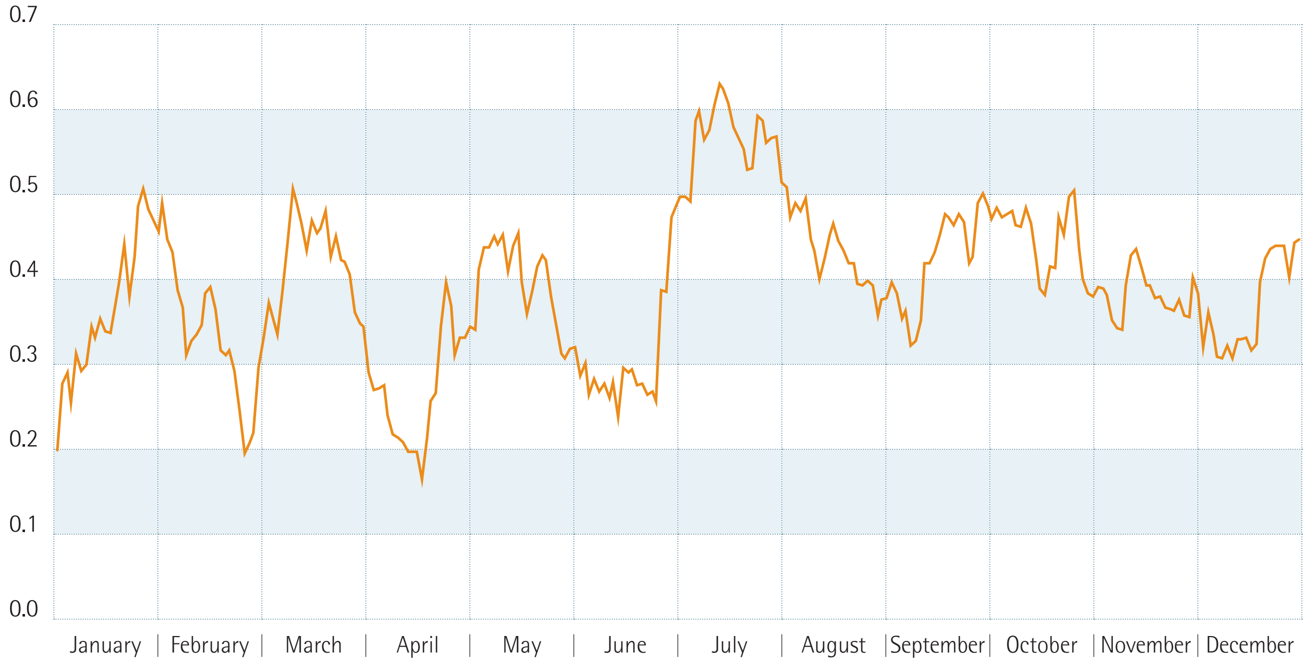
FINANCIAL MARKETS

Financial markets were supported by the unexpectedly favourable economic developments, as well as the central banks' unchanged generous provision of liquidity, and a better mood among market participants than in previous years.

During the course of the year the European Central Bank (ECB) nevertheless retained its expansive monetary policy and left its deposit facility rate for banks unchanged at minus 0.40 percent, while its interest rate on the main refinancing operations (MRO) held steady at 0 percent. Within the framework of its asset purchase programme the net amount of monthly purchases over the course of the year amounted to 60 billion euros per month. Additional important central banks, like the Bank of Japan, the Bank of England and the Swiss National Bank, also provided expansive liquidity in support of the economic recovery process. The policy followed by the American central bank, the Federal Reserve (Fed), diverged from the other central banks as the Fed further tightened its monetary policy during the year under review and raised its key interest three times by 25 basis points each time in light of the favourable development of the American economy. At the end of 2017 the Fed's decisions led to a federal funds rate corridor of 1.25 percent to 1.5 percent. Concurrently, the Fed began to reduce its balance sheet that had expanded due to its bond purchases.

The ECB's policy led to further declines in spreads versus swaps and a slight increase in yields in the bond market. Over the course of the year the yield on 10-year Bunds rose moderately from 0.20 percent to 0.42 percent and was primarily driven by adjusted expectations in light of the economic upswing in the euro area. Yields on longer term treasury bonds in the USA still remained stable despite increased interest rates. Shorter maturities moved in line with interest rates increases resulting in a notable flattening of the yield curve. Starting at the mid-year point capital markets increasingly believed that the ECB was really aiming to achieve normal conditions and not a further loosening of its monetary policy. In contrast, the ECB's continued purchases of sovereign bonds, covered bonds, corporate bonds and asset-backed securities supported these asset classes and in some instances resulted in a further tightening of spreads.

Figures in % | YIELD ON TEN-YEAR BUNDS 2017



Source: Bloomberg (closing rate)

In the currency markets the US dollar tended to weaken over the year despite the substantial increase in US money market interest rates and unbroken low euro rates. This development was in response to declining political risks and the surprisingly favourable development of the European economy. Over the course of 2017 the US dollar lost 14 cents to the euro and at the end of the year stood at 1.19 to the euro. The euro also posted significant gains over the Swiss franc during the year adding 9 percent to about 1.17 CHF. Although the British pound had already lost substantial value due to the Brexit decision it continued to weaken into 2017, albeit at a slightly slower pace. The improved outlook for an orderly Brexit had a stabilising effect on the pound in the second half of the year. Over the course of the year the pound fell by about 4 percent to end the year at 0.89 euro.

The covered bond market remained heavily influenced by the ECB's Covered Bond Purchase Programme (CBPP 3). About 30 percent of the volume of new issues was bought by the ECB. Although classical investors like banks, insurance companies and funds were active as buyers, the low level of interest rates and spreads limited their willingness to build new positions. Nevertheless, investments in covered bonds continued to benefit from their high credit standing and preferential regulatory treatment. The volume of new euro-denominated benchmark covered bond issues did, however, decline from € 127 billion in 2016 to € 112 billion in 2017, with a notable weakening seen in the second half of the year. French covered bonds represented 25.7 of the total volume of new covered bond issues in 2017 giving them the largest market share followed by German Pfandbriefe with 18.7 percent.

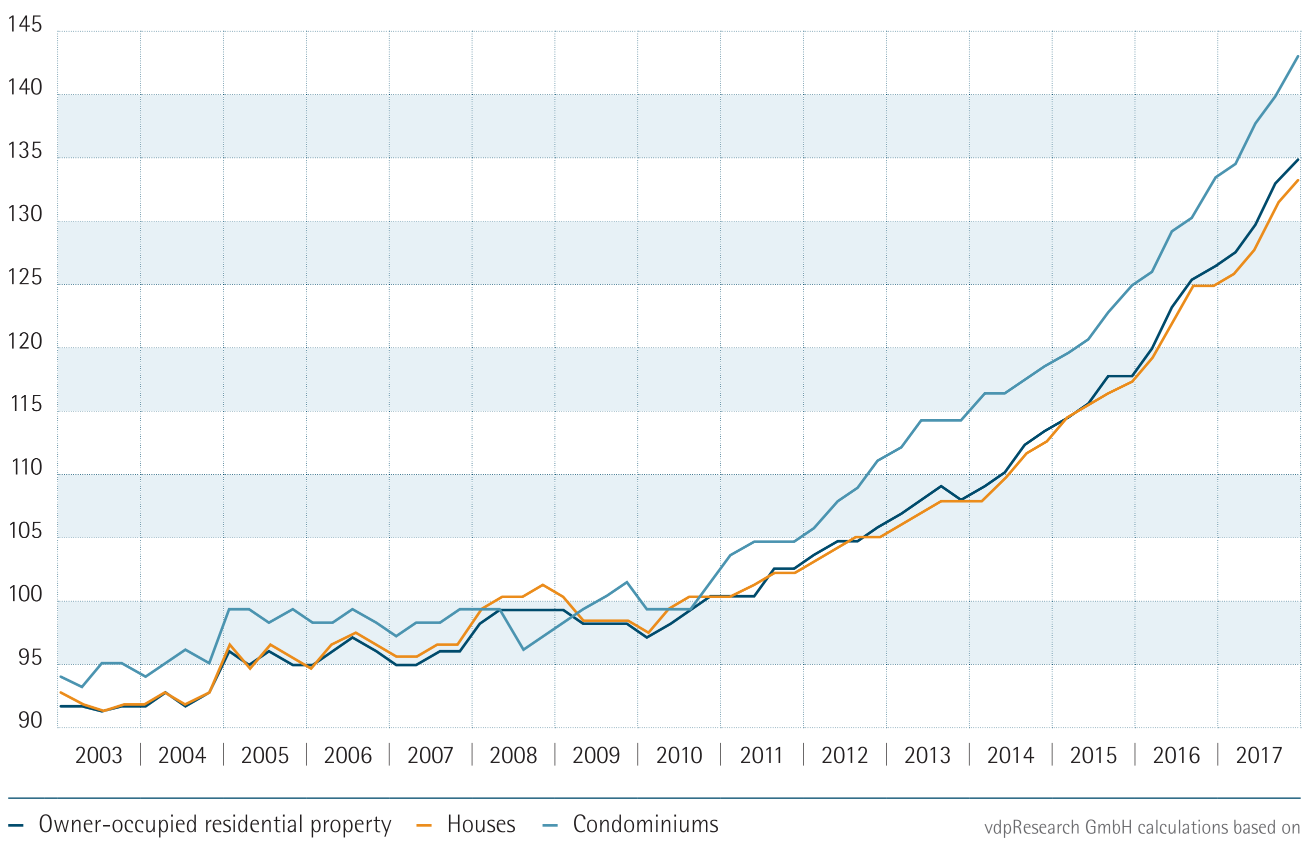
PROPERTY AND PROPERTY FINANCING MARKETS

RESIDENTIAL PROPERTY – GERMANY

The residential property market in Germany was again marked by rising purchase prices and rents in 2017. Prices accelerated even further compared to the previous year rising by 6.9 percent in 2017 according to the Association of German Pfandbrief Banks' (vdp) index for residential property prices. The strong 5.8 percent rise in prices affected owner-occupied residential property, as well as multi-family houses, which posted an increase of 7.9 percent.

