Press Release

Pre-tax profit for the third quarter of 2016 rises to €159 million, boosted by extraordinary gain related to Heta

- Adjusted pre-tax profit stable, at €42 million
- New business up slightly, to €2 billion (Q2 2016: €1.8 billion)
- Due to Heta gain pbb now anticipates higher pre-tax profit for 2016, between €280 million and €290 million – operating profit expected at around €170 million
- Special dividend from Heta gain contemplated
- pbb aims for 2017 pre-tax profit between €150 million and €170 million

Munich, 11 November 2016 – pbb Deutsche Pfandbriefbank (pbb) posted €159 million in pre-tax profit for the third quarter of 2016 (Q3 2015: €53 million; unaudited consolidated figures in accordance with IFRS). Third-quarter results include €132 million in income from previously impaired receivables from Heta Asset Resolution AG (Heta), against which pbb has recognised €15 million in provisions and expenses, as a precautionary measure. pbb showed a stable operating performance during the third quarter: adjusted pre-tax profit amounted to €42 million (unchanged from Q2 2016), the aggregate of net interest income and net commission income rose to €99 million (Q2 2016: €94 million), and new business (including extensions of more than one year) increased slightly, to €2 billion (Q2 2016: €1.8 billion).

At €246 million, pre-tax profit for the first nine months of the year clearly exceeded the figure for the same period of the previous year (9m 2015: €165 million), largely driven by income on Heta receivables. On this basis, pbb has raised its **guidance for the 2016 financial year**, with pre-tax profit now expected between €280 million and €290 million. Excluding the net extraordinary effects of €117 million, pbb expects operating profit before taxes to the tune of €170 million, in line with original expectations. The Management Board anticipates a higher tax burden for the full year 2016 than in first three quarters, due to valuation losses on deferred tax assets from losses carried forward, as well as additional tax payments due following a tax audit. This should translate into a notional Group tax rate of around 35%.

Along with the third-quarter results, pbb also discussed **dividends for 2016**. The Management Board and Supervisory Board are considering a proposal to the Annual General Meeting – subject to compliance with all legal and regulatory requirements or developments – to distribute for the financial year 2016 a special dividend from the Heta gain in addition to the distribution according to its communicated dividend policy. From pbb's point of view, this does not imply any fundamental change to its communicated dividend policy, which the Management Board will review as soon as the impact of a changed regulatory environment can be perceived. Such regulatory changes predominantly concern the models used by banks to determine risk-weighted assets, as well as new capital requirements which will be introduced as part of the “Basel IV” regime. With a CET1 ratio of currently 19.1% (fully-phased in), pbb already holds a significant capital buffer, over and above existing regulatory requirements.

Deutsche Pfandbriefbank AG
Communications
Freisinger Strasse 5
85716 Unterschleissheim, Germany

pbb expects **pre-tax profit for 2017** of between €150 million and €170 million, assuming a largely stable development of its core portfolio in Europe, in conjunction with expanding lending business in the US and a slight increase in the aggregate of net interest and commission income. The forecast also encompasses normalised (and hence, increased) risk costs as well as a slight increase in general administrative expenses. Moreover, pbb intends to use the year 2017 to implement certain strategic decisions, including initiatives aimed at further diversifying its existing business in line with the Bank's risk standards – as already seen during the second half of 2016, with pbb's entry into the US market. In addition, pbb wants to expand its value-creation chain and to review platforms and processes with a view to digitalising its business. The Bank also wants to devise measures enabling it to reduce risk-weighted assets, against the background of regulatory changes. Finally, pbb is determined to take specific action to counter further increases in its cost base going forward.

Andreas Arndt, CEO of pbb Deutsche Pfandbriefbank, commented: "The stable development of adjusted pre-tax profit and the slight increase in new business are evidence of pbb's operative strength – in a market environment that remains very challenging indeed. In our view, pbb's shareholders should benefit from the Heta gain in the form of a special dividend. Looking ahead to 2017, the biggest challenge – besides ever-intensifying competition and the low interest rate environment – will be the dynamically-changing regulatory environment."

New business of €2 billion originated during the third quarter included €1.8 billion accounted for Commercial Real Estate Finance, the larger of pbb's two strategic business units. Approx. a third of new business in this segment was in extensions of more than one year. New business for the first three quarters totalled €6.7 billion and was thus below the previous year's level (9m 2015: €8.9 billion), reflecting pbb's selective stance in originating new business. In line with the Bank's strategy, Germany remained pbb's most important market, accounting for 49%, followed by the United Kingdom (17%), and by France and Central and Eastern Europe (around 10% each). Moreover, pbb closed its first transaction in the US in the third quarter, in an amount of US$70 million. Average gross margins on new business stood at around 170 basis points during the current financial year, in line with the previous year's level; the average loan-to-value ratio (LTV) was 62% (9m 2015: 63%).

