Annual Report 2013

PUBLIC SECTOR FINANCE
REAL ESTATE FINANCE

DEUTSCHE
PFANDBRIEFBANK

Financial Highlights
Ratings

Financial Highlights		2013	2012
Operating performance according to IFRS			
Pre-tax profit/loss	in € million	165	124
Net income/loss	in € million	160	69
Key ratio			
Return on equity before taxes	in %	5.0	3.8
Return on equity after taxes	in %	4.9	2.1
Cost-income ratio[1]	in %	64.7	73.0
Balance sheet figures		**31.12.2013**	**31.12.2012**
Total assets	in € billion	74.3	97.1
Equity (excluding revaluation reserve)	in € billion	3.4	3.2
Equity	in € billion	3.5	3.3
Personnel			
Employees		852	1,044

[1] The cost-income ratio is the ratio of general administrative expenses and operating revenues

Senior unsecured ratings and ratings for Pfandbriefe of pbb[1]	31.12.2013			31.12.2012		
	Fitch Ratings	Moody's	Standard & Poor's	Fitch Ratings	Moody's	Standard & Poor's
Long-term rating	A–	Baa2	BBB	A–	Baa2	BBB
Outlook	Stable	Negative	Stable	Stable	Negative	Stable
Short-term rating	F1	P–2	A–2	F1	P–2	A–2
Public sector Pfandbriefe	–	Aa1	AA+[3]	–	Aa1	AA+[2]
Mortgage Pfandbriefe	–	Aa2	AA+[3]	–	Aa1[2]	AA+[2]

[1] Ratings from mandated rating agencies
[2] CreditWatch Negative
[3] Stable outlook

Due to rounding, numbers presented throughout this document may not add up precisely to the totals provided and percentages may not precisely reflect the absolute figures.

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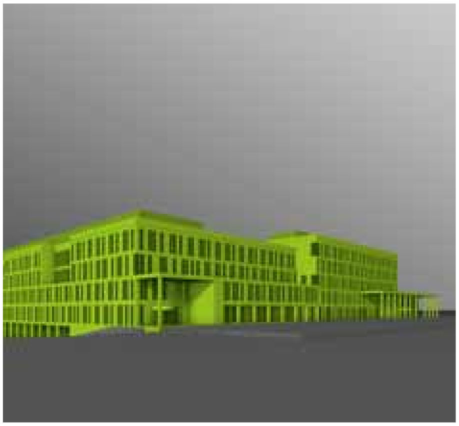

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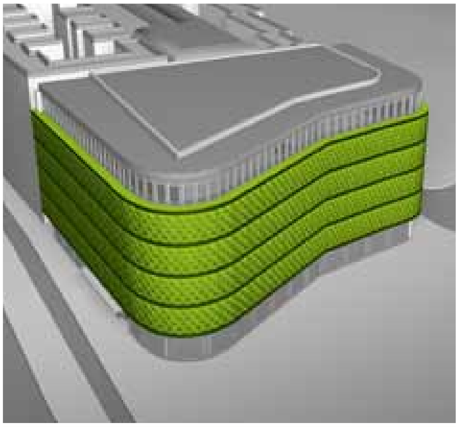

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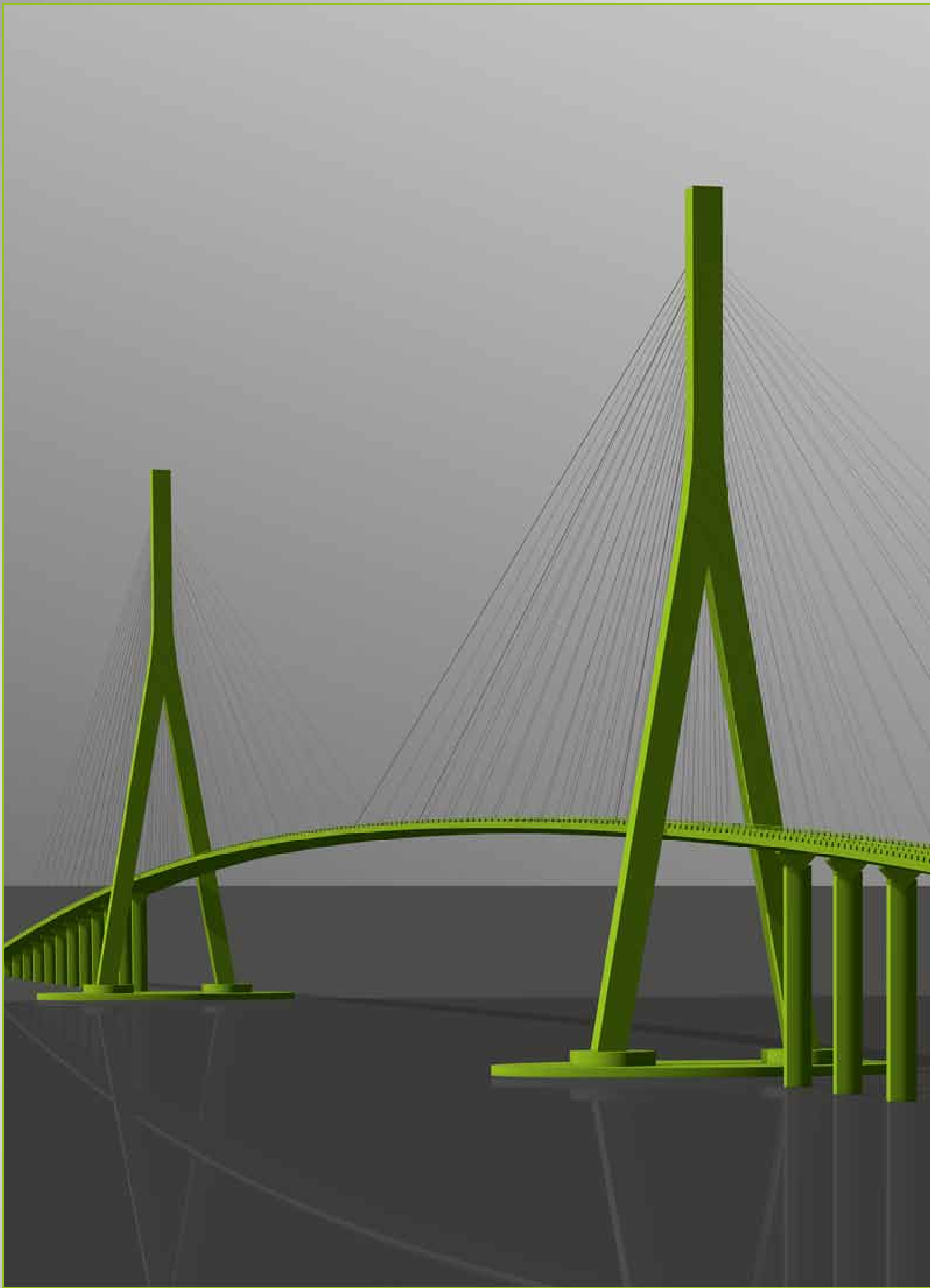


pbb Deutsche Pfandbriefbank is a specialist bank for real estate finance and public investment finance. We are active in selected European countries; in addition to Germany, we focus on the United Kingdom, France, the Nordic region and individual countries in Central and Eastern Europe.

pbb Deutsche Pfandbriefbank fulfils an important economic function by supplying credit to the real estate industry and by funding public sector infrastructure projects.

Real Estate Finance

We structure medium to large financing transactions for professional real estate investors in office, retail, residential and logistics properties in particular. Our customers benefit from our mix of local and international expertise.

Public Investment Finance

We finance public sector investment in infrastructure projects, for example public housing, utilities and waste disposal, health care and nursing care properties, as well as child care and educational facilities. We also provide government-backed export finance.