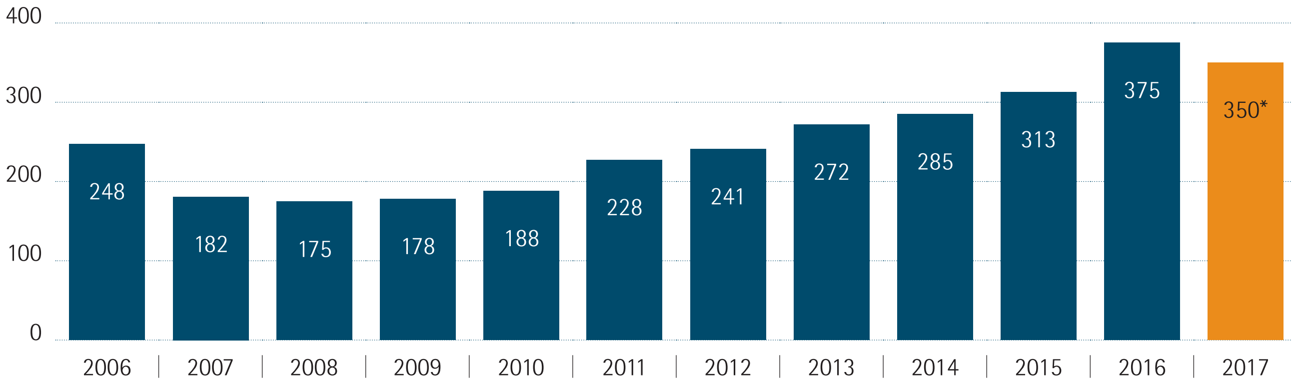
The pronounced increase in prices paid for multi-family houses was driven by high demand shown by institutional investors, which in turn led to a further decline in yields. A total of € 15.6 billion was invested in residential property portfolios in 2017, the third highest amount recorded within the last ten years. This segment of the market remained dominated by domestic investors with foreign buyers only representing 20 percent of the capital invested. Buying activity was focused on the seven biggest cities and major cities with above-average population growth as investors viewed these cities as offering the greatest market liquidity and thus the least risk. The availability of existing properties was tight across Germany. This led to a shift in investors' buying activities over to projects that were in the developmental stage. As a result, new construction developments represented about 30 percent of the total volume of transactions.

DEVELOPMENT OF PROPERTY PRICES IN GERMANY (YEAR 2010 = 100)



vdpResearch GmbH calculations based on information provided by vdp transaction databank
As of: February 2018

Figures in 000 | RESIDENTIAL BUILDING PERMITS IN GERMANY 2005 – 2017



* 2017 = estimated
Source: German Federal Statistical Office

The great interest shown in residential property in Germany – despite low yields – is due, in particular, to the situation in the rental housing market where shortages have existed for years in major metropolitan areas. The excess demand is due to the high number of persons moving to these regions, the current favourable income opportunities, as well as the significant increase in single-person households. This has led to rising rents, in particular, without higher yields as purchase prices have increased at a faster pace than rents. Based on vdp figures, the tempo of rental increases has slowed slightly to 3.2 percent, although it does continue to show that the situation in the rental housing market remains tight.

Although construction of new multi-family housing accelerated, the figures for newly completed housing still lags noticeably behind the number of newly issued building permits. In addition to the fact that the construction sector is operating at a high level of its capacities, it is thought that many building permits are being obtained without a specific intention to build. The total number of building permits issued by the end of November 2017 declined by 7.8 percent compared to the same year-ago period. This decline affected all segments.

Despite the very strong gains recorded for housing prices in many regions, high demand seen for houses and condominiums has also remained unchanged. Many private households would like to realise their hopes to buy their own home in view of low interest rates, the good employment situation and the favourable development of incomes. However, the number of transactions involving one and two-family houses barely changed in 2017. On average, about 250,000 private homes change hands every year indicating that there is a limited supply. Homeowners' willingness to sell was held back by a lack of investment alternatives and expectations that property prices will continue to climb.

New construction activity noted during the year under review was once again unable to keep pace with the high demand. Although the number of newly built homes has continually increased across the nation since 2010, and set a new 15-year record in 2017 with about 280,000 new housing units, it still lags behind actual housing needs. After taking into consideration various factors – above all migration to and within Germany, smaller households, and the backlog of demand for housing – Germany needs 350,000 to 400,000 new housing units per year.

Higher demand is primarily driven by fast growing regions and cities, which in turn have posted above-average strong price increases in recent years. According to figures released by vdp, residential property prices in the seven largest German cities rose by 13.7 percent in comparison to the previous year.

This was sufficient reason for the Bundesbank to closely examine development in cities and regions with very strong price growth in its latest Financial Stability Review. The study concluded that exaggerated prices exist in 127 German cities. However, the Bundesbank believes that threats to price stability still remain limited. This statement is based, in particular, on the slower pace of growth of loans for new housing, which is lower than the long term average rate. Furthermore, debt carried by private households showed a further slight decline and in 2017 and was substantially below the average figure in comparable economies. Another important aspect in the assessment was the unbroken trend of borrowers to obtain longer terms of fixed interest rate loans for financing housing, which also reduces their risk of fluctuating interest rates.

Competition among providers of private property financing increased even further. Enterprises within the Cooperative Financial Network, which include MünchenerHyp and its partner banks, held up well in this environment. As in previous years, the portfolios of residential property loans held by institutes within the Cooperative Financial Network expanded at a faster rate than the market.

RESIDENTIAL PROPERTY – INTERNATIONAL

In general, the residential property markets in Europe developed favourably, whereby the average increase in prices for all countries within the European Union (EU), as well as those within the euro area, strengthened again in 2017. The rise was driven by the favourable economic situation and the continuing low level of interest rates. Prices paid for houses in the EU in the third quarter of 2017 rose by 4.6 percent over the same year-ago period and by 4.1 percent in the euro area. Markets where a stronger pace of growth was noted include the Czech Republic, Ireland, Portugal, Hungary and the Netherlands, where double-digit percentage gains were recorded. Italy was the sole market where housing prices once again declined slightly.

The pace of rising prices for residential property in Great Britain weakened since mid-2016 as a consequence of the Brexit vote. However, in 2017 housing prices still increased by 5.2 percent over the previous year's figure, although there were notable regional differences. Prices in South West England grew by 7.5 while prices in London only increased by 2.5 percent. Furthermore, the volume of transactions fell by 6 percent in the same period of time. New construction of housing amounted to about 180,000 new housing units, which was substantially below the government's target of 275,000 housing units per year. The pace of growth noted in the private rental housing also slowed and the 1.1 percent increase noted was the lowest recorded since January 2012. London's increase of only 0.2 percent made it one of the weakest growing regions in the UK.

New construction of housing in France expanded notably in the past year as the number of housing units being built rose by about 15 percent to nearly 400,000 units or the highest level since 2011. At the same time, demand for housing was quite favourable in light of low lending rates. This development was also reflected in the number of new housing transactions, which climbed by 8 percent, and turnover of existing properties, which advanced by 9 percent. Prices paid for housing also rose. In the third quarter of 2017 prices of newly built properties rose by 3.6 percent over the same year-ago quarter, while existing properties were 3.9 percent more expensive. French residential property also gained in attraction by institutional investors, which in turn increased pressure on yields notably and especially for prime properties.

The Dutch housing market was driven by above-average economic growth, which was reflected by the very substantially higher figures recorded for the number and volume of transactions. A total of about 242,000 housing units changed hands in 2017, or about 13 percent more than in the previous year. The volume of transactions surged by 22 percent to nearly € 64 billion. Parallel to this development, prices paid for housing rose even further by 7.9 percent in comparison to the previous year's figure. This increase was driven by high demand that met a very limited supply. Excess demand was particularly visible in the four major population centres of Amsterdam, Utrecht, Den Haag and Rotterdam. Institutional investors also focused their demand on these four cities last year as they invested € 3.5 billion in residential property. Domestic buyers accounted for about two-thirds of the volume of transactions. The Dutch housing market as a whole was marked by a very tight supply of properties for institutional investors, which led to a further decline in returns.

Despite overall favourable economic conditions, growth noted for the Swiss housing market slowed over the course of the year. This is reflected by figures released by the Swiss Federal Statistical Office which showed that the number of vacant housing units stood at about 65,000 at mid-year 2017. This figure is nearly 15 percent higher compared to the previous year's figure, whereby the rental housing market was particularly affected. During the course of the year rents declined slightly, especially for units in the higher-priced segment. The level of prices paid for housing hardly changed on a year-over-year basis. Prices for condominiums rose by 1.9 percent and were only marginally higher than in 2016; prices for single-family homes grew at an unchanged 3.2 percent. Demand for residential property for personal use and as an investment remained high due to the Swiss National Bank's negative interest rates, as well as low mortgage rates.

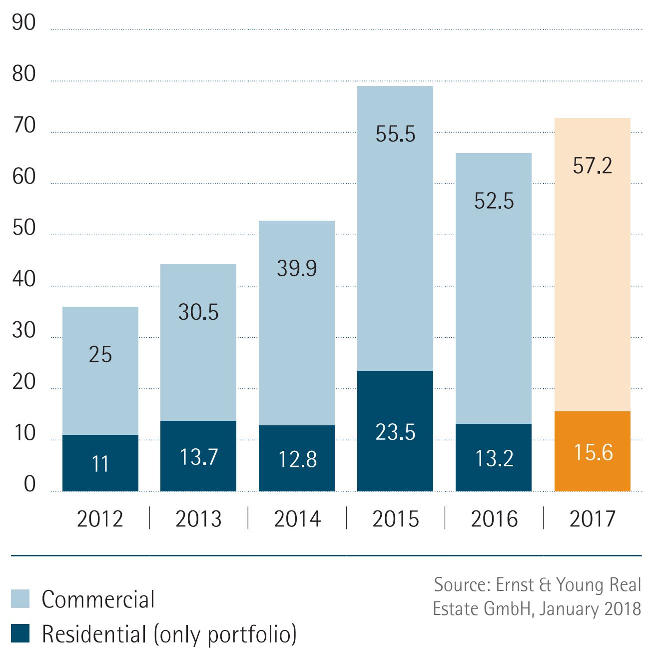
The upswing in the housing market in the USA continued in 2017. In November of 2017 the S&P/Case-Shiller Index figures showed a 6.2 percent year-over-year increase in housing prices. Prices did, however, vary quite differently on a regional basis with the strongest growth again recorded in the Seattle region, while Chicago and Washington D.C. remained at the bottom of the list. The increase in prices is due to excess demand and insufficient construction of new housing. Rents developed less dynamically rising by 2.4 percent following the 3.8 percent increase recorded in the previous year. Investments in residential property also fell. During the first nine months of 2017 USD 94 billion, or 12 percent less, was invested than in the same year-ago period. This change indicates that for the first time since 2009 the volume of transactions may also be lower for the entire year.

COMMERCIAL PROPERTY – GERMANY

German commercial property was again highly sought after by both national and international investors. This was, above all, due to the quality of Germany as an investment location, and not yields, as meanwhile returns on all asset categories are at historically low levels following above-average increases in prices seen in recent years. This was also the case in 2017 as the vdp index for commercial property rose by 6.5 percent on a year-over-year basis. This was the greatest increase in prices since the outbreak of the crisis in the financial markets.

The strong pace of growth noted for prices also led to a record volume of transactions in 2017. The figure if more than € 57 billion exceeded the top results recorded in 2015 by about 3 percent. Investors continued to focus on the seven biggest cities. Where € 31 billion were invested, or 54 percent of the total volume of transactions.