During the third quarter, pbb's activities on the **funding markets** were at a similar level to the second quarter. The Bank raised total funds of €1.2 billion, which were almost evenly distributed amongst Mortgage Pfandbriefe (€0.3 billion), Public-Sector Pfandbriefe (€0.5 billion) and unsecured bonds (€0.3 billion). Aggregate issuance during the first nine months of €4.8 billion was clearly higher compared to the same period of the previous year (9m 2015: €2.9 billion), when pbb cut back its funding activities due to early loan repayments and its comfortable liquidity position.

FACTS AND FIGURES ON THE THIRD QUARTER/FIRST NINE MONTHS OF 2016

1. Consolidated income statement (IFRS, unaudited)

Third-quarter results were affected in particular by €132 million in an **extraordinary gain related to Heta**, against which pbb has recognised €15 million – largely in **provisions** – as a precautionary measure. These effects are visible in various line items of the income statement.

- pbb held Heta receivables in a total nominal amount of €395 million, which it adjusted in 2014 and 2015 by a total of €197.5 million (50% of the nominal value). Having accepted a buy-back offer from the Carinthian Compensation Payment Fund (*Kärntner Ausgleichszahlungs-Fonds*), in conjunction with the purchase of a guaranteed zero-coupon bond, pbb has realised just under 90% of the nominal value of its receivables. Adjusted for interest payments not received, as well as other unsatisfied claims, pbb recognised gross income of €132 million in the third quarter of 2016, which increased net income from financial investments by €123 million and permitted the reversal of loan loss provisions in a gross amount of €9 million.

- Against the extraordinary gain, pbb recognised provisions for legal costs related to tax audits for prior periods and other legal disputes (-€6 million, included in net other operating income/expenses), restructuring provisions (-€5 million, included in net miscellaneous income/expenses), and costs for implementing new regulatory requirements (-€4 million, included in general administrative expenses).

Third-quarter **net interest income** of €97 million was in line with the previous year's level (Q3 2015: €95 million), and with the previous quarters of the current year (Q2 2016: €93 million; Q1 2016: €102 million). On a nine-month comparison, net interest income declined to €292 million (9m 2015: €324 million). Current net interest income in pbb's strategic portfolios fell only slightly; the decline was largely driven by the scheduled ongoing reduction of positions from the non-strategic Value Portfolio, by way of maturities or sales. Income was also under pressure as a result of generally lower interest rate levels, further growing competitive pressure, and the proliferation of negative interest rates throughout the euro area.

Net fee and commission income totalled €2 million for the third quarter and €5 million for the first nine months (Q3 2015: €3 million; 9m 2015: €12 million). The figure for the same period in the previous year included €5 million in commission income generated in connection with a financing arrangement, which was repaid in full.

In its business, pbb continues to adhere to a conservative approach to risk, which is evident in the fact that **loan loss provisions** have remained at a low level. During the third quarter of 2016, the net figure additionally benefited from releases related to Heta, leading to a net release of loan loss provisions of €3 million in the third quarter. Given that pbb did not recognise any net additions during the first half of the year, the nine-month figures also show a net release of €3 million (9m 2015: net release of €8 million).

General administrative expenses of €53 million were slightly higher than in the same period of the previous year (Q3 2015: €52 million), but slightly lower for the first nine months (€147 million – 9m 2015: €150 million). Non-personnel expenses of €70 million increased from the previous year (9m 2015: €66 million); this item includes €4 million for a Bank-wide project for the implementation of new regulatory requirements. Personnel expenses declined to €77 million (9m 2015: €84 million). Thanks to the extraordinary gain from Heta, the cost/income ratio fell strongly to 37.2% (9m 2015: 50%).

Net trading income totalled -€3 million for the third quarter, compared to a flat figure for the same period of the previous year. Net trading income for the first nine months totalled -€10 million (9m 2015: €7 million). As in the second quarter of the current year, this largely reflected valuation effects from derivatives: at around -€9 million each, the so-called 'pull-to-par effect' as well as effects from bilateral Credit Value Adjustment (which reflects the credit risk of pbb and its derivatives counterparties) both burdened net trading income. This was offset by €7 million in positive measurement effects from interest rate and currency derivatives.