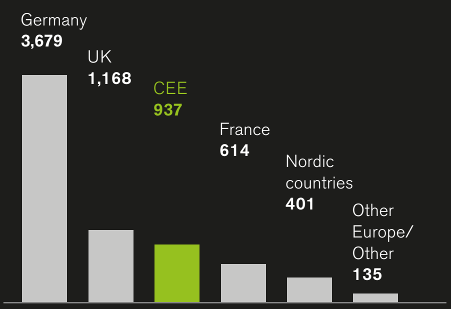
The Park Prague

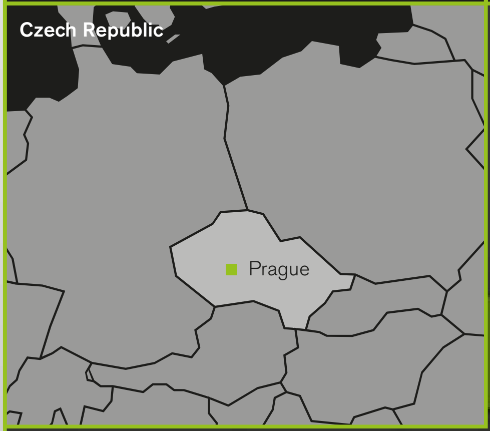
€ 90 million

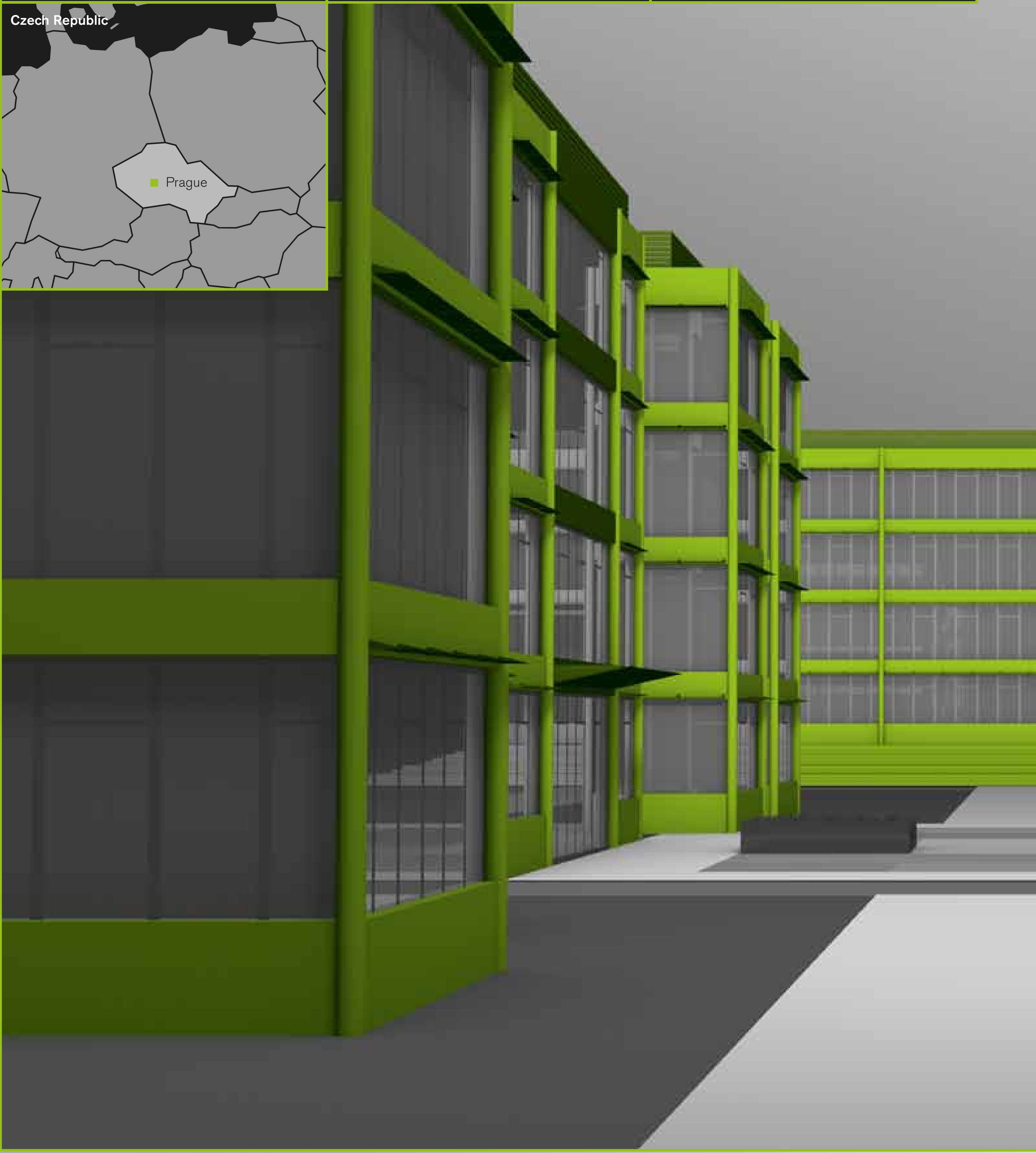
Syndicated investment finance
Czech Republic
July 2013

Central and Eastern Europe – and especially Poland and the Czech Republic – is an important target market for pbb Group's Real Estate Finance business. «The Park», a campus-style office complex in Prague, the Czech Republic's capital, is considered to be one of the most successful properties of its kind in the entire region. Almost all the tenants are international companies. pbb and Helaba provided equal funding for the purchase of «The Park» by a subsidiary of Starwood Capital Group. pbb also manages the loan payments and the collateral. The purchase was one of the largest property transactions for several years in Central and Eastern Europe.

Real Estate Finance: new business by region
Commitments in € million

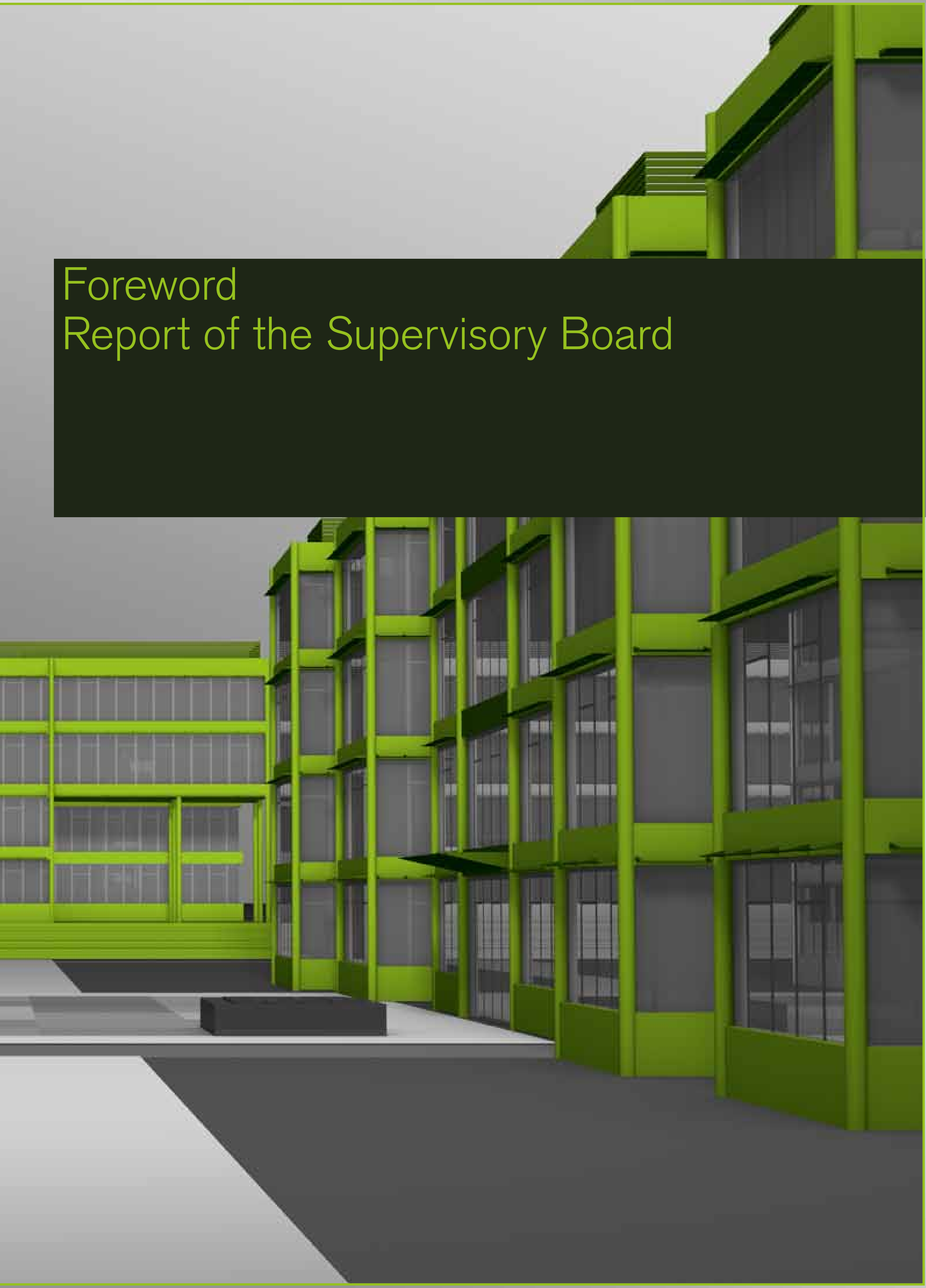






Foreword

Report of the Supervisory Board



Foreword

Deutsche Pfandbriefbank Group (pbb Group) looks back on a successful financial year. Tensions on the financial markets eased in 2013, as policymakers and central banks were able to contain the disruptions caused by the European sovereign debt crisis. In this somewhat improved environment, banks' earnings situations remained negatively impacted by the very low level of interest rates. However, pbb Group continued its successful performance of the last few years in financial year 2013 and significantly exceeded its new business and earnings targets. Additionally, the non-strategic business activity of servicing the FMS Wertmanagement portfolio was stopped as planned, and the Group's structures and processes were revised. This has positioned pbb Group properly for the future as a specialised Pfandbrief bank with a European focus. In this set-up the Group is now ready to move forward in 2014 and with its planned privatisation in 2015.

We once again demonstrated our origination power in our core business – real estate financing and public investment financing. At €8.2 billion, new business was at a record high, up almost 50% on the previous year, the risk-return profile remaining at an attractive level. The new sales locations in Germany and Sweden became fully operational, enabling us to get closer to customers in core markets and improve our market penetration.

A further increase in funding volumes was essential to our new business success. pbb Group's funding strength in the area of refinancing is also evidenced by the successful issuance of a 15-year public sector Pfandbrief – something that no other bank had realised for a decade – as well as mortgage Pfandbriefe denominated in foreign currencies. In the area of unsecured funding, we broadened our base with pbb direkt, a term and overnight deposit for private investors. The deposit-taking business has been extremely well received by customers, who invested approximately €620 million in pbb direkt between its launch in March and the end of 2013.