DEVELOPMENT OF COMMERCIAL PROPERTY TRANSACTIONS IN GERMANY 2011 – 2017
Figures in € billion



Source: Ernst & Young Real Estate GmbH, January 2018

Office properties retained their preferred status as investments. This sector has held about a 44 percent share of the total volume of transactions for years and represents turnover of just about € 25 billion. The great popularity of office properties is based on the very good state of the rental market, which again set a new record in the past year with total turnover of about 4.2 million square metres of space in the seven biggest cities. The volume of newly completed properties was, however, lower compared to the previous year's figure. This led to a further decrease in available vacant space. At the end of 2017 the vacancy rate stood at the lowest level seen in the last 15 years. In the interim there is hardly any office space available in preferred office districts in the seven biggest cities, which in turn has driven rents for office space even higher. The greatest increase in rents was noted in Berlin. Moreover, rising rents and great investor interest accelerated the pace of rising prices for office properties. Based on vdp figures, prices for office properties rose by 8.4 percent in comparison to the previous year.

The popularity of logistics properties increased in the past year while interest in retail properties decreased slightly. Many investors are increasingly viewing retail properties more critically in view of the booming online shopping business and the very high level of prices demanded for retail properties, which has shifted investors' attention to other asset categories.

COMMERCIAL PROPERTY – INTERNATIONAL

The good overall economic conditions had a particularly beneficial effect on the European office property market. Turnover of space in the rental market increased by 10 percent to 13 million square metres, which was the best result noted since 2007. This rise was accompanied by a substantial reduction of vacant space, which declined across Europe to 7.4 percent. On average, rents in Europe rose by 4 percent due to the limited availability of space.

Following the sudden downturn after the Brexit decision, the commercial property market in Great Britain has regained its footing and is advancing notably once again. This is reflected by the 15 percent increase in the volume of investments made in 2017. Foreign investors dominated market activities and accounted for about three-quarters of the volume of transactions recorded for office properties in London. Furthermore, turnover of space increased by 7 percent shrinking the vacancy rate to 4.7 percent and below the 10-year annual average. The short-lived drop in rents that occurred the previous year was stopped in 2017 due to the good demand seen for office space. This made it possible for peak rents to end the year on a stable note.

The volume of transactions noted for the French investment market declined once again. During the first nine months of 2017 more than € 14 billion was invested in commercial properties, or about 30 percent less than in the same year-ago period. The drop was due to a lack of investment properties as investors were still very keen on buying. Yields fell further in view of this situation. Properties in the Île-de-France were the preferred choice of investors with a significant focus on office properties. The vacancy rate moved at the previous year's 6.7 percent level. Top rents paid for office space remained stable while average rents paid, however, rose to a level last seen in the year 2000.

The Dutch investment market ended the last year with record results as total turnover for properties amounted to € 19.5 billion. Foreign companies accounted for a major portion of the capital invested. The primary focus was on office properties followed at great distant second place by retail and industrial properties. The upturn in office properties continued in 2017 and led to a substantial increase in rents. Amsterdam posted the highest rate of growth in Europe. The vacancy rate for office space fell reflecting the extremely favourable development of the economy.

The volume of transactions recorded for the American investment market declined again as foreign investors were less active. At mid-year point in 2017 volume was 14 percent below the same year-ago level. As the most important investment location in the USA, New York was particularly affected by this development as the volume of transactions recorded fell by half. In contrast, investors significantly expanded their activities in Boston, Washington D.C. and Los Angeles. The rental market is already in an advanced phase of its cycle, as reflected in the notable weakening in the growth of rents. Office properties were also the most important asset class in the USA and demand for office space was robust. The average rent paid for office space rose by 2.7 percent on a year-over-year basis. Nevertheless, the vacancy rate for office space rose slightly due to brisk new construction activities accompanied by a lower rate of pre-completion leases signed.

BUSINESS DEVELOPMENT

NEW MORTGAGE BUSINESS

MünchenerHyp set a new record in 2017 as our volume of new mortgage business exceeded € 5 billion for the first time. Our new business grew by 2.5 percent as we made € 5.1 billion in lending commitments (previous year € 4.9 billion), thereby reflecting a slightly faster pace of growth in our business.

Both of our main areas of business, private and commercial property financing, benefited from the good environment for property and the associated high demand for property financing seen during the year under review. For this reason, we are very satisfied with the development of our new business activities, which were able to expand as forecast

MÜNCHENERHYP NEW MORTGAGE BUSINESS
2013 – 2017
Commitments in € million

We were able to sustain our new business performance in the private property financing area at the previous year's very high level in the intensely competitive market. We made loan commitments for a total volume of € 3.2 billion (previous year: € 3.3 billion). Our special sales campaigns in the spring and autumn of 2017 contributed to this success as each of them was met very favourably by our partner banks and customers. In addition, the share of forward financing transactions developed favourably in view of considerations that the ECB's loose monetary policy could be ending.

The volume of new lending commitments made to finance domestic private residential property brokered by banks within the Cooperative Financial Network was € 2.4 billion, basically unchanged from last year's volume of € 2.45 billion. Sales generated by independent providers of financial services increased by 8 percent on a year-over-year basis to € 419 million. New business brokered by Swiss PostFinance totalled € 373 million, or about € 50 million below the previous year's level due to intensifying price competition.

Our commercial property financing business was successful in 2017 and grew by 13 percent to € 1.9 billion (previous year € 1.7 billion).

We are particularly pleased that we were able to achieve these good results in a competitive environment characterised by shrinking margins and competitors willing to take on riskier financing deals. For our part we succeeded in attaining comparatively attractive margins across the entire span of our new commercial property business without exposing the Bank to inappropriate risks.

We posted gains in our domestic, as well as our international business activities, especially in Great Britain, Spain and the Netherlands, which contributed to our good results. In addition, our re-entry into USA also made a favourable impression.

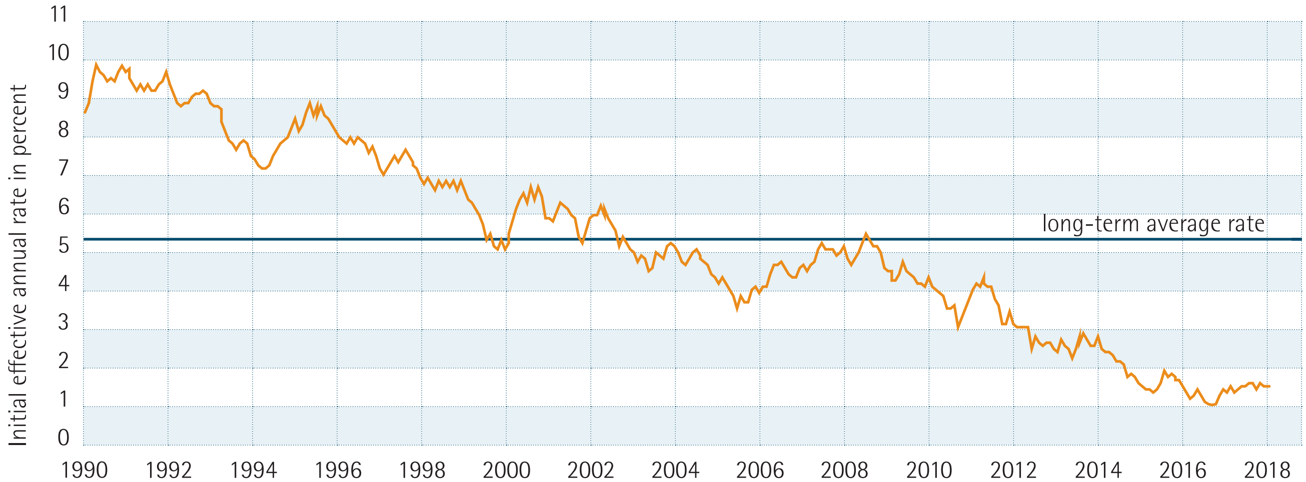
Furthermore, our new commercial property finance business benefited from the Bank's new syndication strategy where we act as the underwriter for larger loans that are generally more margin-attractive. We then syndicate a volume of about € 200 million to other providers of financing, with a special focus on our Cooperative Financial Network's syndication programme. Within the framework of the programme we enable the Volksbanken and Raiffeisenbanken to participate in commercial property loans we have made. This offer received a very favourable response.

CAPITAL MARKETS BUSINESS

Our investment strategy concerning securities issued by the public-sector and banks in 2017 was determined by regulatory requirements and very low spreads. Sovereign bonds and covered bonds continue to trade at very high levels due to the ECB's asset purchase programme.

In accordance with our business strategy, we again limited our capital market dealings in the past year. The net total volume of our existing portfolio was reduced by about € 1.0 billion to

MORTGAGE RATES MÜNCHENERHYP (TEN YEAR FIXED RATE)



As of: 02.01.2018

€ 5.7 billion. Our volume of new business totalled € 25 million in 2017 following € 109 million in 2016.

REFINANCING

The Pfandbrief markets were once again dominated by the ECB's Covered Bond Purchase Programme (CBPP3) in 2017. Markets were additionally influenced by political developments in Europe, especially elections in Germany, France and the Netherlands. Despite this difficult environment we found ample windows of opportunity to place new issues, which we used to refinance our activities at attractive conditions.

We floated our first benchmark issue of the year under review in May with a € 500 million Mortgage Pfandbrief that had a term of ten years and carried a coupon of 0.625 percent. The issue was priced at 12 basis points below the mid-swap rate. Thirty-four orders were received from investors in nine countries with Germany accounting for 83.5 percent of the volume sold followed by countries in Asia and the Middle-East. Excellent market conditions allowed the Bank to tap the issue by an additional € 250 million in October. The success is reflected by the price, which was set at 17 basis points below the mid-swap rate.

We successfully issued another Mortgage Pfandbrief in benchmark format in August, which is actually the classical summer vacation month in the capital market. Demand in the market was so great that we issued a volume of € 750 million. The Mortgage Pfandbrief had a term of nine years and two months and again carried a coupon of 0.625 percent. Market interest was reflected by the 64 orders received form ten countries, with Germany once again with the lion's share of orders. The issue was placed at a price of 13 basis points below the mid-swap rate.

The share of foreign currency denominated issues declined in the year under review by a total of 13 percent as the attractiveness of refinancing in US dollars and pound sterling declined substantially in comparison to euro-denominated issues.

The Swiss franc was the primary currency for our foreign currency denominated issues as we placed a total volume of CHF 810 million. In January we issued a two-year Mortgage Pfandbrief with a volume of over CHF 250 million. We followed up this issue with an additional two-year Mortgage Pfandbrief that had a volume of CHF 250 million. Due to strong demand seen for this issue we tapped it for an additional CHF 50 million one day after the issue.

We successfully placed a seven-year unsecured Swiss franc denominated bond in September. The bond had a volume of CHF 160 million.