Net income from financial investments of €123 million for the third quarter was strongly influenced by the positive extraordinary effect (in the same amount) related to Heta (Q3 2015: €5 million). It totalled €128 million (9m 2015: -€32 million) for the first nine months of the year. The net figure for the first nine months of the previous year was burdened significantly by a €73 million write-down on Heta securities which was only partially offset by income (€41 million) from the disposal of securities, most of which came from the non-strategic Value Portfolio.

Net income from hedging relationships amounted to €1 million in the third quarter (Q3 2015: €7 million), and also €1 million for the first nine months of the year (9m 2015: €9 million). The net figure was exclusively due to hedge inefficiencies.

Net other operating income/expenses for the third quarter of 2016 totalled -€6 million (Q3 2015: -€12 million). This item includes €6 million in provisions for legal costs related to tax audits from prior periods and other legal disputes. The net figure of -€21 million for the first nine months of the year was roughly in line with the previous year's figure (9m 2015:-€20 million). As in the previous quarters, a major portion of this item was attributable to the bank levy: following the pledge of cash collateral, pbb recognised an expense of €21 million for the bank levy in the first nine months of the year. Expenses of €6 million for foreclosed assets of properties were offset by rental income and positive currency translation effects. The net figure for the same period of the previous year benefited from the divestment of a foreclosed asset in Japan.

Net miscellaneous income/expenses, which was negative at €5 million both in the third quarter and for the first nine months of the year (9m 2015: €7 million), included €5 million in restructuring provisions recognised in the third quarter.

Profit after taxes amounted to €121 million in the third quarter (Q3 2015: €53 million); it totalled €187 million for the first nine months of the year (9m 2015: €141 million). The total tax burden stood at €59 million for the first nine months of 2016 (9m 2015: €24 million).

2. Total assets and regulatory indicators

Consolidated total assets of pbb Group (in accordance with IFRS) amounted to €65 billion (31 December 2015: €66.8 billion). Besides the first-time netting of derivatives entered into with Eurex Clearing, the decline was also attributable to the planned reduction of the non-strategic Value Portfolio.

pbb's **CET1 ratio** was 19.1% as at 30 September 2016 (31 December 2015: 18.2%); the **own funds ratio** stood at 20.8% (31 December 2015: 19.9%); all regulatory indicators were calculated on a 'fully phased-in' basis, i.e. assuming the lapse of all transitional arrangements under Basel III.

Media contacts

Walter Allwicher, +49 89 2880-28787, walter.allwicher@pfandbriefbank.com
Oliver Gruss, +49 89 2880-28781, oliver.gruss@pfandbriefbank.com

Consolidated Income Statement of pbb Group (in accordance with IFRS, unaudited; € million)

	2015				2016			
	Q1	**Q2**	**Q3**	**9m**	**Q1**	**Q2**	**Q3**	**9m**
Operating income	93	109	98	300	90	91	214	395
Net interest and similar income	113	116	95	324	102	93	97	292
Net fee and commission income	7	2	3	12	2	1	2	5
Net trading income	5	2	-	7	-5	-2	-3	-10
Net income from financial investments	-20	-17	5	-32	4	1	123	128
Net income from hedging relationships	-1	3	7	9	1	-1	1	1
Net other operating income/expenses	-11	3	-12	-20	-14	-1	-6	-21
Loan loss provisions	4	1	3	8	-	-	3	3
General and administrative expenses	-48	-50	-52	-150	-45	-49	-53	-147
Net miscellaneous income/expenses	2	1	4	7	-	-	-5	-5
Pre-tax profit/loss	51	61	53	165	45	42	159	246
Income taxes	-12	-12	-	-24	-11	-10	-38	-59
Profit/loss after taxes	39	49	53	141	34	32	121	187

Overview of the pbb Group

	2015	2016
	9m	**9m**
Key financial indicators		
Earnings per share[1] (€)	1.05	1.39
Cost/income ratio (in %)	50.0	37.2
Return on equity (%)		
▪ before taxes	6.8[2]	12.2
▪ after taxes	5.8[2]	9.3
Balance sheet figures (€ billion)	**31 Dec 2015**	**30 Sep 2016**
Total assets	66.8	65.0
Equity (excluding revaluation reserve)	2.7	2.8
Reported equity	2.7	2.8
Regulatory indicators (%)		
CET1 ratio (fully phased in)	18.2	19.1
Own funds ratio (fully phased in)	19.9	20.8
Leverage Ratio (fully phased in)[3]	3.9	4.1

1) Basic and diluted
2) Excluding the silent partnership contribution, return on equity would be 8.8% before taxes and 7.6% after taxes.
3) The Leverage Ratio is defined as the ratio between tier 1 capital and the relevant exposure according to CRR.