EMBARGO: 7 June 2019, 10:00 CEST

Annual General Meeting 2019

7 June 2019

Andreas Arndt
CEO

Deutsche Pfandbriefbank AG

Manuscript – please check against delivery

Deutsche Pfandbriefbank AG
Communications
Freisinger Strasse 5
85716 Unterschleissheim, Germany

1. INTRODUCTION

Good morning dear shareholders,
Ladies and Gentlemen,

My fellow Board members, Thomas Köntgen, Andreas Schenk and Marcus Schulte, and I are very pleased to welcome you to our 2019 Annual General Meeting. I am delighted that you can participate in today's AGM, being the most important decision-making body of a public limited company.

I would like to open my comments by outlining three core statements, which I will discuss in more detail later (CHART #1).

1. pbb concluded the 2018 financial year with good results, in what was once again a challenging environment. We can therefore distribute an attractive dividend to our shareholders.

2. While we do not expect a significant market correction in 2019, the potential for instability is increasing from our point of view. We will therefore focus to an even greater extent on quality.

3. The dynamics of our environment and our aspiration to achieve sustainable development require innovation and investment. We will therefore continue to invest in the expansion of the US business and in digitalisation in the course of this year. We will finance these investments by making corresponding savings in other areas.

2. Financial year 2018

I will start with a summary of the good financial year 2018; and in this context I shall initially touch on the operative business, followed by the financial result and then the dividend proposal.

2.1 Operative business

2.1.1 Markets, new business, and portfolio

In 2018, **real estate markets** developed solidly once again: transaction volumes remained on a high level, prices and rents were stable, and vacancies stayed low.

Competition amongst real estate lenders also failed to abate, making it more difficult to originate new business that combined a conservative risk profile with appropriate profitability. Margins on new business generally remained under pressure, increasingly impeding the efforts of commercial property finance providers to enforce contractual covenants.

pbb responded to this situation by **selecting its new business** even more carefully, and by clearly stipulating that the Bank's high risk standards are to be adhered to – in cases of doubt, to the detriment of the new business volume. In 2018, pbb once again fared well with this strategy (CHART #2).

- The Bank generated total new business of **€10.5 billion** in 2018 (2017: €11.6 billion, including extensions of more than one year). We are therefore exactly in the middle of the range we had set ourselves.

  New business originated (including extensions of more than one year) included approx. €9.5 billion in **Commercial Real Estate Finance** (2017: €10.7 billion). We were able to largely preserve our gross margin on new business, at approximately 155 basis points (2017: >155 bps).

- Thanks to strong new business and at the same time relatively low prepayments, pbb's **strategic portfolio** rose by more than € 1 billion to €33.2 billion.

  Within the scope of our portfolio management, we **underweighed individual markets**, because the value stability of markets varies along the cycle.

  - Due to the uncertainty arising from Brexit, we are now handling business in the **United Kingdom** even more selectively than before. The share of new business from the UK was therefore lower.

    On the other hand, new business in the **US** increased, where we have been active in selected sub-markets since the second half of 2016.

  - Of course, we do not only manage our portfolio with regard to regions, but also with regard to **property types**. In this context, we look at retail properties in particular very cautiously; we further reduced their share in 2018. However: not every retail property is the same. The dynamics can vary greatly – also on a regional basis – in the sub-segments, and we take this into account.

2.1.2 Funding

The lending business remained strong in 2018, as were the successful **funding activities** (CHART #3).

Lower funding needs led to a sharp decline in the **interest expense** of the funding operations. At the same time, we launched our new issues at lower rates than the maturing liabilities. Some specific figures:

- We raised **new long-term funding** of €5.2 billion, which is almost €1 billion less than the year before (2017: €6.1 billion).

  At €3.6 billion, **Pfandbrief issues** accounted for the lion's share thereof (2017: €3.8 billion). pbb therefore continues to rank among the leading Pfandbrief issuers.

  Added to this were **unsecured issues** and **additional tier 1 capital** (AT1 capital). We issued the latter in April 2018 in the form of a €300 million AT1 bond, in order to optimise the capital structure.

- Issuance spreads, in other words the **risk premia** on the 3-month Euribor reference interest rate, fell sharply year-on-year, to an average of 6 bp for Mortgage Pfandbriefe compared with 16 bp in 2017. We paid an average spread of 42 bp for unsecured funding in 2018. This also represents a marked decline from the previous year's levels of 75 bp.