In October we entered new territory when we issued a 15-year Mortgage Pfandbrief in benchmark format with a volume of CHF 100 million. The issue was priced at 8 basis points below the Swiss franc mid-swap rate. The issue caused a commotion in the Pfandbrief markets as this marked the first time ever that a foreign issuer of covered bonds achieved a higher interest rate discount compared to the domestic Swiss Pfandbrief curve.

Only one large-volume bond matured during the previous business year: a Public Pfandbrief with a volume of € 0.5 billion matured in September.

The total volume of issues placed in the capital markets in 2017 amounted to € 5.6 billion, of which Mortgage Pfandbriefe accounted for € 4.2 billion in covered refinancing, while unsecured refinancing amounted to € 1.4 billion. During the period under review we once again did not issue any Public Pfandbriefe due to the direction of MünchenerHyp's business strategy.

PORTFOLIO DEVELOPMENT MÜNCHENERHYP
2013 – 2017
in € million

ASSET, FINANCIAL AND EARNINGS SITUATION

BALANCE SHEET STRUCTURE

By the end of 2017 total assets had risen to € 38.9 billion, following € 38.5 billion at 31 December 2016. The increase was driven by the unbroken favourable development of our new business results.

Our portfolio of mortgage loans grew by € 1.4 billion over the course of the year to € 29.2 billion. Private residential property financing was again the strongest growing segment of our business as it increased by € 1.0 billion.

Our portfolio of private residential property loans is structured as follows: domestic mortgage loans € 17.0 billion (previous year € 15.9 billion), foreign mortgage loans € 4.1 billion (previous year € 4.2 billion), which are solely loans made to finance residential property in Switzerland.

Our portfolio of commercial property loans totalled to € 8.1 billion (previous year € 7.7 billion), of which € 1.9 billion (previous year € 1.7 billion) represented loans made outside of Germany. Great Britain is our most important foreign market with 25 percent (previous year 23 percent), followed by the Netherlands with 21 percent (previous year 20 percent) and France with 18 percent (previous year 18 percent). Property we financed in the USA accounted for 10 percent (previous year 13 percent) of the total.

In accordance with our business and risk strategy, our portfolio of loans and securities related to our business with the public-

The item "Other liabilities to customers" is structured as follows:

	Remaining term < one year	Remaining term > one year	Total
	in € 000	in € 000	in € 000
Other liabilities to customers as of 31.12.2017	**738,865**	**2,081,807**	**2,820,672**
Registered bonds	**13,852**	**1,283,681**	**1,297,533**
of which institutional investors	13,121	1,261,681	1,274,802
Promissory note loans on the liabilities side	**654,129**	**798,126**	**1,452,255**
of which institutional investors	353,825	759,926	1,113,751
Other	**70,884**	**0**	**70,884**
of which institutional investors	28,549	0	28,549

sector and banks declined further from € 6.8 billion to € 5.7 billion, of which € 2.4 billion were securities and bonds.

At the end of 2017 the net sum of unrealised losses and unrealised gains in our securities portfolio amounted to plus € 58 million (previous year plus € 41 million). These figures include unrealised losses of € 1 million (previous year € 6 million) stemming from securities issued by countries located on the periphery of the euro area and banks domiciled in these countries. The total volume of these securities still amounted to € 0.4 billion (previous year € 0.6 billion).

Following a detailed examination of all securities we came to the conclusion that no permanent reductions in value are required. We are keeping these bonds on our books with the intention of holding them until they mature. Write-downs to a lower fair value were not necessary.

The portfolio of long-term refinancing funds increased by € 1.3 billion to € 34.1 billion, of which € 23.1 billion consisted of Mortgage Pfandbriefe, € 3.4 billion of Public Pfandbriefe and € 7.6 billion of unsecured bonds. The total volume of refinancing funds – including money market funds – increased from € 35.8 billion in the previous year to € 36.4 billion on 31 December 2017.

Paid-up capital increased by € 49.0 million to € 1,004.9 million. Total regulatory equity capital amounted to € 1,390.9 million (previous year: € 1,343.1 million).

Common Equity Tier 1 capital rose from € 1,251.3 million in the previous year to € 1,316.0 million. On 31 December 2017 the Common Equity Tier 1 capital ratio was 23.8 percent (previous year 22.9 percent), the Tier 1 capital ratio was also 23.8 percent (previous year 22.9 percent) while the total capital ratio was 25.2 percent (previous year 24.5 percent). The leverage ratio was 3.4 percent on 31 December 2017.

DEVELOPMENT OF EARNINGS

Net interest income[1] increased by € 23.2 million or 9.9 percent to € 256.6 million. We were able to increase this figure as predicted, which was especially due to the sustained success of our new business activities during the year under review. This figure also contains a single-digit million euro expense figure arising from the early termination of interest rate swaps.

Commissions paid were close to last year's level and amounted to € 82.6 million. Commission income declined to € 8.1 making net commission balance[2] a minus € 74.5 million, following minus € 74.2 million in the previous year.

1) Net interest income is calculated by adding Item 1 Interest income plus Item 3 Current income plus Item 4 Income from profit-pooling, profit transfer or partial profit transfer agreements minus Item 2 Interest expenses as shown in the Income statement.
2) The net commission balance is the net sum of Item 5 Commission received plus Item 6 Commission paid as shown on the income statement.

This resulted in a net interest income and net commission income figure[3], of € 182.1 million, an increase of € 22.9 million or 14 percent.

"General administrative expenses" rose by € 7.6 million to € 93.6 million, while personnel expenses increased by € 1.9 million or 4.3 percent.

Other administrative expenses rose by € 5.7 million or 13.5 percent. This increase was mainly due to projects aimed at optimising the processing of loans. Regulatory issues also contributed to higher costs, especially the implementation of the Markets in Financial Instruments Directive (MiFID II) and its corresponding regulation.

"Depreciation and write-downs of intangible and tangible assets" amounted to € 6.0 million or € 0.2 million less than the same year-ago figure.

Total administrative expenses[4] amounted to € 99.6 million compared to the € 92.2 million noted in the previous year. The cost-income ratio[5] was 55 percent (previous year 56 percent).

The net sum of other operating expenses and income totalled minus € 3.8 million.

Results from operations before deducting provisions for risk[6] rose by 24 percent over the previous year's figure to € 78.7 million Euro.

The item "Income from reversals of write-downs to claims and certain securities, as well as from reversals of provisions for possible loan losses", totalled plus € 1.5 million after allocations to reserves pursuant t o Article 340f of the German Commercial Code. The credit risk situation remained unremarkable. The net sum of reversals to provisions made for risks in the lending business (including direct write-downs) amounted to plus € 10.5 million (previous year: minus € 16.4 million).

Net income derived from the sale of promissory note loans, and the redemption of registered securities and debt securities, amounted to € 4.5 million.

The item "Income from write-downs on participating interests, shares in affiliated companies and securities treated as fixed assets" amounted to plus € 4.9 million. This figure is primarily the result of proceeds from the sale of securities held as fixed assets.

Results from ordinary business activities amounted to € 85.1 million, an increase of 26 percent. After transferring € 5 million to the "Fund for General Banking Risks" pursuant to Art. 340g of the German Commercial Code and a tax expense item of € 33.8 million, annual net income amounted to € 46.3 million, which was 45 percent higher than in the previous year.

RATING, SUSTAINABILITY AND REGULATORY CONDITIONS

RATING

In November 2017 the rating agency Moody's raised its Baseline Credit Assessment (BCA) for MünchenerHyp to ba1. The BCA corresponds to the standalone rating of a bank. This decision takes various favourable developments of MünchenerHyp's key figures into consideration. The higher BCA rating was primarily due to the further improvement in the Bank's level of equity capital, as well as the moderate risks in its loan portfolio.

Moody's final rating for the Bank – including external support from the government and the Cooperative Financial Network – did not change. In December 2017 the agency did, however, change the outlook for the rating of the Bank's senior unsecured liabilities to negative.

3) The net interest income and net commission income balance is the sum of net interest income and the net commission balance.
4) Administrative expenses are the sum of Item 8 General administrative expenses and Item 9 Depreciation and write-downs of intangible and tangible assets as shown on the income statement.
5) Ratio between administrative expenses and net interest and commission income.
6) Net sum of Income Statement items 1 to 10.

Current ratings at a glance:

	Rating
Public Pfandbriefe	Aaa
Mortgage Pfandbriefe	Aaa
Senior unsecured liabilities	A1*
Short-term liabilities	Prime-1
Long-term deposits	Aa3

* The outlook for the rating for senior unsecured liabilities is negative.

The revision is due to a change in the methodology Moody's employs to make its ratings. The rating agency now assumes that the EU's Bank Recovery and Resolution Directive (BRRD) will be transformed into national law in Germany leading to the federal government providing weaker support to many banks. For this reason, the negative outlook affects a total of 16 banks that Moody's rates in Germany. The outlook for all other of MünchenerHyp's ratings remained stable.

Moody's did not change its opinion that MünchenerHyp had a solid reputation in the capital markets as an issuer of Pfandbriefe and thus has a correspondingly high level of refinancing strength. The agency also noted favourably the Bank's firm ties and related support within the Cooperative Financial Network.

Even to achieve its highest rating of Aaa for Pfandbriefe, Moody's only requires that legal requirements are observed, thus voluntary provision of surplus cover is not required.

Our long-term unsecured liabilities are rated AA- by both of the two other major rating agencies Standard & Poor's and Fitch due to the group rating assigned to the Cooperative Financial Network by the agencies.

SUSTAINABILITY

The strategic goal of our sustainability management activities is to further anchor sustainability in our core business. These efforts are directed by a sustainability manager and a sustainability committee comprised of employees from various departments within the Bank.

During the year under review we developed an additional sustainable financing product in our residential property financing area of business: the MünchenerHyp Family Loan. This product addresses an important social dimension of a holistic understanding of sustainability. The social benefits of the MünchenerHyp Family Loan consist of providing support to lower and middle income families by making an interest rate rebate available to them. The sustainability of the Family Loan has been certified by Oekom Research, which confirmed that the loan "makes a contribution to the intergenerational creation and securing of prosperity,

The development of our sustainability ratings since 2015 at a glance:

	2015	2016	2017/2018
oekom research	C	Corporate Responsibility Prime rated by oekom research C+	Corporate Responsibility Prime rated by oekom research C+
imug	Public Pfandbriefe: favourable Mortgage Pfandbriefe: neutral Unsecured bonds: neutral	Public Pfandbriefe: very favourable Mortgage Pfandbriefe: favourable Unsecured bonds: favourable	Public Pfandbriefe: very favourable Mortgage Pfandbriefe: favourable Unsecured bonds: favourable
Sustainalytics	**57 of 100 points**	**57 of 100 points**	**60 of 100 points**

taking into account such aspects as equal opportunity, participation and quality of life, as well as developments that arise in the course of demographic change". The Family Loan was introduced to the market at the beginning of 2018.