Management Board of Deutsche Pfandbriefbank AG from left to right:
Dr. Bernhard Scholz, Wolfgang Groth, Alexander von Uslar, Manuela Better (CEO), Andreas Schenk

The discontinuation of portfolio management for FMS Wertmanagement, which pbb Group transferred to the latter's service company at the end of September 2013, further reduced pbb Group's complexity, allowing it to focus even more strongly on its core business. This created the basis for optimising structures and processes to meet our demands as a specialised, consistently customer-oriented Pfandbrief bank now even more effectively. We implemented this project in parallel to the transfer of services, which means that pbb Group has achieved its target structure for privatisation.

We will focus consistently on further increasing medium- and long-term profitability. Net interest income is a greater lever than general expenses – which we will naturally continue to monitor. New loans are more profitable than expiring loans, and pbb Group's strategic loan portfolio will also continue to grow. We will also use 2014 to continually demonstrate skills, which will be decisive for privatisation: We want to show pbb Group's origination power and funding strength, as well as its risk management expertise. We will continue to convince our customers with a combination of loan structuring skills, pan-European reach and reliable lending and credit risk management.

As in the previous years, pbb Group's success was primarily based on its employees' commitment. I would like to thank them for their dedication and their loyalty.

Yours sincerely,

Manuela Better

Report of the Supervisory Board

The Supervisory Board of Deutsche Pfandbriefbank AG (pbb) hereby reports on the focuses of its supervisory and advisory activities for the 2013 financial year.

The macroeconomic environment was dominated by the stabilisation of the global economy and by the easing of the euro crisis. This allowed pbb to focus more strongly on new business, particularly in the area of real estate financing. As part of its supervisory and advisory function, the Supervisory Board addressed in particular the business activities of pbb Group that reflect market developments. One particular focus was on supporting the Company in recovering its sales strength/market presence giving due regard to a conservative risk profile.

Corporate Governance

The Supervisory Board continually monitored the Management Board in financial year 2013, as in the past, and provided it with regular advice on the management of the Company.

It assured itself in all cases that the management measures taken by the Management Board were lawful, appropriate, and due and proper. The Management Board fulfilled its duties to provide information and informed the Supervisory Board in a regular, timely and comprehensive manner, both in writing and orally, about matters and measures relevant to the Company. This also included information on variances between target and actual figures. The members of the Supervisory Board had sufficient opportunity at all times to critically assess the reports and proposed resolutions submitted by the Management Board and to make its own suggestions in the Supervisory Board committee meetings and in the plenary sessions.

In particular, the Supervisory Board held in-depth discussions on, and reviewed the plausibility of, all business transactions material to the Company on the basis of written and oral reports by the Management Board.

On 22 February 2013, the Supervisory Board again resolved the declaration of conformity with the Public Corporate Governance Code of the Federation, which is published online on pbb's website (www.pfandbriefbank.com). Please also refer to the Group's remuneration report, which is printed in this annual report and is also published on pbb's website. With respect to the requirement of the Public Corporate Governance Code of the Federation to disclose the proportion of women in supervisory bodies, please refer to the table showing the composition of the Supervisory Board and its committees.

Supervisory Board Meetings

The Supervisory Board of pbb held eight meetings in 2013, two of which took the form of conference calls, and passed one resolution outside the meetings that was adopted by circulating written documents.

All regular meetings addressed the current business position of pbb Group, which was discussed in detail with the Management Board in each case. The Management Board informed the Supervisory Board regularly and in a timely manner about pbb Group's economic and financial development. During the regular meetings, the Supervisory Board also received reports on the risk position, risk management, new business and the liquidity strategy, as well as on significant events that are of material importance to the assessment of the Company's position, development and management.

In the conference call on 18 January 2013, the Supervisory Board and Management Board discussed the planned restructuring measures at pbb in preparation for the planned privatisation. The regular meeting on 22 February 2013, which was also attended by a member of the Management Committee of the Financial Market Stabilisation Agency (FMSA), mainly discussed and resolved the multi-year planning, as well as addressing pbb's business strategy. In addition, the Supervisory Board resolved in this meeting to perform an efficiency review on the activities of the Supervisory Board and its committees. The meeting on the financial statements held on 9 April 2013 approved the 2012 consolidated financial statements and adopted the annual financial statements. The Annual General Meeting was also prepared and the amended risk strategy was discussed.

The meeting on 13 May 2013 mainly concerned the report on the first quarter of 2013. The Supervisory Board discussed the interim report as at 30 June 2013 in its meeting on 12 August 2013 in Dublin. In the same meeting, the Supervisory Board was also given a status update on the transfer of the services provided for the portfolio outsourced to FMS Wertmanagement to FMS Wertmanagement Service GmbH. On 11 November 2013, the discussion focused in particular on an analysis of the opportunities and limitations associated with spinning off the Bank's Public Sector Finance business and the status of preparation of a recovery plan, in addition to the quarterly financial statements. In the last meeting of the Supervisory Board of pbb, in the form of a conference call on 10 December, the Supervisory Board approved the multi-year planning resolved by the Management Board for 2014–2017 following in-depth discussion.

Furthermore, the Supervisory Board also informed itself via written reports about the probable effects of Basel III. The Supervisory Board checked that the auditors, KPMG AG Wirtschaftsprüfungsgesellschaft (KPMG), complied with the independence requirements, engaged the auditors, and agreed the fee with them.

The CEO was in continual contact with the Chairman of the Supervisory Board with regard to important developments. The Supervisory Board regularly discussed developments in the lending business and the overall credit policy, all reportable exposures, risk trends and risk management, the business strategy, and developments and trends on the lending and funding markets.

Supervisory Board Committees

The **Audit Committee** held a total of seven meetings and comprised Dagmar Kollmann (Chairperson), Dr. Bernd Thiemann, Dr. Günther Bräunig and Dr. Hedda von Wedel.

Its meetings reviewed and discussed the annual financial statements and consolidated financial statements for 2012, the interim reports and the reports by Internal Audit and KPMG on internal and external audit findings. KPMG also provided an overview of the review of pbb Group's internal control system (ICS) in financial year 2012, as well as the results of the ICS audit in accordance with IDW PS 951 Type B in connection with FMS Wertmanagement Servicing. In addition, the Audit Committee addressed the proposal for the election of the auditors and the audit plan for financial year 2013, as well as the effects of current regulatory developments on the Bank. Furthermore, regular reports were received on the internal control system and the monitoring of the key controls that have been established, existing legal disputes, compliance issues, and Internal Audit's audit planning and implementation.

The **Risk Management and Liquidity Strategy Committee** (RLA) held six meetings and also discussed credit exposures, usually during monthly conference calls. It comprised Dr. Günther Bräunig (Chairman), Dagmar Kollmann and Dr. Bernd Thiemann.

The RLA consolidated the Supervisory Board's supervision of risk management and liquidity management, reviewed the Management Board's risk reporting and was involved in the credit approval process to the extent laid down in the rules of procedure. The RLA also regularly discussed the situation with respect to new business, liquidity and funding. In 2013, it also addressed the asset upgrade and the novations in connection with FMS Wertmanagement, the credit process, the salvage acquisitions and development loans, enhancements to the risk methodology, and the implementation of findings relevant to risk management. The RLA also received reports on developments on the French real estate market and a number of country portfolios.

In addition, the RLA addressed individual exposures on numerous occasions, usually in conference calls. These related to regular resubmissions and approvals for change applications and new business required to be submitted under the RLA's rules of procedure.

In 2013, the members of the Supervisory Board participated in the meetings of the Supervisory Board and the committees as follows:

Supervisory Board of pbb as of 31 December 2013			Committee function and meeting attendance	
Name and place of residence	Principal activity	Supervisory Board function and meeting attendance	Audit Committee	Risk Management and Liquidity Strategy Committee
Dr. Bernd Thiemann Münster, Germany	Former Chairman of the Management Board of DG Bank AG	Chairman 8 of 8	Member 7 of 7	Member 6 of 6
Dagmar Kollmann Vienna, Austria	Businesswoman	Deputy Chairperson 8 of 8	Chairperson 7 of 7	Member 6 of 6
Dr. Günther Bräunig Frankfurt am Main, Germany	Member of the Management Board of KfW	Member 8 of 8	Member 7 of 7	Chairman 6 of 6
Dr. Christian Gebauer-Rochholz Hochheim, Germany	Bank employee	Employee representative 8 of 8		
Dr. Alexander Groß Teltow, Germany	Head of Department I, Economic Policy in the Federal Ministry for Economic Affairs and Energy	Member 7 of 8		
Georg Kordick Poing, Germany	Bank employee	Employee representative 8 of 8		
Dr. Ludger Schuknecht Frankfurt am Main, Germany	Head of Department, Fiscal Policy and Macroeconomic Affairs, International Financial and Monetary Policy in the Federal Ministry of Finance	Member 8 of 8		
Heike Theißing Munich, Germany	Bank employee	Employee representative 8 of 8		
Dr. Hedda von Wedel Andernach, Germany	Retired President of the Bundesrechnungshof (Federal Court of Audit)	Member 8 of 8	Member 7 of 7	

Training and Further Education

Members of the Supervisory Board were personally responsible for ensuring they received the training and further education necessary for their duties. In a special meeting on 21 February 2013, the Supervisory Board members were trained in the real estate markets by the Management Board and experts from the Bank.