2.2 Financial results

Ladies and Gentlemen, this concludes my coverage of pbb's operating activities in 2018. Let me now turn to pbb's consolidated financial results in accordance with IFRS.

pbb's most important earnings item is **net interest income** (CHART #4).

- The good new business development and the marked increase of our strategic portfolio, that I mentioned earlier led to an increase in interest-bearing assets. This positive development was supported by the relatively stable gross new business margin, as mentioned before. **Interest income** rose as a result.

- At the same time, **interest expense** fell, thanks to the lower funding requirements and new issues at more favourable terms – which I also referred to just now.

Overall, **net interest income** was up 11% in the year under review, to €450 million. We are very proud of this achievement.

N**et fee and commission income**, which amounted to €6 million in 2018, is mentioned for the sake of completeness; traditionally it does not contribute significantly to pbb's success.

Risk provisioning for the loan portfolio was largely stable, with net additions up by €4 million to €14 million. This means that we once again remained below our projections in this respect (CHART #5):

At €193 million, **general administrative expenses** were slightly lower in the 2018 financial year. Please note that – due to the first-time application of IFRS 9 – impairments now account for an individual item in the income statement (net income from write-downs and write-ups). We have restated the figure for 2017, in order to ensure comparability.

- **Personnel expenses** were down €5 million year-on-year, to €114 million in 2018. While employee numbers (in full-time equivalents) increased from 744 to 750, the previous year's figure was burdened by additions to provisions.

- At €79 million, **non-personnel expenses** were almost in line with the previous year's level (2017: €80 million), which, at first, does not sound very spectacular. What is important in this context is the fact that this item contains expenses for investments – which I will discuss later on.

The bottom line is that **profit before taxes** came to €215 million, up by around 5% year-on-year (2017: €204 million, CHART #6).

With **profit after taxes** of €179 million, pbb is nonetheless down slightly on the previous year's figure of €182 million. Despite having achieved higher net income, our profit after taxes is slightly lower year-on-year, due to positive deferred tax effects in 2017, which did not materialise again in 2018.

2.3 Dividend proposal

The basis for the dividend proposal is the **profit attributable to ordinary shareholders**, which was €167 million in 2018. The difference relative to profit after taxes of €179 million arises from the pro-rata coupon paid to holders of the AT1 bond which we issued in April 2018.

The Management Board and the Supervisory Board propose to you, our shareholders, a **dividend payment of €1.00 per share entitled to dividend payments**. This means that we would distribute €134.5 million – or 81% of the profit attributable to shareholders.

- The proposal comprises a **regular dividend** of 50% plus a **special dividend** of 25% – 75% in total – applicable to the upper end of the original guidance for consolidated profit before taxes (in accordance with IFRS) of €170 million.

- In addition, we want to distribute **income over and above** the original guidance (after remaining taxes) in full.

As in previous years, we want you – our shareholders – to participate significantly in pbb's success. With our dividend proposal, we would achieve a **dividend yield** of 11.4% for 2018, based on the Xetra year-end price for 2018. Applying the calculation on the basis of the annual average Xetra price for 2018 (volume-weighted daily closing prices) this let to 7.9%.

Ladies and Gentlemen, I hope you will agree with the following summary of my statements on the financial year 2018: pbb once again delivered a good result, in which you as shareholders participate via an attractive dividend.

3. TRENDS AND OUTLOOK

This brings me to my third topic, the outlook for the financial year 2019. I will differentiate here between the operative business and the key financial ratios. I shall additionally address the topic of regulation.

3.1 Trends in the operative business

Let me begin with the present trend in the operative business – lending and funding, in other words.

Sentiment on the real estate markets and the status of the real estate cycle have been described by many, and for quite some time now, as being stuck at “five to twelve”. Sticking with this scenario, the ECB recently set the clock back somewhat when it rejected interest rate increases in the short term.

Many economists meanwhile believe that we will not see any significant increases in interest rates until well into 2021. Furthermore, a growing number of observers see **Europe facing Japanese conditions** – in other words, moving towards a permanent low interest rate environment.

We at pbb do not expect a significant market correction in 2019, even though the **instability potential** is increasing from our point of view. Some sub-segments in particular are experiencing momentum peculiar to themselves (CHART #7).

- This applies for example to the UK, where **Brexit** is generating considerable uncertainty.
- **Retail properties** in certain sub-segments must also be seen critically.
- We consider the **office property markets** in the big cities as largely stable overall, with some special developments worth noting here too. For instance, co-working office providers are meanwhile playing a very important role in terms of demand. These spaces are generally passed on for considerably shorter rental terms within the scope of sub-lettings. This poses a problem, since such properties need to be rentable – and rented out – in calm and crisis conditions alike.