The sustainability rating agency oekom research continues to rate MünchenerHyp as one of the three best banks in the category of "Financials/Mortgage and Public Sector Finance". We received a C+ rating. Oekom Research rates MünchenerHyp ecological commitment with B-, and its social commitment with C+. At the same time the agency also confirmed the Bank's "Prime Status".

The agency imug confirmed all of MünchenerHyp's sustainability ratings at the beginning of 2017. The agency issued a "very favourable" rating for our Public Pfandbriefe, and a "favourable" rating for our Mortgage Pfandbriefe and unsecured bonds. The rating for Mortgage Pfandbriefe means that the Bank holds the best rating among the 30 German issuers rated by imug.

The sustainability rating agency Sustainalytics raised our rating in the beginning of 2018. We currently are rated 60 out of a possible 100 points.

REGULATORY CONDITIONS

BASEL III

MünchenerHyp uses the Internal Ratings Based Approach (IRBA) to calculate its equity capital requirements.

The Liquidity Coverage Ratio (LCR) was comfortably met throughout the entire year with figures considerably higher than 100 percent. Furthermore, the Net Stable Funding Ratio (NSFR) was also continuously over 100 percent.

Within the framework of Basel III a leverage ratio with a limit of 3 percent for the entire nominal volume of loans made by a bank in relation to its equity capital was also introduced. Up until now this ratio only had to be reported. However, as of 1 January 2019 this new rule will become a mandatory requirement for banks. At the end of 2017 MünchenerHyp's leverage ratio stood at 3.43 percent.

The Basel Committee on Banking Supervision (BCBS) finalised new standards for equity rules for credit institutions at the end of 2017. The regulatory standards are particularly focused on revising the standard approach as well as the internal approaches used to calculate risk weight for credit risks; establishing a binding definition of a new standard approach for operational risks, and the introduction of a floor of 72.5 percent to limit the effects of internal approaches compared to standard approaches. The finalised standards reflect the content of the most recent discussions to a great extent. Above all, this means that banks operating with a low level of risk, like MünchenerHyp, will be impacted by the changes as the introduction of the floor will have a negative effects on MünchenerHyp's equity capital ratios. Based on the current state of information, we do not expect that we will have to raise additional equity capital due to our very good level of capital.

We are attentively following current discussions and publications of various authorities regarding regulatory requirements. It is difficult to comprehensively prepare to meet future requirements at this time as widely varying positions are still regularly held by the different institutions involved in the current discussions at national, European and international levels. For this reason, we will continue to prepare to the greatest extent possible, although we will wait until the final version of the individual rules have been approved before we begin to implement them. We therefore believe it is necessary for the regulators to provide an appropriate amount of time – especially IT requirements – for implementation purposes.

All regulatory issues were, and are being, monitored by a central unit within MünchenerHyp, transmitted to the responsible departments and implemented in various projects. Up until today all of the requirements have been implemented on time. The enormous flood of new requirements mandated by the supervisory authority does, however, generate significant costs and requires us to continually create new plans to utilise the Bank's tight resources.

SINGLE SUPERVISORY SYSTEM FOR EU BANKS

The ECB again conducted its Supervisory Review and Evaluation Process (SREP) in 2017 that carefully examined the Bank's business model, its internal governance as well as its available capital and liquidity. The results indicate if additional equity capital or liquidity is required. The results of the SREP for MünchenerHyp revealed a mandatory minimum required ratio of 7.88 percent for the Bank's Common Equity Tier 1 capital.

MINIMUM REQUIREMENTS FOR RISK MANAGEMENT (MaRisK)

The MaRisk was updated at the end of 2017. As no major changes were made compared to the last versions, we anticipate that the Bank will be able to implement the updated requirements on time.

RECOVERY AND RESOLUTION PLANS

The Recovery Plan was updated. Furthermore information required for the Resolution Plan was provided to the resolution authority. Only minor adjustments were required in comparison to the previous year.

MAIN OFFICE, BODIES, COMMITTEES AND PERSONNEL

MAIN OFFICE

Münchener Hypothekenbank eG's main office is located in Munich. In addition, the Bank maintains a branch office in Berlin, and also has ten regional offices.

BODIES AND COMMITTEES

The Delegates Meeting elected Josef Hodrus, Spokesman of the Board of Management of Volksbank Allgäu-Oberschwaben eG, as a new member of MünchenerHyp's Supervisory Board.

At the end of Delegates Meeting Heinz Fohrer, member of the Board of Management of the Volksbank Esslingen eG, stepped down from the Supervisory Board. The Chairman of the Supervisory Board, Wolfhard Binder, thanked Heinz Fohrer for his great dedication and efforts during the years marked by numerous regulatory challenges.

EMPLOYEES

Following the slight increase in the number of employees noted in the past two years, the growth in the Bank's number of employees accelerated again in 2017 as we recruited 74 new employees to fill vacant position. This development meant that the focus of our human resources work was on recruiting and, above all, the integration of the new employees. In comparison to the previous year, MünchenerHyp's employee fluctuation figure rose slightly to 6.0 percent (2016: 5.4 percent). However, when compared to the average percentage for the sector, our figure remained at a low level.

The integration and development of personnel continued to gain importance at the Bank in light of the more than 100 new colleagues we hired in the past two years. The central elements in this area are the internal and external opportunities to advance employee skills and knowledge, management development, as well as other personnel development and personal commitment measures.

The average number of persons employed[7] by MünchenerHyp during the year under review was 509 employees, plus 11 apprenticed trainees. Despite numerous new hires, the average number of years of employment per employee remained almost constant at 11.3 years.

CORPORATE GOVERNANCE STATEMENT PURSUANT TO ART. 289f GERMAN COMMERCIAL CODE (HGB)

In 2016 the Supervisory Board passed a resolution defining a quota for women represented on the Supervisory Board, the Board of Management and the top two executive levels below the Board of Management. The target quota for the Supervisory Board and the top two executive levels below the Board of Management is 20 percent and 33 percent for the Board of Management. During the year under review the quota for women in each of the top two executive levels below the Board of Management was 18 percent and 8 percent in the Supervisory Board. No women were represented on the Board of Management. During the year under review the Supervisory Board's Nomination Committee resolved to recommend that the target quota should be achieved by the end of October 2021. Notwithstanding the above MünchenerHyp considers itself to be a modern enterprise as reflected by its social, cultural and business values and views the promotion of the underrepresented gender as a natural element of its embedded leadership culture.

7) Number of employees pursuant to Art. 267 (5) German Commercial Code (HGB): Excluding apprenticed trainees, employees participating in parental leave, early retirement, partial retirement (non-working phase), or employees suspended with pay.

MANAGEMENT REPORT 2017
RISK, OUTLOOK AND OPPORTUNITIES REPORT

RISK REPORT

The ability to monitor and keep risks under control at all times is essential for the successful management of business development at MünchenerHyp. For this reason, risk management plays a very important role in the overall management of the Bank.

The business and risk strategy defines the parameters of the Bank's business activities. MünchenerHyp's entire Board of Management is responsible for this strategy, which is regularly reviewed regarding the attainment of goals and updated as necessary and then submitted to the Supervisory Board no less than once a year.

As part of its supervisory duties, the Supervisory Board is advised about the Bank's risk profile no less than on a quarterly basis and additionally as required. This takes place using the reports concerning the Bank's risk-taking capabilities and lending risks, the OpRisk reports, as well as the risk report prepared in accordance with the "Minimum Requirements for Risk Management" (MaRisk).

The basis of risk management consists of, on the one hand, the analysis and presentation of existing risks, and, on the other, comparing these risks with the risk cover potential (ability to bear risk). Furthermore, a series of additional relevant analyses are in place and only when they are viewed as a whole do they permit the Bank to be managed appropriately. This objective is achieved by employing appropriate monitoring processes involving internal process-dependent supervision measures. Our internal audit department, as a process-independent unit, plays an additional monitoring role within the Bank.

The analysis and presentation of existing risks primarily distinguishes between counterparty, market price, credit spread, liquidity, investment, modelling and operational risks. Additional risks such as placement risks, reputational risk, business risk etc., are viewed as parts of the abovementioned risks and are taken into consideration at the appropriate place in the individual calculations.

COUNTERPARTY RISK

Counterparty risk (credit risk) is of major importance for MünchenerHyp. Counterparty risk refers to the danger that counterparties may delay their payment obligations to the Bank; only make partial payments or even default.

The Credit Handbook presents the competencies and procedural requirements of the units involved in lending, as well as the approved credit products. The business and risk strategy contains additional explanations pertaining to sub-strategies regarding target customers and target markets, as well as definitions for measuring and controlling credit risks at the individual deal and portfolio levels. A procedure based on the credit value-at-risk (Credit-VaR) is used to determine lending limits. The individual contribution of every borrower (aggregate debtor or limit group as appropriate) – the Marginal Credit-VaR – to the Bank's total credit risk is limited. Furthermore, limits are also set for each country to ensure adequate regional diversification.

We take care to ensure that the vast majority of our mortgage business activities consist of top tier loans with moderate loan-to-value ratios. The current breakdown based on loan-to-value ratios is as follows:

TOTAL PORTFOLIO OF MORTGAGE AND OTHER LOANS (INCLUDING OPEN COMMITMENTS)

MORTGAGE LENDING VALUE RATIO	31 Dec. 2017		31 Dec. 2016	
	€	relative	€	relative
Up to 60 %	14,296,965,287.66	45.6%	13,728,296,351.62	46.2%
60.01 % to 70 %	6,280,906,478.52	20.0%	5,677,718,196.80	19.1%
70.01 % to 80 %	6,682,115,544.81	21.3%	6.311,223,356.12	21.2%
80.01 % to 90 %	2,272,306,838.37	7.2%	2,154,390,691.97	7.3%
90.01 % to 100 %	1,053,463,631.24	3.4%	1,106,925,787.91	3.7%
over 100 %	755,022,711.92	2.4%	711,366,203.19	2.4%
without	15,847,972.98	0.1%	25,419,250.26	0.1%
Total	**31,356,628,465.50**	**100.0%**	**29,715,339,837.87**	**100.0%**

The regional breakdowns within Germany and abroad are as follows:

TOTAL PORTFOLIO OF MORTGAGE AND OTHER LOANS (INCLUDING OPEN COMMITMENTS)