Annual Financial Statements

The auditors of the annual and consolidated financial statements elected by the Annual General Meeting, KPMG, audited the annual and consolidated financial statements of pbb dated 31 December 2013, including the management reports, and issued them with an unqualified audit opinion. The financial statement documents and audit reports were submitted to all Supervisory Board members in good time. The Audit Committee addressed the financial statement documents in its meeting on 31 March 2014. The annual financial statements and consolidated financial statements, as well as the management reports and audit reports, were discussed with the Management Board and representatives of the auditors in detail. Following its own review, the Supervisory Board did not raise any objections to the result of the auditors' audit. In the meeting on the financial statements, the Supervisory Board approved the consolidated financial statements prepared by the Management Board and adopted the annual financial statements.

The Supervisory Board wishes to thank the Management Board, all employees and the employee representatives for their dedication and achievements in the past financial year.

For the Supervisory Board

Dr. Bernd Thiemann
Chairman

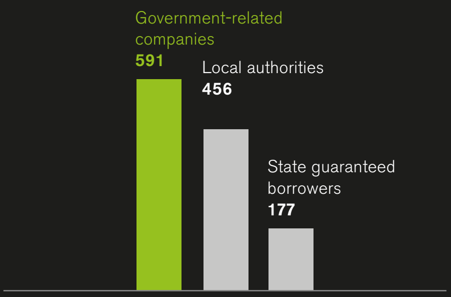
Jena University Hospital

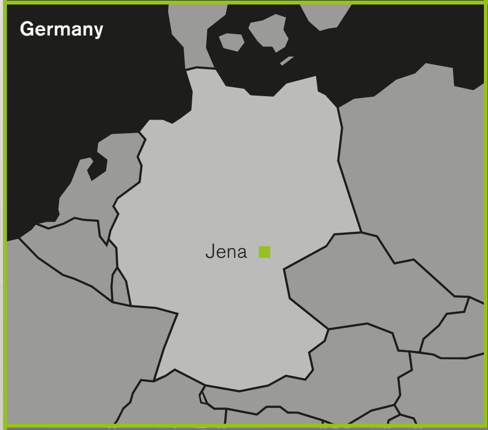
€ 121 million

Syndicated public investment finance
Germany
June 2013

pbb Group provides public sector funding for public infrastructure investment. The Group is currently active in this sector in Germany, France and the Nordic region. With Jena University Hospital, one of Germany's most modern hospital clinics is now under construction in Thuringia. In the second construction phase, Jena University Hospital (UKJ) is largely implementing the construction measures with general contractor Ed. Züblin AG. Project finance is being provided by Thüringische Aufbaubank (TAB). The financing takes the form of forfaiting with a waiver of objections. UKJ will repay the banks within 20 years.

Public Investment Finance: new business by counterparty
Commitments in € million





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Group Management Report

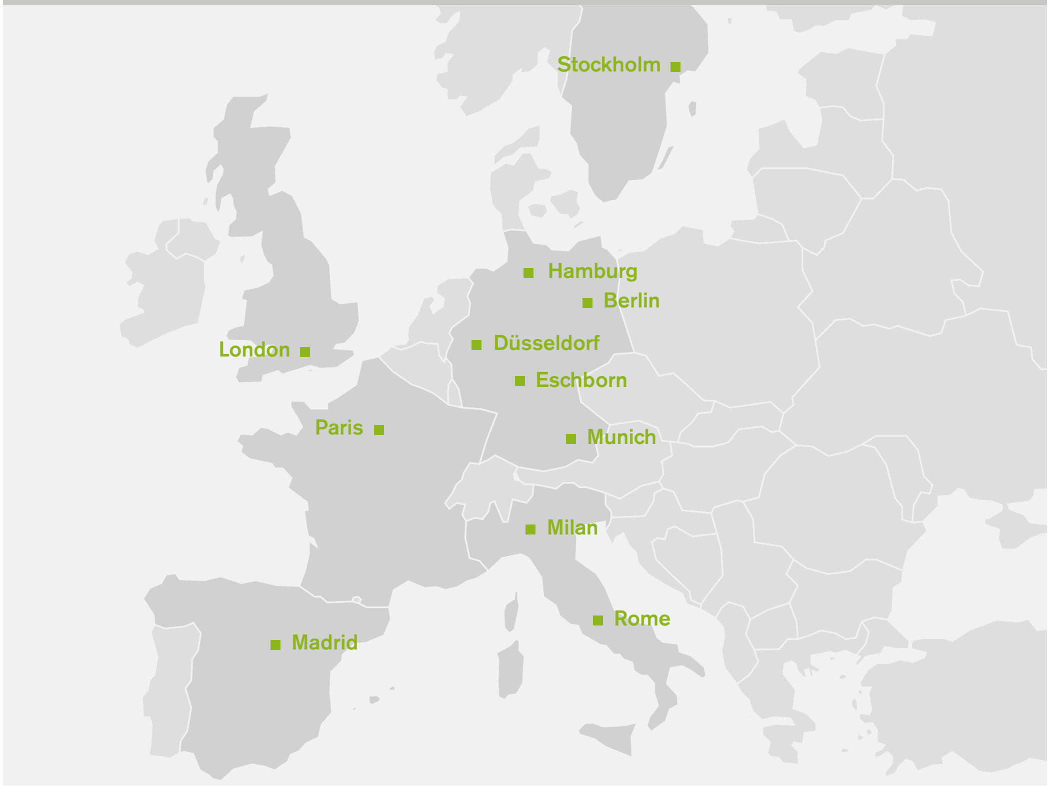
Group Management Report

Fundamental Information about the Group

Group Structure

Deutsche Pfandbriefbank AG (pbb) is the parent company of Deutsche Pfandbriefbank Group (pbb Group). It is a wholly owned subsidiary of Hypo Real Estate Holding AG (HRE Holding). HRE Holding is wholly owned by the Financial Market Stabilisation Fund (Finanzmarktstabilisierungsfonds-FMS), which is administered by the Financial Market Stabilisation Agency (FMSA). FMSA is an institution of the Federal Republic of Germany. pbb has branches in roughly a dozen national and international locations; the Bank's headquarters are in Munich.

Sales branches


Stockholm
Hamburg
Berlin
London
Düsseldorf
Eschborn
Paris
Munich
Milan
Rome
Madrid

Business Model and Strategy

pbb Group specialises in real estate finance and public investment finance. The Group is active in both areas in selected European countries. The focus is on Germany, the United Kingdom, France, the Nordic countries as well as some Central and Eastern European countries. The Group's core business is medium- to long-term lending: pbb Group plays an important role in this area, providing credit to the real estate industry and funding to the public sector for public infrastructure improvement projects and measures. pbb Group's focus is on primary customer business. In addition to traditional, individually customised financing solutions, the Group offers clients derivatives for hedging credit transaction risk. It does not maintain a trading book for securities portfolios held to realise short-term gains.

In the lending business, pbb Group either acts as the sole lender or – in particular for high-volume transactions – works together with financing partners. The Group has a wide network of banking partners and other sources of finance, such as mezzanine finance and private equity. In this syndicate business, the Group also functions as the arranger responsible for all coordination between the syndicate and the borrower; alternatively it takes over duties in connection with the management of syndicated loans as an agent. In addition, it acts as an underwriter, initially providing the financing itself and then selling on parts of these loans to interested partners in the syndication process.

Competitive Position

In commercial real estate finance, pbb is one of the leading institutions in its target markets and segments. As such, pbb is one of the few remaining banks that can provide its customers with financial expertise in real estate finance and public investment finance practically everywhere in Europe. In key locations, the bank has local contact persons.

Strategic Portfolios

In the real estate finance area, pbb's services are aimed at medium- to long-term professional real estate investors in Germany and abroad (real estate companies, institutional investors, real estate funds, etc.). In addition, it targets customers with a regional focus in Germany. pbb Group specialises in providing medium to large volumes of finance. Its main area of emphasis is on less volatile types of properties such as office buildings, retail properties, residential real estate and logistics facilities. The regional market focus is on the core European Pfandbrief markets: Germany, the United Kingdom, France and the Nordic countries, as well as other selected European regions. Here, the pbb Group offers both local and cross-border financing expertise. A large majority of the loans concerned are for investment finance – i.e. loans to acquire existing properties or follow-up financing with existing cash flows; development loans are significantly less important, not speculative and mainly relate to the property development business in Germany.

In its public investment finance, pbb Group finances Pfandbrief-eligible, mid- to long-term public sector infrastructure projects. The focus in this area is on public institutions, public housing, utilities and waste disposal buildings and health care/nursing care properties, as well as child care and educational facilities. The Group is also active in the field of government-backed export finance. It provides loans to public sector borrowers, companies operating under public or private law and publicly guaranteed special-purpose vehicles. The regional focus is on Germany, France and the Nordic countries, although pbb Group also does business in other selected European regions.

Run-down Portfolios

In addition to its two strategic portfolios, pbb Group has non-strategic portfolios. These relate almost entirely to an existing portfolio of outstanding non-specific public sector loans (budget financing). This portfolio of recognised assets generates interest income and matures in line with the underlying maturities. As mandated by the European Commission as a result of the state aid proceedings in 2011, the Group does not actively generate any new business in this area. A few transactions are permitted to manage cover pools or safeguard liquidity. Run-down portfolios also include few structured products within the area of other portfolios.