This means we will have to **focus to an even greater extent on the quality** of our new business.

- This applies on the one hand to the **real estate** to be financed, where the focus is on **value stability**.
- On the other hand, we focus on the quality of **investors** – who need to have the ability to **provide additional funds if required**, and whose ability has been tested across the cycle.
- Finally, we continue to place great importance on contractual arrangements, so-called covenants.

To **fund** our lending business, we want to benefit in 2019 from a new debt capital class available for use since the legal provisions were created in mid-2018. So-called **senior preferred bonds** range in the liability cascade between Pfandbriefe and senior non-preferred bonds; they therefore have a better structural rating and hence lower risk premiums, which allow us to borrow at more favourable rates than for senior non-preferred bond issues.

3.2 Key financial indicators

3.2.1 Results for the first quarter of 2019

Our start into a new financial year has once again been successful (CHART #8):

- The **volume of new business** in Commercial Real Estate Finance climbed to €1.9 billion during the first quarter, which is 12% more than in the same quarter of the previous year (1Q18: €1.7 billion, both including extensions of more than one year).

  However, average **gross new business margins** fell during the same period to 130 basis points, compared with approximately 155 bp for the full year 2018. This change resulted from the high share of transactions with a very conservative risk profile – and hence lower margins.

  I had already mentioned the **composition of the new business**. The share of business in Germany and France – as well as in office and residential properties – was relatively high in the first quarter. New business levels in the UK, in Central and Eastern Europe, and in logistics properties, on the other hand, were all lower. Furthermore, the average loan-to-value ratio of 58% for new commitments was below the 2018 level, and pbb was involved in fewer development financings.

- **Profit before taxes** of €48 million (IFRS, consolidated, unaudited) in the first quarter was unchanged from the same period of the previous year.

  Net interest income grew by more than 8%, to €116 million (1Q18: €107 million). This was due to higher interest income from the continued growth in the strategic portfolio, and to funding costs remaining low.

  At the same time, we maintained **general administrative expenses** at a low level of €46 million (1Q18: €44 million). **Risk provisioning** amounted to a net addition of €1 million (1Q18: net reversal of €4 million).

  Expenses for the bank levy of €20 million, which are recognised for the full year in the first quarter, burdened results (1Q18: €20 million, each taking into account 15% cash collateral pledged).

3.2.2 Outlook/guidance

However, growth is not unlimited, and we continue to pursue our conservative risk policy in Commercial Real Estate Finance – vis-a-vis the market and the competitive environment.

- We aim to generate **new business** in the volume of €8.5-9.5 billion (including extensions of more than one year) in Commercial Real Estate Finance in 2019. Taking into account the volume of €9.5 billion achieved in 2018, our target is still ambitious when one considers the very mature real estate cycle. We also anticipate slightly lower **gross margins on new business**.

- We will aim to generate **profit before taxes** in the range of €170 million to €190 million for the year as a whole.

3.3 Regulation and capital

A further increase in the complexity of regulatory topics belongs to the reliable invariables of our banking business. I would like to conclude this part of my report with a few statements about this topic.

In essence, we will continue with the topics seen in the last few years: TRIM, EBA Guidelines and Basel IV. The effective direction of these regulatory initiatives is obvious: they have already resulted, and will continue to result, in an **increase in risk-weighted assets** and thus in a higher level of capital requirements in the banking business.

As you know, pbb is **well-capitalised**. Our CET 1 capital ratio was 18.5% at the end of 2018. We deliberately retain a buffer here, not only to meet the regulatory requirements but also to counter any potential cyclical modulations or to be prepared for strategic requirements.

In summarising the topic of trend and guidance, I would like to say this: we are adhering to our risk-conservative approach due to the challenging market and competitive environment in commercial real estate financing, and yet we anticipate generating another good result for **2019**. We have already made a start, with an excellent first quarter that met with our expectations.

4. STRATEGIC INITIATIVES – INNOVATION AND INVESTMENTS

I now want to talk about the last major point of my report, namely our strategic initiatives. Our aspiration to achieve sustainable development - at pbb on the one hand, as well as with regard to the dynamics of our environment on the other – **requires** continued **innovation**. We are consistently developing pbb, concentrating at present on two significant initiatives: further expanding our US business, and digitalisation. We will fund the additional investment expense through savings in other areas.