REGION	31 Dec. 2017		31 Dec. 2016	
	€	relative	€	relative
Baden-Wuerttemberg	2,794,684,631.11	8.9%	2,616,357,406.41	8.8%
Bavaria	5,849,474,855.94	18.7%	5,646,905,936.17	19.0%
Berlin	1,515,024,630.55	4.8%	1,621,952,619.85	5.5%
Brandenburg	549,477,361.59	1.8%	490,537,743.87	1.7%
Bremen	93,497,213.85	0.3%	72,477,010.74	0.2%
Hamburg	936,793,198.61	3.0%	714,905,017.62	2.4%
Hesse	1,742,536,130.56	5.6%	1,616,366,977.79	5.4%
Mecklenburg-Lower Pomerania	384,874,380.79	1.2%	338,336,073.85	1.1%
Lower Saxony	2,102,093,778.96	6.7%	1,947,571,402.44	6.6%
North Rhine-Westphalia	4,502,314,653.67	14.4%	4,175,437,802.38	14.1%
Rhineland-Palatinate	1,227,865,749.56	3.9%	1,090,638,755.50	3.7%
Saarland	276,568,563.00	0.9%	224,663,431.89	0.8%
Saxony	873,208,941.08	2.8%	830,836,929.91	2.8%
Saxony-Anhalt	479,890,424.73	1.5%	432,564,548.35	1.5%
Schleswig-Holstein	1,694,132,583.00	5.4%	1,675,695,390.58	5.6%
Thuringia	317,419,939.59	1.0%	235,292,855.09	0.8%
Total domestic	**25,339,857,036.59**	**80.8%**	**23,730,539,902.44**	**79.9%**

TOTAL PORTFOLIO OF MORTGAGE AND OTHER LOANS (INCLUDING OPEN COMMITMENTS)				
SOVEREIGN STATE	31 Dec. 2017		31 Dec. 2016	
	€	relative	€	relative
Austria	117,228,434.45	0.4%	129,371,291.34	0.4%
France	334,128,112.01	1.1%	306,183,794.26	1.0%
Great Britain	457,267,526.70	1.5%	389,373,033.56	1.3%
Spain	241,773,685.93	0.8%	187,861,502.87	0.6%
Luxembourg	80,026,000.00	0.3%	48,626,000.00	0.2%
Switzerland	4,163,212,729.66	13.3%	4,321,626,705.80	14.5%
The Netherlands	392,584,077.07	1.3%	326,947,813.21	1.1%
Belgium	43,455,852.39	0.1%	49,976,456.52	0.2%
USA	187,095,010.70	0.6%	224,833,337.87	0.8%
Total foreign	**6,016,771,428.91**	**19.2%**	**5,984,799,935.43**	**20.1%**
Total domestic and foreign	**31,356,628,465.50**	**100.0%**	**29,715,339,837.87**	**100.0%**

The management of credit risks begins with the selection of the target business when drafting the terms of the loan, using risk cost functions that are regularly reviewed. A variety of rating or scoring procedures are used depending on the type and risk content of the transaction.

In addition, a computer-based early warning system is used to identify risks on a timely basis.

Property financing contains a broadly diversified portfolio of loans with emphasis on residential property financing and a credit approval process that has proven its value over many years as reflected in a portfolio with a low level of credit risk. Our lending business with public sector borrowers and banks is primarily focused on central and regional governments, regional and local authorities, and west European banks (only covered bonds). Regional emphasis is on Germany or Western Europe respectively. Our objective for this portfolio is to further reduce its volume due to reasons such as the introduction of the leverage ratio. Highly liquid sovereign bonds and other very creditworthy securities will, however, continue to be needed in order to meet the new liquidity requirements mandated by Basel III.

Depending on their ratings, mortgage loans are examined to determine any non-performance or other negative factors which could trigger an individual adjustment to value. Furthermore, an additional system to monitor individual adjustment to value is used by the Bank's work-out management department, especially for the non-retail market business.

The Bank has created a general adjustment-to-value reserve as a precautionary measure to cover latent lending risks. This general adjustment to value is calculated per the terms contained in a Federal Ministry of Finance notice dated January 10, 1994.

Individual adjustments to value taken remained at a low level for our residential property financing business due to the great stability of the residential property market. This also generally applies for our commercial property financing business.

Business relationships with financial institutions are primarily based on master agreements that permit settlement of claims and liabilities (netting) vis-a-vis the other institution. In general, we also enter into security agreements. We use a so-called Central Counterparty (CCP) as the preferred basis for settling derivative trades.

The individual and general adjustments to value developed as follows in 2017:

TOTAL LENDING BUSINESS						
in € millions	Opening balance	Addition	Reversals	Utilisation	Changes related to exchange rate shifts and other factors	Closing balance
Individual adjustments to value	66.0	6.0	-13.0	-8.5	-4.0	46.5
General adjustments to value	13.0	0.0	0.0	0.0	0.0	13.0

MARKET PRICE RISKS

Market price risks consist of the risks to the value of positions due to changes in market parameters including interest rates, volatility and exchange rates among others. These risks are quantified as potential losses of present value using a present value model that differentiates between risks related to interest rates, options and currency rates.

Interest rate risks are divided into two categories: general and specific interest rate risks. General interest rate risks refer to risks arising from changes in the market value of investments or liabilities that are dependent on the general level of interest rates, and which will react negatively if interest rates change.

Specific interest rate risks are also referred to as (credit) spread risks, and are included under market price risks. Credit Spread is the term used to describe the difference between the yield generated by a risk-less bond and a risky bond. Spread risks take into account the danger that this difference in interest rates can change although credit-worthiness ratings remain unchanged. The reasons for altered yield premiums are:

- varying opinions of market participants regarding positions,
- the creditworthiness of the issuer actually changes although the issuer's credit rating does not yet reflect this change,
- macro-economic factors that influence creditworthiness categories.

The Bank's portfolio of bonds issued by euro area countries more heavily affected by the sovereign debt crisis, or in bonds issued by banks domiciled in these countries, remained at a moderate level. The Bank has not made any new investments in countries located on the periphery of the euro area since 2011. We do not believe that our investments are in danger of default. We are of the opinion that measures taken by individual countries, as well as protective mechanisms enacted at EU levels, are sufficient to ensure the repayment of the affected liabilities. In the case of bank bonds issued by banks domiciled in these countries, all of these bonds are covered bonds so that in this instance we also anticipate that they will be repaid as contractually agreed.

Among other risks, options involve the following risks: volatility risk (Vega; risk that the value of a derivative instrument will change due to increasing or decreasing volatility), time risk (Theta; is understood to the risk that measures how the passage of time impacts on the value of a derivative instrument), Rho risk (risk associated with a change in the value of the option due to a change in a riskless rate of interest), and Gamma risk (risk of a change in the option's Delta due to a change in the price of the underlying security; the option's Delta thereby describes the change in the price of the option due to the change in the value of the underlying security). The volume of risks assumed is moderate as options are generally not employed in the capital market business for speculative purposes. Option positions are almost solely entered into on an implied basis due to debtors' option rights (for example the right to give legal notice of termination per Art. 489 of the German Civil Code – BGB) and are then hedged if needed. These risks are attentively monitored in the daily risk report and are limited.

Currency risk defines the risk arising from changes in the market value of investments or liabilities dependent on currency exchange rates and which will react negatively due to changes in currency exchange rates. MünchenerHyp's transactions outside Germany are hedged against currency risks to the greatest extent possible and only margins involved in payment of interest are not hedged.

Stock risks play a minor role for MünchenerHyp as our total investments in this asset class consist of investments in enterprises within the Cooperative Financial Network. The Bank additionally invested in a mixed fund (a special fund) in 2017. This fund can also invest in equities. The calculation of the risk figure is thus transferred to the company managing the investment fund. The results will be examined for their plausibility and then integrated into our own system.

Market price risks are managed by determining the present value of all of MünchenerHyp's transactions on a daily basis. The Bank uses the "Summit" IT programme for these calculations. The backbone of our interest rate risk management is the "bpV-vector", which is calculated on a daily basis. This figure is determined by the change in the present value incurred per range of maturities when the mid-swap curve is shifted by one basis point. Furthermore, sensitivities regarding the currency exchange rates, rotations of the interest rate curve, as well as changes in the basis spreads and volatility are also determined.

MünchenerHyp uses the value-at-risk (VaR) figure to identify and limit market risks. Linear as well as non-linear risks are taken into consideration using a historical simulation when calculating VaR. In addition, different stress scenarios are used here to measure the effect of extreme shifts in risk factors and the effects of other risk categories.

The current daily stress scenarios (others are conducted less frequently) are:

- Legal supervisory requirements: The interest rate curve is completely parallel shifted up and down by 200 base points for every separate currency. The worst result of the two shifts is used for calculation purposes.
- Parallel shifts: The current interest rate curve is completely shifted up and down by 50 base points across all currencies. The worst result of the two shifts is used for calculation purposes.
- Steepening/flattening: The interest rate curve is rotated in both directions pursuant to Guideline BCBS 368.
- Historical simulations:
  - September 11, 2001 terror attack in New York: Changes seen in market prices between September 10, 2001 and September 24, 2001 – the immediate market reaction to the attack – are played out using current levels.
  - The 2008 crisis in the financial markets: Changes in interest rates seen between September 12, 2008 (last banking day before the collapse of Lehman Brothers) and October 10, 2008 are played out using current levels.
  - Euro-crisis: the scenario replicates changes in interest rates that took place during the Euro-crisis between 21 May 2012 and 4 June 2012. Interest rates fell sharply during this period.

The Value at Risk (VaR) of the banking book (interest, currencies and volatilities) at a confidence level of 99 percent at a ten-day holding period in 2017 amounted to a maximum of € 21 million. The average figure was about € 14 million.

Although MünchenerHyp is a trading book institution (only for futures), as in the past the Bank did not enter into any futures deals in 2017.

MünchenerHyp manages its credit spread risks by calculating the present value of its asset-side capital market transactions on a daily basis to determine credit spread risks. The Bank uses the Summit valuation system to calculate the credit spread VaR, credit spread sensitivities and various credit spread stress scenarios.

MünchenerHyp uses the VaR figure to identify and limit credit spread risks. The VaR figure is calculated based on historical simulation.

The current (daily) credit spread stress scenarios are:

- Parallel shifts: All credit spreads are shifted up and down by 100 base points. The worst result of the two shifts is used for calculation purposes.
- Historical simulation of the collapse of the investment bank Lehman Brothers: the scenario assumes an immediate change

in spreads based on the changes that occurred one working day before the collapse of the investment bank until four weeks after this date.

- Flight into government bonds: The scenario simulates a significantly visible aversion to risk that was previously seen in the markets. Spreads for riskier classes of paper widen while spreads for safer government bonds narrow.
- Euro-crisis: The scenario replicates the development of spreads during the Euro-crisis that took place from October 1, 2010 and November 8, 2011. During this period the spreads of less creditworthy government bonds, in particular, rose sharply.

The credit spread VaR for the entire portfolio using a 99.9 percent level of confidence and holding period of one year stood at a maximum of € 101 million in 2017, while the average figure was about € 92 million.