Funding

Loans are largely funded using matching maturities and primarily via the Pfandbrief market, supplemented by unsecured funding. Issues are regularly placed on the international capital markets using the benchmark format or take the form of bilateral private placements. pbb Group structures private placements as bearer or registered securities depending on investor requirements. This means that, for example, the term and interest payment structure can be negotiated on an individual basis. As is the case in the lending business, issues are denominated in a range of currencies, with a focus on the euro.

pbb issues mortgage Pfandbriefe and public sector Pfandbriefe, and is the second-largest issuer in Germany by outstanding volume. The Pfandbrief market is highly liquid and has a broad investor base. It is the second-largest market for fixed-income securities in Germany after the market for public sector bonds. The global Pfandbrief market share is about 20% of the total oustanding covered bonds volume. Promissory notes and bearer bonds are the main vehicles used for unsecured funding.

Banks, funds and insurance companies as well as central banks and state funds are the main investors in debt securities. Private investors have played only a minor role to date. Since March 2013, pbb Group has added deposit-taking activities with private investors in Germany to its range of activities, offering them call money and term deposit accounts with various maturities via its pbbdirekt.com online platform.

Strategy

pbb Group's strategy aims to ensure sustainable business success and avoid speculative elements. Assessing and appropriately pricing credit risk in its new business and access to funding markets on appropriate terms are crucial for its business success. An additional critical success factor is managing the existing portfolio with the aim of identifying changing risks at an early stage and mitigating them by taking appropriate measures.

According to the 2011 European Commission decision on the state aid proceedings, the Federal Republic of Germany, as the ultimate owner, shall privatise pbb by the end of 2015. The core strategic objective is therefore to enable pbb to be privatised.

pbb Target Model

2012 the Management Board has started of a project to align pbb Group's structure and size with its vision of being a specialist Pfandbrief bank with a European focus. With the implementation of this vision in 2013, the Management Board laid the foundations for privatisation and prepared the Group well for the future above and beyond 2015.

In the past two years, the Group expanded its sales capabilities, adding new locations in Stockholm, Berlin, Hamburg and Düsseldorf, and further improved its market penetration by strengthening its market teams.

In addition to this strategic development project, projects to optimise primary processes and to harmonise IT were completed over the last two years.

Termination of FMS Wertmanagement Servicing

At the end of 2013, the services that pbb Group had provided to FMS Wertmanagement for the latter's portfolio were discontinued. This move was mandated by the European Commission and is also in line with pbb's strategy as a specialist bank for real estate finance and public investment finance. Activities were transferred to FMS Wertmanagement's service company, FMS Wertmanagement Service GmbH, and to other external service providers. pbb Group and FMS Wertmanagement have planned, prepared and implemented the transfer of servicing in a joint project since autumn 2011.

Hypo Real Estate Japan Corporation, Tokyo, a subsidiary of pbb, is an exception; it provides services for FMS Wertmanagement's Japanese Real Estate Finance portfolio.

pbb Group and FMS Wertmanagement have also continued to provide each other services after 30 September 2013 that cannot be otherwise obtained on the basis of what is currently a cost-plus agreement. These services relate in particular to the provision of information, the granting of powers of attorney and the provision of services required under supervisory laws. In addition, pbb and FMS Wertmanagement entered into a settlement agreement in the fourth quarter of 2013 under which all potential claims by FMS Wertmanagement for damages related to services provided, all past, present and future claims for the reimbursement of costs for the legal transfer of assets (upgrades) that were previously only transferred or hedged by means of subparticipations, back-to-back derivatives, or financial guarantees, as well as payment obligations by pbb in connection with the transfer of employees to FMS Wertmanagement Service GmbH, are taken to have been settled.

In the course of the discontinuation of the services, certain pbb Group employees also moved to FMS Wertmanagement's service company, where their knowledge of the portfolio will permit continuity in its future management.

Increasing Profitability

pbb's Management Board is aiming to further significantly increase the Group's profitability in the period up to its privatisation. This is to be achieved by expanding the earnings base by increasing the profitability of new business while also growing the strategic portfolios and continuing to reduce operating costs.

In particular, discontinuing the services provided for FMS Wertmanagement's portfolio is having a positive impact on costs. Although no income has been received for the services provided after 1 October 2013, the associated personnel and non-staff expenses have also largely been reduced. Moreover, additional savings potential exists in the form of reducing complexity and strict cost discipline at pbb Group.

Internal Management System

pbb Group's internal management system is focused on achieving long-term growth in the value of the Group as a prelude to its successful privatisation, considering aspects of risks and regulatory requirements. The key objective is to achieve a balanced risk/return ratio. Risks taken on should be consistent with external and internal risk-bearing capacity guidelines and an adequate return on capital employed should be generated.

Internal management and measurement at pbb Group are based on a consistent and integrated key performance indicator system (KPI system), which assists executives in the management of the Group. The KPI system comprises the dimensions of profitability, growth in the strategic real estate finance and public investment finance portfolios, risk and capital. Regular target-actual comparisons and related analyses show management the reasons for any variances in the key performance indicators. Current market developments, such as interest rates, are also shown. In addition to strategic planning for the Bank as a whole, regular medium-term projections for profitability indicator and (stress) scenario forecasts ensure management has a comprehensive overview of the Group's future business development.

No changes were made year-on-year to the internal management system. Non-financial key performance indicators are not explicitly managed. The following financial key performance indicators have been defined:

> One key profitability indicator is return on equity after taxes. This is calculated by dividing net income/loss in accordance with the IFRSs by the average equity available in the financial year, excluding the revaluation reserve. Pre-tax profit/loss is a further financial key performance indicator. The aim is to increase it both by generating higher revenues and through strict cost discipline. Cost discipline and efficiency are monitored using the cost-income ratio, i.e. the ratio of general administrative expenses to operating revenues.

> The new business volume, which includes prolongations with maturities of more than one year, is a key factor influencing the volume of interest-bearing assets and hence in future earning power. A present value management approach is used for managing and calculating new business. In line with the management of the Bank as a whole, each new business transaction should make a positive value contribution to the Bank's overall income after the deduction of all costs (full absorption costing).

> Risk management is based on two risk-bearing capacity approaches, the gone concern approach and the going concern approach. Management using the going concern approach ensures that pbb Group can still meet the regulatory minimum capital ratios even after an adverse economic scenario. The gone concern approach, on the other hand, is based on the assumption that pbb Group, in the hypothetical event of the institute being liquidated, is able to fully service its unsubordinated debt instruments with a very high degree of probability. A precondition for demonstrating risk-bearing capacity in both cases is that the risk cover amounts exceed the required economic risk capital. The results of the risk-bearing capacity assessment and the methods used are described in detail in the risk and opportunity report.

> In accordance with the waiver rule set out in Section 2a of the KWG, pbb is exempted from the requirement to comply with regulatory capital ratios at the level of the Bank. However, the Tier 1 capital ratio, a key management indicator, is calculated regularly on a pro forma basis. This ratio is calculated by dividing the Tier 1 capital as defined in the Solvabilitätsverordnung (SolvV – German Solvency Regulation) by the risk-weighted assets in accordance with Basel II. Since 31 December 2013, for all portfolios which were requested for approval and after authorisation by BaFin, the Advanced Internal Rating Based Approach (Advanced-IRBA) has been applied in full for the calculation of regulatory capital backing. After the implementation of Basel III a regulations requirement in the form of a minimum Common Equity Tier 1 capital ratio (core equity Tier 1 ratio) will be calculated.

pbb Group as an Employer

pbb Group employed a total of 852 people at the end of 2013 (previous year: 1,044 employees). The Group's adjusted turnover rate[1] was 12.03% in 2013 (previous year: 9.92%).

In connection with the transfer of the services provided for FMS Wertmanagement's portfolio, a total of 109 employees were transferred to FMS Wertmanagement Service GmbH as at the end of 30 September 2013, mainly by way of a transfer of business in accordance with section 613 a of the Bürgerliches Gesetzbuch (BGB – German Civil Code) in Germany, and on the basis of the comparable national provisions at the Bank's international locations. In the process, the rules governing the transfer of business were incorporated into the individual agreements where possible and appropriate.

At the same time, the necessary organisational changes relating to the implementation of the target model – a specialised Pfandbrief bank – as well as the required privatisation of pbb and the intended sale of its fellow subsidiary DEPFA, were successfully implemented. With respect to the required job reduction measures, most employees were able to be placed in new roles in other functions. Agreed settlements based on the current redundancy plan measures and the respective national standards were reached without any further court involvement for employees who could not be offered a new position. The job cuts were completed in 2013 with the exception of individual cases and the reductions in functions that had been scheduled for a later date.

Human resources development plays a key role at pbb Group. The continuous professional development (CPD) offering, which had already been enhanced in 2012, was continued in 2013 and further adapted to departmental and employee training requirements. After focusing on internal management seminars and external training in financial statements analysis and appraiser training in 2012, the offering was expanded in 2013 to include new external courses and training both on specialist topics (e.g. in connection with regulatory requirements and new developments in capital markets law, credit risk and interest rate derivatives) and on soft skills and methodological know-how.

€ 0.9 million (previous year: € 1.2 million) was spent on internal and external training measures for pbb Group employees in 2013. The decline in training expenses is attributable to the decrease in employees scheduled for 2013 in connection with the discontinuation of the services provided to FMS Wertmanagement.

[1] The adjusted turnover rate is defined as turnover as a result of termination by the employee or the Bank, the expiration of temporary contracts, or of termination agreements being signed. It does not include cessation of employment due to death, retirement, early retirement, or Group transfers. In financial year 2013 the rate was additionally adjusted for the non-recurring effect in connection with the transfer of employees to FMS Wertmanagement Service GmbH.

Remuneration Report

The remuneration received by the various members of the Management Board and the Supervisory Board for financial year 2013 is disclosed individually in the following.