I will now talk about these two initiatives (CHART #9) and then explain how we will finance these investments internally.

4.1 Initiatives

4.1.1 US business

We have built up **personnel resources**, so as to further expand the real estate finance business in the United States. We opened our office in New York in summer 2018, commencing operations with a small team. We are currently expanding this team, and are now approaching the target size. Our colleagues in New York are supported by additional dedicated employees in Unterschleissheim and London – especially in the area of risk management.

We are now in a position to **expand our activities** – **of course in a moderate and cautious manner**.

- In our East Coast target markets of New York, Boston and Washington DC, we now aim to do business on the **primary market**, too, instead of solely focusing on syndications in the secondary market.

- We will also extend our reach, offering our services to new **sub-markets** in Chicago, Los Angeles, San Francisco and Seattle, where we will exclusively engage in the syndication business at first – in line with our East Coast approach so far. We have already carried out the first syndications in Los Angeles and San Francisco.

4.1.2 Digitalisation

Besides expanding our business in the US, we are also focusing on the digitalisation of pbb as part of the strategic initiatives. We are doing so because of the **opportunities** we see for improving ourselves further – and it goes without saying that we do not want to miss out on any important developments.

All in all, the **commercial real estate financing sector anticipates significant changes** through digitalisation. The key changes in our existing business will take place in customer interfaces and processes in general, and in the credit process in particular. The importance of platform solutions is also expected to grow. A change in working methods on the market is also evident from this.

We have determined our strategic directions: we want to improve the interfaces to our clients, increase the efficiency of our internal processes, and tap new sources of income.

To some extent, our digitalisation approach is agile, since we have already **implemented first initiatives**, whilst simultaneously continuing to work on the comprehensive target image of a digital pbb.

- We have launched the first stage of a **client portal**, thus simplifying the exchange of data with our real estate developer client group. We are determined to considerably expand this portal in the course of this year, to include other functions in real estate financing.

- Our **CAPVERIANT** platform for municipal financing was launched in May 2018. By bringing together credit supply and demand, we want to improve the market and price efficiency of municipal financing on a pan-European level, as well as simplifying processes. CAPVERIANT will also offer supplementary services for the public sector, as well as for institutional investors.

  We also launched CAPVERIANT in France in April.

4.2 Focusing as a means to internally finance investments

Innovations require investment. We have set out to offset the investments with savings on the costs side, to the extent possible. We are therefore **financing ourselves internally** in this respect.

To this effect, we are **relocating tasks** from satellite locations to Unterschleissheim and Garching respectively. Secondly, we are adapting our **Public Investment Finance business** to the market conditions. More than 90 per cent of the personnel measures associated with these changes have already been implemented or initiated. It is just as important to us to protect the interests of the colleagues affected as well as those of the Bank and its shareholders.

Overall, **employee numbers in the Bank remain largely constant** – jobs or functions that are reduced are being created at other locations. In this context, it is important to us that colleagues are able to change location and/or function – allowing them to remain with pbb.

With the expansion of our US business, we are opening up additional business opportunities while adhering to our conservative risk strategy. pbb's digitalisation strategy is equipping pbb to face a digital future. We are compensating for the costs incurred through savings.

5. SUMMARY

Ladies and Gentlemen.

Allow me to now summarise my comments (CHART #10):

- pbb achieved a **good result** for 2018, which is a sign of our **operating strength**.

  - We increased our most important source of income, the aggregate of **net interest income and net fee and commission income**, by 10%. Furthermore, our **risk costs** for the lending business and **general administrative expenses** were better than we had planned.

  - Thanks to the good performance, we want to pay you, our shareholders, an **attractive dividend of €1 per share**. Since its initial public offering, pbb has established itself as a 'dividend share'.

- We are, and will remain, **cautious and risk-conservative**, so that we can cushion the risks of cyclicality. This includes preserving a strong capital base and stable funding, as well as a stable rating.

  - We will continue to act **prudently with regard to new business**, especially in 2019, since we regard the real estate cycle as being very mature.

  - This approach should be reflected in our results. With profit before taxes targeted between €170 million and €190 million (consolidated figures in accordance with IFRS), we are once again aiming to post **good results**.

- We are **investing in pbb's future**, financing these investments with our focused approach.

  - We are expanding our business in some **US** sub-markets.

  - **Digitalisation** is both an opportunity and a challenge – to improve the interfaces to our clients, enhance the efficiency of our processes, and generate additional income.

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Thank you very much for your attention.