LIQUIDITY RISKS

Liquidity risks consist of the following risks:

- Inability to fulfil payment obligations when they come due (liquidity risk in the narrow sense),
- inability to procure sufficient liquidity when needed at anticipated conditions (refinancing risk),
- inability to terminate, extend or close out a transaction, or only be able to do so at a loss, due to insufficient market depth or market turbulence (market liquidity risk).

MünchenerHyp differentiates between short-term assurance of solvency and mid-term structural liquidity planning.

SHORT-TERM ASSURANCE OF SOLVENCY

The purpose of short-term assurance of solvency is to ensure that the Bank is fully able to meet its required payment obligations (payment willingness) as agreed on a daily basis, even during stress situations. All of the currently applicable legal supervisory requirements as defined by the terms of MaRisk and CRD IV, regarding liquidity reserves that must be held by banks, are being fully implemented.

In doing so, MünchenerHyp has categorised itself as a capital market oriented institution per the terms of MaRisk, and therefore also fulfils requirements pursuant to BTR 3.2.

MaRisk distinguishes between five different scenarios, which were implemented accordingly:

1) Base Case: corresponds to the bank's control case.
2) Bank stress: the reputation of the institution deteriorates, for example due to high balance sheet losses.
3) Market stress: Short-lived event that affects a segment of the financial markets. Examples of this are the September 11, 2001 terror attack, or the financial market/sovereign debt crisis.
4) Combined stress: Simultaneous occurrence of bank and market
5) Combined stress without counter-measures: Scenario 5 assumes that it is impossible to obtain any liquidity.

MaRisk demands that an institution must be able to meet its liquidity requirements arising from scenarios 1-4 for at least 30 days. Scenario 5 represents the worst case situation for internal management purposes.

Varying model assumptions for all important cash flows were derived for each scenario; for example utilisation of our liquidity lines or guarantees (Aval), utilisation of previously made lending commitments, or the development of collateral. Beyond this, all securities were divided into different liquidity categories. Based on this, we determined the volume that would be sold, over which time period, or could be used for a repo transaction, to generate additional liquidity in each individual scenario. Legal restrictions, like the Pfandbrief Act's 180 day rule, were always observed in all cases. The result is a day-certain presentation of the available liquidity for a three year horizon in three currencies: euro, US dollar, and Swiss franc. Positions in other currencies are negligible. Limitation in the stress scenarios takes place using various horizons as early-warning indicators in each scenario.

In addition, the Liquidity Coverage Ratio (LCR), including a forecast, pursuant to CRD IV is calculated at least once a week for all currencies. Furthermore, it is also separately presented on a regular basis for all relevant currencies (currently, the euro and the Swiss franc). The ratio was notably higher than 100 percent at all times in 2017.

MID-TERM STRUCTURAL LIQUIDITY PLANNING

The purpose of structural liquidity planning is to ensure mid-term liquidity. The legal basis consists of the MaRisk BTR 3 and CRD IV for the Net Stable Funding Ratio (NSFR).

Mid-term liquidity management in accordance to the terms of MaRisk is based on short-term liquidity management pursuant to the terms of MaRisk, which means that both procedures use the same scenario definitions and modelling assumptions. However, due to the longer observation period, additional modelling assumptions are also taken into account which are not essential for managing short-term liquidity – for example, new business plans or current expenses such as salaries and taxes.

Mid-term liquidity planning involves the following key liquidity figures as components for determining results across all due dates:

- accumulated total cash flow requirements,
- available uncovered and covered potential funding including planned new business and prolongations in line with the surplus cover requirements set by the rating agency Moody's,
- additional detailed data for planning and control activities.

The limitation of liquidity risks takes place using the structured liquidity forecast and the stress scenarios based on the available liquidity within a year.

In addition, pursuant to CRD IV, the NSFR is calculated on a quarterly basis for all currencies. Furthermore, it is presented separately for all relevant currencies (currently the euro and the Swiss franc). As the supervisory authority has not yet issued any binding minimum amounts for complying with NSFR requirements, and the values are currently stable at just over 100 percent, this key figure is not being actively managed at this time.

In order to reduce refinancing risks, MünchenerHyp strives to refinance loans with matching maturities and continuously checks if its relevant refinancing sources (primarily those within the Cooperative Financial Network) still remain available. In order to limit market liquidity risks in its lending business with public-sector borrowers and banks, MünchenerHyp primarily acquires securities that are acceptable as collateral by the ECB, and which can be used for open market transactions at any time.

MünchenerHyp does not have any less-liquid bonds, like Mortgage Backed Securities (MBS) or similar securities, in its portfolio.

INVESTMENT RISK

Investment risk is understood to mean the danger of financial loss due to a decline in the value of a holding to less than its book value. This refers to long-term investments MünchenerHyp has made in companies within the Cooperative Financial Network due to strategic reasons.

OPERATIONAL RISKS

Operational risks refer to possible losses caused by personal misconduct, weaknesses in process or project management, technical failure or negative outside influences. Personal misconduct also includes unlawful actions, improper sales practices, unauthorised actions and transaction errors.

We minimise our operational risks by qualifying our employees, using transparent processes, automating standard procedures, and by having fixed working instructions in writing, comprehensive functional testing of the IT-systems, as well as appropriate emergency plans and preventive measures. Insurable risks are covered by insurance to the normal extent required by banks.

Within the framework of a risk analysis, the materiality in accordance with MaRisk standards of all of the services that MünchenerHyp outsources related to banking transactions, financial services or other services that are typical for an institution like MünchenerHyp, is examined. All of the outsourced services that are defined as being material are monitored pursuant to MaRisk requirements and are integrated within the risk management process.

ABILITY TO BEAR RISKS

The professional concepts and models used to calculate the Bank's ability to bear risks are continuously further developed in accordance with legal supervisory requirements. MünchenerHyp calculates its ability to bear risks based on the so-called Going-Concern, as well as the Insolvency Case. However, the so-called Going-Concern scenario is the relevant method used for control purposes, which determines if the bank would still have an adequate equity capital ratio exceeding legally required levels after the occurrence of risks contained in all of the risk categories.

The scenario deducts market risks, counterparty risks, operational risks, spread and migration risks, investment risks, property risks, as well as modelling risks containing other non-explicitly defined risks. Risks on cover potential for risks are accounted for on a conservative basis and without taking diversification effects between the risk categories into consideration.

The Bank's ability to bear risks was given at all times during the year under review.

USE OF FINANCE INSTRUMENTS FOR HEDGING PURPOSES

We engage in hedging activities – interest rate and currency derivatives – in order to further reduce our risks and to hedge our business activities. Credit derivatives are not employed. We use asset swaps as micro-hedges at the level of individual transactions. Structured fundamental transactions such as callable securities are hedged accordingly with structured asset swaps. Matching currency funding is primarily sought to hedge foreign exchange risks arising from transactions involving foreign currencies; the remaining deals are hedged using (interest rate) currency swaps. The main hedging instruments we use at the portfolio level are interest rate swaps and swaptions. In addition to linear instruments, Bermudan options on interest swaps (swaptions) and interest options (caps and floors) are also used as hedges for embedded legal termination rights or arrangements to limit interest rates.

ACCOUNTING-BASED INTERNAL CONTROL AND RISK MANAGEMENT PROCEDURES

The accounting-based internal control system is documented in organisational guidelines, descriptions of work processes, financial reporting handbooks, and operating instructions. It contains organisational security measures, as well as ongoing automatic measures and controls that are integrated in the work processes. These are, in particular, separation of functions, the double-check principle, access limitations, payment guidelines, new product and new structure process and balance confirmations. Process-independent measures are, above all, carried out by the internal audit department.

The risk management methods described in the risk report provide continuous qualitative and quantitative statements regarding MünchenerHyp's economic situation, including, for example, the development of performance. This evaluation involves aspects of all risk categories.

A close coordination process exists between the risk controlling and accounting departments at MünchenerHyp. This coordination process is supervised by the entire Board of Management.

The results from the risk management system form the basis for the multi-year planning calculations, year-end projections, and agreement procedures for approving the key figures generated by the Bank's accounting process.

CORPORATE PLANNING

MünchenerHyp continues to pursue a growth strategy focused on its residential and commercial property financing activities built on a solid refinancing foundation primarily based on Pfandbriefe and other bonds. The Bank's overarching strategic goal will continue to be the further strengthening of its earning power and thus its ability to retain profits. The Bank's strategic planning is focused on measures to improve net interest income and net commission income, increase cost efficiency, and keep risks under control.

The annual adjustment of our business and risk strategy required by the MaRisk defines the formal planning framework for this. Our integrated annual planning process plays a key role in the planning and management of our operations. This process synchronises our sales goals, management of the decentral and central components of our administrative expenses – including our project portfolio – with the outlook for the profit and loss account as it develops over the course of the year. All of the income and expense elements, as well as our ability to bear risks, are continually monitored, or additionally planned on a rolling basis, thereby allowing the Bank to respond appropriately and in a timely manner to fluctuations in earnings or costs.

Planning also includes issues regarding appropriate levels of equity capital – especially in view of meeting supervisory requirements.

OUTLOOK – OPPORTUNITIES AND RISKS

ECONOMIC DEVELOPMENT AND FINANCIAL MARKETS

The outlook for the global economy is clearly optimistic. Forecasts anticipate that the broad-based upswing will continue with the IMF expecting global GDP to grow by 3.9 percent per year in 2018 and in 2019.

The upswing is mainly driven by strong growth in advanced economies where production is predicted to grow further. The ECB foresees the euro area growing by 2.3 percent as it did in the year under review. Growth is only anticipated to slow slightly to 2.0 percent in 2019 against a background of a possible diminishing monetary support.

The strong and wide growth of the German economy will continue in 2018. In line with this outlook the German Federal Government's latest Annual Economic Report predicts that the country's gross domestic product will expand by 2.4 percent. This growth is still supported by the domestic economy, especially by private consumer spending. A notable increase is also foreseen for investments in construction due primarily to unwavering attractive financing conditions. However, the construction industry is already operating at the upper limits of its capacities. This is increasingly leading to bottlenecks and higher prices. The good global economy is also benefiting the export sector, which will also contribute to the growing economy. It is estimated that the rate of inflation will remain at the level recorded in 2017 and therefore still to be moderate. The labour market will continue to develop favourably in light of the good economy as employment figures continue to increase and jobless numbers decrease. The Kiel Institute for the World Economy (IfW) estimates that the average unemployment figure for the year will be 5.4 percent.

In the interim, the normalisation of monetary policies is viewed as the primary risk facing the German and the global economy, and could lead to uncertainty in the capital markets. At the beginning of 2018 economic experts also mentioned political risks, such as the outcome of the Brexit negotiations, or protectionist tendencies, especially in the USA, as possible factors that could burden the global economy, although they were not as strongly weighted as they were in the previous year.