Management Board

pbb does not remunerate the activities of its Management Board, which is also the Management Board of the parent company, HRE Holding. Management Board remuneration is paid exclusively by HRE Holding; the pension commitments also exist exclusively at the level of HRE Holding. In this respect, the Group remuneration and pension commitments by HRE Holding to the members of the Management Board are presented in the following for information and transparency purposes:

Group Remuneration Paid to Members of the Management Board of HRE Holding			2013			2012
in € thousand	Monetary remuneration	Non-cash benefits[1]	Total	Monetary remuneration	Non-cash benefits[1]	Total
Manuela Better[2]	500	17	517	500	15	515
Wolfgang Groth	500	18	518	500	42	542
Dr. Bernhard Scholz[2]	500	16	516	500	24	524
Alexander von Uslar[2]	500	23	523	500	23	523
Total	**2,000**	**74**	**2,074**	**2,000**	**104**	**2,104**

[1] Includes the cost of customary non-cash incidental benefits, which are subject to tax

[2] In addition, individual agreements have been entered into with respect to pension obligations comprising a percentage of the fixed annual remuneration

Pension Commitments to Members of the Management Board of HRE Holding				2013	2012
in € thousand	Present value of pension claims vested	Interest expense	Outstanding past service cost	DBO as of 31.12.	DBO as of 31.12.
Manuela Better, Chairperson	105	138	-	4,160	4,235
Dr. Bernhard Scholz	114	124	-	3,786	3,817
Alexander von Uslar	111	120	-	3,569	3,680
Total	**330**	**382**	**-**	**11,515**	**11,732**

Supervisory Board

The members of pbb's Supervisory Board receive annual remuneration of € 10,000 in accordance with Article 10 (1) of the Articles of Association. No additional remuneration is paid for committee work. Remuneration entitlements accrue on a pro rata basis for the period of the appointment in each case. The Bank reimburses travel expenses; no attendance fees are paid.

Provision for the Remuneration of the Supervisory Board of pbb			2013	2012
in €	Remuneration	VAT	Total	Total
Annual remuneration per member	10,000	19 %		
Dr. Günther Bräunig	10,000	1,900	11,900	11,900
Dr. Christian Gebauer-Rocholz[1] (from 21 November 2012)	10,000	-	10,000	1,370
Dr. Alexander Groß[2] (from 1 June 2012)	10,000	-	10,000	5,850
Dagmar Kollmann[3]	10,000	-	10,000	11,900
Georg Kordick[1]	10,000	1,900	11,900	11,900
Dr. Ludger Schuknecht[2] (from 1 June 2012)	10,000	-	10,000	5,850
Heike Theißing[1]	10,000	1,900	11,900	11,900
Dr. Bernd Thiemann	10,000	1,900	11,900	11,900
Dr. Hedda von Wedel	10,000	1,900	11,900	11,900
Total	**90,000**	**9,500**	**99,500**	**84,470**

[1] Employee representative
[2] Since the government ministry representatives perform their Supervisory Board activities on their employer's instructions, income from these activities is not subject to VAT
[3] Due to the place of residence abroad not subject to VAT. Taxes for Supervisory Board members are paid by the Company instead.

Employee Remuneration

Employees are remunerated in accordance with regulatory and statutory requirements, in particular the Restrukturierungsgesetz (German Restructuring Act). In the course of the implementation of these requirements, the new remuneration system introduced in financial year 2010 was adapted to reflect the special provisions and requirements prohibiting variable remuneration. It remains in place as a target-based system, but its variable remuneration component is still suspended. As a result, it was once again impossible to fully take into account the regulatory requirements derived among other things from the Institutsvergütungsverordnung (InstitutsVergV – Remuneration Regulation for Institutions) and governing, for example, the long-term nature of remuneration, its sustainability and an appropriate management and incentive effect. In cooperation with employee representatives, a functional bonus was introduced in 2011 in order to maintain the Company's operational capacity to act. However, this is well below the variable remuneration originally planned, both in the aggregate and in the individual cases. The bonus was agreed with both the Supervisory Board and the owner. The remuneration system will be reviewed in 2014 for any potential adjustments made necessary by the InstitutsVergV, which entered into force as at 1 January 2014. Any adjustments required as a result, including with respect to the currently suspended provisions, will be addressed in further implementation measures.

Remuneration Committee

In 2013, pbb's Remuneration Committee comprised representatives from the sales units and Human Resources, Treasury, Portfolio Administration, Risk Management & Control, Board Office/Compliance and Finance, as well as a representative from the Internal Audit division (non-voting member). The Remuneration Committee is chaired by the CFO/COO, who is also responsible for Human Resources.

pbb's Remuneration Committee held a total of five regular meetings in 2013. It primarily discussed the remuneration principles in connection with the 2013 pay round, taking into account the statutory and regulatory requirements, the implementation of the risk analysis and the development of a proposal for identifying functions with a material influence on the Bank's risk profile («risk takers») in accordance with section 5 of the InstitutsVergV, as well as the preparation of the remuneration report for financial year 2012.

The risk analysis and the process of identifying risk taker functions were expanded in 2013. They are already largely based on the criteria published by the European Banking Authority (EBA) in connection with the implementation of the consultation paper on draft regulatory technical standards (EBA/CP/2013/11).

A total of 124 employees were identified as risk takers. pbb's Management Board approved the Remuneration Committee's proposal and adopted the corresponding resolution.

Sustainability

Companies have a responsibility for the environment in which they operate – towards their employees, their customers and investors, to society and for the environment. For pbb Group, this responsibility is known as corporate responsibility.

Responsible corporate management takes into account all aspects of corporate responsibility and sets the highest standards for corporate activity. In pbb Group, sustainability is the guiding principle behind corporate responsibility. We act responsibly, have a long-term focus and are aware of the consequences for all of the Company's stakeholders and for the environment.

Employees

The Bank's employees are the critical factor behind its success. pbb Group employs men and women from a wide range of nationalities and specialist backgrounds. Particular emphasis is placed on diversity.

This employee diversity is a valuable asset which the Group promotes by encouraging specialist, professional and personal development. How staff should behave towards each other and in their professional dealings with third parties are laid down in a code of conduct.

Customers and Investors

As a specialist bank, pbb finances professional real estate investors' projects and public sector infrastructure projects. pbb applies high standards to lending operations in both of these areas. Priority is given to financing buildings which meet sustainability criteria, and to supporting the public sector in its task of providing public infrastructure projects.

The Management Board of the Company, that is wholly owned indirectly by the Federal Republic of Germany, has resolved to use the Public Corporate Governance Code of the federal government, which is based on the «comply or explain» principle, subject to identical resolution by the Supervisory Board. The Public Corporate Governance Code of the federal government reflects current international developments in, and standards of, corporate governance.

Social Responsibility

pbb Group currently channels its corporate social responsibility activities through its two charitable foundations, the pbb Stiftung Deutsche Pfandbriefbank and the pbb Stiftung für Kunst und Wissenschaft. The foundations are based in Munich and are independently funded; their capital is ring-fenced from the Bank and is used exclusively to fulfil the foundations' purpose.

> pbb Stiftung Deutsche Pfandbriefbank supports projects which promote art and culture, targeting support particularly towards the next generation of artists. It also promotes higher architectural standards for commercial buildings in Germany by sponsoring a highly regarded national architecture prize, for aesthetically and ecologically outstanding commercial buildings.
> pbb Stiftung für Kunst und Wissenschaft was established in 1968 by Württembergische Hypothekenbank and focuses on promoting intellectual and artistic activity in Baden-Württemberg, in particular writing, painting, sculpture, music, theatre, architecture and design, and regional and cultural studies.

pbb Group complements these primarily cultural and academic activities with a commitment to social action. It supports the St. Nikolaus children's hospice in the Allgäu region, a rest and recuperation centre for families with chronically or terminally ill children. In addition, the Group focuses on supporting projects which either have a local connection with the Company or where employees are already involved on a voluntary basis. One example is the JugendKulturHaus Gleis 1 youth centre in Unterschleissheim, where the Group's head office is located. The Company started supporting this in 2013, in the form of a new mobile youth work project. pbb Group also supports its employees' personal commitment to a number of other social projects.

pbb Group has also made its historic collection of Württemberg paper money available on permanent loan to the HVB Stiftung Geldscheinsammlung, HypoVereinsbank's banknote collection foundation. The pbb collection comprises some 8,000 notes from every period in Württemberg's banking history and is considered to be the largest and most important special collection of Württemberg paper currency. Transferring pbb Group's collection to HVB Stiftung Geldscheinsammlung means the collection can remain intact and makes it accessible to interested members of the public.

Environment

As a financial services provider, pbb Group places great importance on the responsible use of resources, both internally within the Group and by manufacturers supplying it.

The Group's head offices in Unterschleissheim near Munich are very energy-efficient. The building's entire electricity requirements have been met from renewable energy sources since 2011. Workflows have been designed to save paper, and only paper certified as environmentally friendly is used. Protecting the environment is always a consideration with business trips, too, which is why pbb Group encourages its staff to travel by train within Germany. In fact, this is mandatory for travel between the Company's sites in Munich/Unterschleissheim and Frankfurt/Eschborn. Installing extensive video conferencing facilities has reduced business travel overall. In keeping with the principle of environmental compatibility, Company vehicles must comply with regulations on CO_2 emissions. Vehicles exceeding these amounts are subject to a financial penalty or may not be purchased. All of the Bank's hardware meets the Green IT label criteria.

Corporate Responsibility Ratings

Institutional investors and financial services providers are increasingly factoring independent corporate responsibility ratings into their decisions to invest in particular issuers. pbb Group currently meets these investor requirements with two corporate responsibility ratings from oekom and imug.

oekom currently rates pbb Group as «prime». It awards this status to companies that are classified as sector leaders under the oekom corporate rating system and that meet sector-specific minimum standards. Of the around 3,000 companies regularly evaluated by oekom, around 550 currently belong to the oekom «prime universe».

pbb's debt instruments are rated by imug. In 2013, pbb's public sector Pfandbriefe were given an above-average «positive» rating. Its mortgage Pfandbriefe and unsecured bonds were rated as «neutral», or average. Currently, imug regularly analyses and issues ratings for around 70 German and European bank bond issuers and covered bonds.

Report on Economic Position

Macroeconomic Environment

The global economy grew by 2.2% in 2013 (2012: 2.4%). Real GDP in the eurozone slowed by only 0.4% during the year (2012: –0.7%).

While Germany saw slight growth of 0.4%, it remained down on the figure for 2012 (0.7%). In France, real GDP was on a level with the previous year at 0.3%, while the United Kingdom recorded economic growth of 1.4% (2012: 0.2%). The decline in economic output in Italy (–1.8%), Spain (–1.3%) and Portugal (–1.8%) slowed year-on-year. In 2013, the Nordic countries ranged from near stagnation to growth of 2% year-on-year. Eastern Europe showed a mixed picture, where in particular Poland performed well.

Interest rates were kept extremely low in all of pbb Group's core markets in order to boost the economy. At the end of 2013, the European Central Bank's key interest rate was at a historic low of 0.25% (2012: 0.75%). This was primarily due to the extremely low level of inflation in the eurozone.

Debt levels in the eurozone continued to rise in 2013. However, net new debt continues to decline, thanks mainly to the consolidation efforts being undertaken by many European countries in the hope of stabilising their public-sector finances.

At the 2013 year end, the euro had appreciated compared with 31 December 2012 against pbb Group's main foreign currencies. The gain against the Japanese yen was particularly significant. The euro also rose to a lesser extent against the US dollar, sterling and the Swedish krona.

Sources: Eurostat, Statistisches Bundesamt, ECB, IMF

Sector-specific Environment

Overall Situation in the Banking Sector

Tensions on the international financial markets eased in 2013. The wide variety of measures taken by politicians and central banks contained the systemic disruptions caused by the European sovereign debt crisis. However, the crisis is not yet over.

Banks' earnings situations were significantly impacted by the extremely low interest rates. In addition, the new regulatory requirements meant that credit institutions had to re-evaluate which business activities will still be attractive in future in terms of profitability, costs, equity and liquidity. The main focus here was on the implementation of the Basel III reform package. It will be implemented in the EU via a recast Capital Requirements Directive (CRD) and will take effect successively starting from 2014. The plan to transfer supervision of the systemically relevant eurozone banks to the ECB also involved considerable effort for the banks involved. In addition, new accounting standards and reporting requirements made business more complex.

The general public remained extremely critical of the banking sector, due in particular to the investigations and prosecutions relating to a wide variety of issues.

Real Estate Finance

The trend of investing in real estate continued undiminished in 2013 boosted in particular by continued low interest rates. The investment volume was up significantly year-on-year, reaching a high not seen since 2007. Demand considerably outpaced the supply of high-quality properties in central locations in Central and Northern European countries, which significantly raised prices. In turn, investment in properties below premium level increased as a way to avoid this trend.

In Germany, the majority of transactions were attributable to the large metropolitan areas. Supply in the United Kingdom – particularly that of high-quality properties and in central locations – became scarce. In France, the future economic development will be a key factor. The current increase in vacancy levels in second-class office properties is a sign of market uncertainty.

The increased transaction volume boosted new business for real estate finance providers, which was up considerably year-on-year. German Pfandbrief banks saw considerable momentum from the office property market. The financing business in other submarkets also performed well.

Sources: CBRE research, Verband deutscher Pfandbriefbanken

Public Sector Finance

The ECB's announcement in September 2013 of a plan to implement an OMT (outright monetary transactions) programme significantly reduced volatility on the eurozone financial markets. As a result, the situation on all segments of the municipal financing market has largely normalised. In addition, countries that had been badly affected by the crisis in public finances saw the first promising developments: Ireland exited the European rescue facility and returned to the capital market. Rating agencies are also taking a less critical stance on the trend in Spanish public finances.

The financing provided by retail banks and development banks for municipal financing was sufficient to fund the majority of relevant municipal investment projects, particularly in the countries less affected by the sovereign debt crisis. Nevertheless, the financing banks and investors continued to hold a critical view of the financial situation in the focus countries, including at sub-sovereign level. The resulting differences in the credit quality assessments for municipalities and local authorities continued in the course of the year.

In Germany, there was sufficient market demand for finance, although extremely long-term loans remained popular and were granted at very low margins by local competitors (primarily public sector and development banks). As a result, the traditional public investment finance market was extremely challenging for other providers. Competition picked up again on the French market, which was reflected in deteriorating margins.

In the Northern European countries, it was possible to enter into transactions with a high credit quality and attractive risk-return profiles. This was mainly due to the withdrawal of, or discontinuation of, business activities by other international competitors and the withdrawal of local banks.

In budget financing, risk premium trends varied widely in individual countries. In Germany and France, premiums on the secondary market edged up slightly from their record lows in the course of 2013. In Italy, Spain and Portugal, risk premiums declined, continuing the fall away from their record highs.

Funding Markets

In 2013, capital markets were dominated by the low interest rate environment, expansionary monetary policy and uncertainty as to how the central banks planned to proceed.

At the beginning of 2013, the positive sentiment seen in the previous year initially continued. Many investors changed their focus given the historically low interest rate environment, taking on higher risk to achieve higher yields. This led to increased demand for unsecured bonds and securities from the periphery of Europe. In the summer, worries about overcoming the sovereign debt crisis resurfaced after Cyprus was bailed out, increasing market volatility. Pfandbriefe remained attractive for investors and the risk premiums for securities placed on the primary market improved again. Fifteen-year bonds were issued for the first time since the crisis, making long-term issues possible again.

Initial speculation about when tapering of the expansionary monetary policy would start led to an increase in long-term interest rates in the third quarter 2013 and made investors cautious. Since then, the markets have been dominated by uncertainty regarding the possibility of central banks ending their support measures. However, the debate on the budget deficit and the associated temporary shutdown of selected parts of the administration in the USA forced the Federal Reserve to continue its expansionary monetary policy. In the eurozone, the mixed performance by countries and emerging deflationary tendencies in fact caused the ECB to expand the liquidity supply even further by lowering interest rates in November 2013.

This liquidity situation made it easier for credit institutions to obtain funding and led to a significant decline in risk premiums for Pfandbriefe and unsecured bonds. Smaller private placements of borrowers' note loans were also well received by German investors.

Course of Business

In financial year 2013, the Management Board aligned pbb Group with its target positioning as a specialist European Pfandbrief bank. Among other things, pbb Group's ability to penetrate the relevant markets was enhanced, allowing it to significantly increase its volume of new business year-on-year. At the same time, underlying general administrative expenses were heavily reduced as against 2012. This development had a positive effect on the result. At € 165 million, pre-tax profit met the forecast, which was lifted to at least € 150 million on 8 October 2013. This figure was also boosted by positive one-off factors. As a result, the return on equity after taxes of 4.9% was also above the projected figure of 2.1%.

Operating revenues exceeded the prior-year level at €482 million. Increased net interest income of € 319 million had a positive effect. This was above the prior-year figure and within the forecast range. One reason for this was the higher volume of new business. This generated margins that were above the previous year and higher than those of the existing portfolio. At €8.2 billion, the volume of new business was in line with pbb Group's forecast that it would significantly exceed the 2012 figure of €5.6 billion. The services provided to FMS Wertmanagement were largely discontinued on 30 September 2013 as mandated by the European Commission, which meant that no material income was generated from these services in the fourth quarter of 2013. Offsetting one-off factors also impacted operating revenues. The sale of Little Britain Holdings (Jersey) Ltd., which was primarily a vehicle for a successfully restructured property, resulted in income of €92 million in net income from financial investments. This positive effect was partly offset by an expense of €–55 million in net trading income arising from the first-time use of overnight yield curves to measure derivatives and from the optimisation of the derivatives portfolio.

Following the implementation of pbb Group's target model and the discontinuation of the services provided to FMS Wertmanagement at the end of September 2013, general administrative expenses decreased in line with expectations. However, dissynergies and fixed costs mean that this reduction in general administrative expenses has not allowed the decline in corresponding income to be completely offset to date. Overall, the cost-income ratio improved as expected to 64.7%, as general administrative expenses decreased in the fourth quarter of 2013 in particular and operating revenues rose.

Provisions for losses on loans and advances increased year-on-year. However, they remained at a low level and hence below the forecast, which predicted a normalised level with respect to the lending business. This reflected the successful restructurings of non-performing loans and the healthy market situation.

The risk-bearing capacity was ensured at all times in financial year 2013, from both a going-concern and gone-concern perspective. The CET1 capital ratio did not decrease as expected, but rose to 17.6%. The ratio was thus significantly higher than the 11% aimed for by pbb Group. This increase was mainly due to lower risk assets. The Tier 1 capital ratio, calculated on a pro forma basis, also rose due to lower risk assets compared with the previous year, and amounted to 20.1%. Risk-weighted assets decreased particularly as a result of repayments and redemptions, changes in the loss-given default (LGD) and changes in the derivatives portfolio. The main offsetting effects were new business and the first full application of the Advanced Internal Ratings-Based Approach (Advanced IRBA) as at 31 December 2013 regarding the use of the Advanced IRBA portfolio requested.