The central banks' monetary policies will still vary in 2018 as, at least, two interest rate hikes are expected in the USA where the Fed is likely to continue shrinking its balance sheet. In contrast, the ECB and the Bank of Japan are expected to leave their key interest rates at their respective low levels and continue buying bonds on the market. At the beginning of 2018 the ECB already announced that it was reducing its monthly volume of purchases from € 60 billion to € 30 billion. This is interpreted to mean that the ECB could raise interest rates for the first time in 2019 – if the rate of inflation moves toward 2 percent. In this environment we anticipate slightly rising interest rates. Yields on 10-year bunds could rise from the 0.43 percent noted at the start of 2018 to a level around 1.0 percent within the remainder of the year.

The euro strengthened in the currency markets in past months. In the interim the euro has largely achieved its purchasing power parity level of USD 1.25 to the US dollar and to a great extent has ended its prevailing under-valuation. We do not expect to see a further rise in the near future. The value of the euro also gained vis-à-vis the Swiss franc and in the interim almost reached CHF 1.20, a level that the Swiss National Bank previously defined as its minimum exchange rate.

The ECB's continuing purchases of bonds within the framework of CBPP 3 should also result in favourable financing conditions for Pfandbrief issuers in 2018. Experts expect that issuing activities will be concentrated in the first months of 2018 as spreads could widen again as the ECB reduces its volume of newly purchased bonds. The total volume of new benchmark covered bond issues is expected to decline further to about € 100 billion. This decrease is mainly due to issuers' notably lower refinancing requirements compared to 2017. All in all, Pfandbriefe and other covered bonds will, however, remain important refinancing instruments. This especially applies to special institutions like MünchenerHyp.

PROPERTY AND PROPERTY FINANCING MARKETS

Property markets will benefit from the favourable economic outlook for another year and expand again. This means that the markets where MünchenerHyp is active will be affected as follows:

The German housing market will again be characterised by excess demand in 2018. This will apply equally to the user market – in other words, demand for owner-occupied housing and rental housing – and institutional and private property investor markets. Demand will continue to be driven by both low interest rates as well as demographic developments. The increase in the number of single-person households, in particular, will lead to a further increase in the number of households, as will population numbers which are growing again. In addition, demand on the part of owner-occupiers and capital investors will remain at a high level because the tight supply of properties noted in recent years was unable to satisfy existing demand.

In view of the high capacity utilisation rates noted for the construction industry, and the declining number of building permits recorded during the year under review, the supply of housing cannot be expected to increase noticeably in the future. Furthermore, the vacancy rates posted over many years in cities is substantially below the required fluctuation reserve. As a result, the accelerated pace of price increases will also continue in 2018.

The outlook for the German commercial property market is also favourable. Heavy demand for commercial properties, and especially office properties, will continue to be shown by national and international investors. The number and volume of transactions will be generally determined by the limited supply of available properties, especially in the seven biggest markets. Thus, experts anticipate the volume of transactions to stabilise at the high level seen in 2017.

Market conditions in the user market in 2018 will be driven by unbroken high demand for office space, which will remain in very tight supply – especially in the preferred office locations. Newly built office space will also remain scarce in view of the high rate of pre-completion leases signed. This situation is likely to lead to a renewed increase in rents in the seven biggest markets. Coupled with great pressure on institutional investors, which will lead anew to slightly declining yields, prices paid for commercial properties will initially rise further. It is felt that only a notable increase in interest rates in the capital market can halt the decline in initial yields and stop prices from rising even further.

Further developments in the UK property market will continue to be influenced by the potential economic effects of Brexit. However, as forecasts for 2018 only anticipate a slight weakening in economic growth, international investors are again showing interest, and especially in the London property market. This indicates that Great Britain is likely to hold its top-ranked status in the European investment market in 2018. However, as the office user market is in a very advanced phase of growth, is appears likely that the trend towards more stable rents that surfaced in the second quarter of 2017 will continue. Development of the residential property market depends to some extent on the number of companies that will move their head offices, and the attendant jobs, to other European cities because of Brexit. This is particularly true for the greater London area where prices for houses are expected to rise at a slower pace than in the rest of Great Britain. This development is likely to be far more visible in the rental housing market. While rents are forecast to decline in London, they are predicted to rise by 2 percent in Great Britain in 2018.

The economic upswing is making French property even more attractive for international investors. In addition, favourable fiscal conditions are also contributing to France's appeal. Thus, based on the assumption that there will be a sufficient supply of properties, the volume of investments is expected to increase. In view of the unchanged low level of interest rates, the French property market is predicted to continue on its upward trajectory among users and investors. It is also foreseen that the market will be marked by a further rise in prices paid, and higher rents.

The Dutch investment market is also experiencing overall favourable conditions in 2018. Demand for property will increase again, especially among foreign investors. The market is expected to grow in view of limited supply and investors' willingness to make riskier investments beyond prime locations. Investors will remain focused on office properties as high demand for office space in the user market promises higher property valuations due to rising rents. The tight availability of properties in the institutional housing market is likely to continue and lead to declining residential property yields in portfolios. At the same time, a noticeable revival of new construction activity is expected and will benefit the development of projects and buildings under construction.

The segments within the Swiss housing market will increasingly develop differently. The decline in rents will continue in the rental housing segment as the share of new rental housing as a percentage of total new housing under construction is expected to remain high. In contrast, prices paid for private homes and condominiums will continue to rise further. This development is supported, on the one hand, by the unchanged low level of interest rates and, on the other, by notable excess demand.

Although forecasts for the American commercial property market are mixed, they do anticipate that the phase of growth will slow. It is expected that the vacancy rate in the office properties market will rise slightly despite declining levels of new construction. Rents are also expected to continue growing at a slower pace in certain regions. This development may lead to a renewed reduction in the volume of investments made in commercial properties. The housing market is experiencing brisk new construction of multifamily houses, thereby offering numerous purchase options to the investment market. In contrast, the pace of rental increases is expected to weaken further in the rental housing market.

DEVELOPMENT OF BUSINESS AT MÜNCHENER HYPOTHEKENBANK

Our new business planning for 2018 is based on overall conditions that do not significantly differ from those noted in the year under review. High demand for property financing is expected to continue in view of the favourable economic conditions and low interest rates. Our planning anticipates a moderate increase in interest rates that will still leave them very attractive. Competition will intensify as the number of finance providers will increase thereby putting further pressure on margins. This situation applies to both private residential and commercial property financing. Against this background we plan to slightly expand our new business compared to figures posted for the year under review. This is because the prevailing competitive conditions and the level reached in the interim do not permit a dynamic increase.

The emphasis of our new business planning remains on financing residential property in Germany. The banks within the Cooperative Financial Network are our key partners in this area of business as they have pronounced sales power and close customer relationships. These attributes have enabled them to steadily expand their share of market over the past years. We anticipate that they will also grow stronger than the market in the residential property financing sector in 2018.

In January 2018 we introduced a new loan product to expand our combined market position: the MünchenerHyp Family Loan. The product offers a sustainable financing solution to families with children and is an innovative offer that favourably distinguishes our Bank from other providers of financial services. In addition, we take a major step toward digitalising the entire lending process by upgrading the Bank's system for disbursements and other portfolio processes. The objective of our efforts in this area is to strengthen perception of our partner banks as modern and very capable property financers thereby expanding the brokered business.

We plan to moderately expand our new business in collaboration with independent providers of financial services. The negative interest rates in Switzerland will lead to a further intensification of competition in the private property financing business. Working together with PostFinance we therefore anticipate that the volume of new business will be at the previous year's level.

We also expect that our new commercial property financing business will be at the 2017 level. Germany will be the focus of our new business activities. In addition we want to step up our business with foreign investors and accompany their investment activities in Germany with attractive financing offers.

Plans for our international business foresee moderate growth in all of the markets served by the Bank. In this context we will accompany domestic customers outside of Germany as well as foreign clients in their respective target markets. Our activities in the USA will continue to be limited to participating in other banks US financing arrangements.

We anticipate that syndication markets will see lively growth in 2018 as there is a clear trend towards ever larger financing deals. Only few banks, however, are willing to completely carry larger lending volumes of € 100 million or more on their balance sheet. For this reason, we expect that the number of club deals will expand in 2018 along with growing volumes in the secondary market. This is why we are planning to intensify our syndication business. On the one hand we will significantly participate in third-party financing deals, and on the other we will again pass on bigger volumes of loans we generated to other banks. The objective of these efforts is to attain a good diversification of risk. In achieving this we will also expand our successful syndication programme with the Cooperative Financial Network.

Our lending business with the public-sector and banks will remain unchanged and primarily serve to control liquidity and cover pools. For this reason, we will strive to further reduce our capital market business portfolio in 2018, which is anticipated to be smaller than in the previous years.

Our refinancing needs in 2018 are planned to be between € 6 billion and € 7 billion, of which we expect to obtain € 5.5 billion from the capital market, with the remaining volume sourced via the money market. As in the previous year, we anticipate that we will float two large volume issues and have additional potential to tap existing bonds. MünchenerHyp will continue to need Swiss francs due to its collaboration with Swiss PostFinance. Beyond these activities we will take advantage of attractive opportunities offered by other foreign currencies to further diversify our investor base.

We developed a deposit product for private customers in 2017 to broaden our refinancing mix. This product meets the requirements of the Cooperative Financial Network and will be sold by cooperative partner banks. The product's procedures and marketability were successfully tested during pilot phases. As a result, we plan to offer this deposit product on a permanent basis in the future.

We will also expand our sustainability activities in 2018. As part of these efforts we are pursuing the goal of successfully launching the MünchenerHyp Family Loan into the market, thereby expanding our portfolio of sustainable financing. Furthermore, we are working on obtaining the required volume of mortgages eligible to serve as cover to enable us to issue another Sustainable Pfandbrief.

We are striving to achieve a moderate increase in net interest income from business operations in 2018. The stable development in our core markets continues to offer us opportunities to once again expand our new business and thus our portfolio of mortgage loans.

This will continue to have an increasingly favourable impact on the Bank's performance. As a result, we anticipate that our earnings will improve again in 2018.

We anticipate that our administrative expenses will increase anew in 2018. Nevertheless, we currently expect that our cost-income ratio will decline slightly.

Based on the currently available information, we expect that provisions for lending risks will develop stably.

In view of the anticipated favourable market conditions, we are confident that we will achieve our targets for the 2018 business year and further expand our market position. We expect that our net income will exceed the previous year's level.

DISCLAIMER REGARDING FORWARD-LOOKING STATEMENTS

This Annual Report contains statements concerning future expectations and forecasts. These forward-looking statements, especially those pertaining to the development of MünchenerHyp's business and income, are based on our planned assumptions and estimates and are subject to risks and uncertainties. There are a number of factors that could affect our business and which are mainly beyond our sphere of influence. These include, above all, economic developments, the state and further development of the financial and capital markets in general and our refinancing conditions in particular, as well as unexpected defaults on the part of our borrowers. Therefore, the actual results and developments may vary from the assumptions that have been made today. For this reason, they are only valid at the time this report was prepared.