Development in Earnings

pbb Group

Pre-tax profit was up significantly on the prior-year level, at € 165 million. A detailed comparison of the results in 2013 and those for the previous year is given below:

Key financials pbb Group		2013	2012	△ in € million
Operating performance				
Operating revenues	in € million	482	467	15
Net interest income and similar income	in € million	319	296	23
Net commission income	in € million	9	23	–14
Net trading income	in € million	–51	10	–61
Net income from financial investments	in € million	96	13	83
Net income from hedge relationships	in € million	9	–6	15
Balance of other operating income/expenses	in € million	100	131	–31
Provisions for losses on loans and advances	in € million	–8	4	–12
General administrative expenses	in € million	–312	–341	29
Balance of other income/expenses	in € million	3	–6	9
Pre-tax profit/loss	in € million	165	124	41
Income taxes	in € million	–5	–55	50
Net profit/loss	in € million	160	69	91
Key ratios				
Cost-income ratio	in %	64.7	73.0	
Return on equity before taxes	in %	5.0	3.8	
Return on equity after taxes	in %	4.9	2.1	

Operating Revenues Operating revenues amounted to € 482 million (2012: € 467 million). The deconsolidation of Little Britain Holdings (Jersey), which was sold in September 2013, resulted in a significant positive effect of € 92 million. By contrast, the first-time use of overnight yield curves to measure derivatives and the optimisation of derivative holdings had a negative effect of €–55 million overall.

Net interest income exceeded the prior-year figure at € 319 million (2012: € 296 million). New business was a key driver, with margins being higher than in the existing portfolio. One-off factors primarily resulted from repayments of receivables. At €27 million, one-off factors were higher than in the previous year (2012: €17 million). Market interest rates, which continued to fall in financial year 2013, reduced the earnings contributions to net interest income made by own funds not invested for the long term.

Net commission income amounted to € 9 million (2012: € 23 million). A key reason for the decline was lower fees from the lending and other services business. pbb Group generates commission income from fees that are only recognised when transactions expire, among other things. This fee income declined year-on-year.

Net trading income stood at €–51 million in the reporting period, after amounting to € 10 million in 2012. The first-time use of overnight yield curves (including tenor basis effects) to value derivatives in 2013 resulted in a first-time application effect of €–33 million. The accounting-related change in the estimate was made as a result of changes in market conventions. An additional expense of €–22 million was due to the optimisation of the derivatives portfolio. The subsequent measurement of derivatives taking into account the bilateral credit value adjustment, i.e. the credit risk of the counterparty concerned and of pbb Group, led to an effect of €7 million (2012: €7 million).

A large majority of the net income from financial investments of €96 million (2012: €13 million) – €92 million – was attributable to income from the deconsolidation of Little Britain Holdings (Jersey) Ltd., which was sold in September 2013. The company was primarily a vehicle for a building that had been successfully restructured by pbb Group. Additional income of €4 million (2012: €20 million) was attributable to securities that were sold as part of the adjustment of the liquidity portfolio. This income was partly offset by net expenses of €–1 million (2012: €–6 million) for the recognition of portfolio-based allowances for securities in the LaR measurement category. Changes in the risk assessment for securities from certain European regions were the main reason for the addition to the portfolio-based allowances.

Net income from hedge relationships amounted to €9 million (2012: €–6 million) and predominantly resulted from hedge inefficiencies of micro (fair value) hedges. The latter were dedesignated when overnight yield curves were used for the first time to measure derivatives in 2013, and then redesignated including the overnight interest rate component. Both the hedging instrument and the hedged item are measured on the basis of overnight yield curves. Measurement does not result in any additional hedge inefficiencies in connection with dedesignation and redesignation. As the last dFVTPL financial instrument matured in financial year 2013, pbb Group did not have any further dFVTPL holdings as at 31 December 2013.

The balance of other operating income/expenses decreased to €100 million in 2013 (2012: €131 million). This was mainly due to the discontinuation to a large extent of the services provided for the FMS Wertmanagement portfolio as mandated by the European Commission on 30 September 2013. These services resulted in income of €60 million in 2013 (2012: €106 million). The corresponding general administrative expenses were also lower than in the previous year, as the headcount was reduced and less office space had to be rented. Net income of €36 million was generated by IT services provided to our fellow subsidiary DEPFA (2012: €40 million). Additional income was attributable to real estate rental income in the amount of €11 million (2012: €7 million). The bank levy impacted the balance of other operating income/expenses by €–11 million (2012: €–24 million). Net gains from currency translation were below €1 million (2012: net gains of €3 million).

Provisions for Losses on Loans and Advances A net amount of €–8 million was added to provisions for losses on loans and advances in 2013 (2012: net reversals of €4 million). The low need for additions reflected the healthy situation on the markets in which pbb Group is active. pbb Group also benefited from the successful restructurings of non-performing loans. This positive trend also led to a decline in problem loans, which decreased from €1.1 billion as at 31 December 2012 to €0.9 billion as at the end of 2013.

Net additions to individual allowances decreased to €–8 million in 2013, after €–23 million in the previous year. Additions to individual allowances were only necessary in a small number of individual cases and were largely offset by reversals of individual allowances. As in the previous year, no specific provisions had to be established for public sector financing, including exposures to focus countries.

Portfolio-based allowances are only established for receivables for which no indication of an individual impairment has been determined. In the reporting period, a net amount of €–9 million was added to portfolio-based allowances (2012: net reversals of €22 million); this was primarily attributable to changes in the risk assessment for individual focus countries.

In addition, provisions for contingent liabilities and other obligations in the amount of € 1 million (2012: € 4 million net) were reversed due to the conclusion of legal proceedings. Recovery payments of € 8 million (2012: € 1 million) were recognised in profit or loss on receivables previously written off.

General Administrative Expenses General administrative expenses improved considerably to €–312 million in 2013 (2012: €–341 million). This reflects the successes of the restructuring measures implemented by pbb Group in recent years. The transfer of pbb Group employees to FMS Wertmanagement Service GmbH also contributed to the positive change in general administrative expenses from the fourth quarter of 2013. Overall, personnel expenses improved by € 10 million to €–121 million (2012: €–131 million). Non-personnel expenses were reduced to €–191 million (2012: €–210 million) particularly as a result of lower consulting and IT expenses. Since general administrative expenses decreased and operating revenues increased, the cost-income ratio improved to 64.7 % (2012: 73.0 %).

Balance of Other Income/Expenses The balance of other income/expenses in the amount of € 3 million (2012: €–6 million) resulted from changes in the restructuring provisions, which were the result of updates following validations of the parameters included in the calculation, and from expenses for other taxes.

Pre-tax Profit/Loss Pre-tax profit amounted to €165 million (2012: €124 million). The return on equity before taxes was 5.0 % (2012: 3.8 %).

Income Taxes Income of € 2 million from current taxes (2012: € 8 million) and a deferred tax expense of €–7 million (2012: €–63 million) resulted in a total tax expense of €–5 million (2012: €–55 million).

Net Profit/Loss pbb Group's net profit was € 160 million (2012: €69 million). The return on equity after taxes amounted to 4.9 % (2012: 2.1 %).

Real Estate Finance (REF) Operating Segment

Key financials Real Estate Finance		**2013**	**2012**	△ in € million
Operating performance				
Operating revenues	in € million	334	264	70
Net interest income and similar income	in € million	240	227	13
Net commission income	in € million	10	25	–15
Net trading income	in € million	–21	2	–23
Net income from financial investments	in € million	96	16	80
Net income from hedge relationships	in € million	4	–3	7
Balance of other operating income/expenses	in € million	5	–3	8
Provisions for losses on loans and advances	in € million	–1	5	–6
General administrative expenses	in € million	–147	–139	–8
Balance of other income/expenses	in € million	2	–3	5
Pre-tax profit/loss	in € million	188	127	61
Key ratio				
Cost-income ratio	in %	44.0	52.7	

The Real Estate Finance operating segment comprises all of pbb Group's real estate financing arrangements. As forecast at the beginning of the year, the Real Estate Finance (REF) segment accounted for the bulk of consolidated profit. The segment's pre-tax profit of € 188 million exceeded the prior-year figure (2012: € 127 million) due to the non-recurring income reported in net income from financial investments from the sale of Little Britain Holdings (Jersey) Ltd., which was primarily a vehicle for a successfully restructured property.

At € 7.0 billion, the volume of new business including prolongations with maturities of more than one year surpassed the prior-year figure (€ 4.9 billion), as expected. New business margins in 2013 were higher than both the prior-year figures and the margins in the existing portfolio. Overall, this trend highlights the attractiveness of the real estate financing market.

Operating Revenues Operating revenues rose to € 334 million (2012: € 264 million), which was attributable to the non-recurring income in net income from financial investments. Without this positive special factor and the negative market-related measurement effects in net trading income, operating revenues would have been at the prior-year level. Net interest income of € 240 million (2012: € 227 million) benefited from the high new business margins, which lifted the profitability of the entire portfolio. Net interest income was also boosted by higher one-off factors, primarily arising from redemptions of liabilities prior to maturity and prepayment penalties. Net commission income amounted to € 10 million (2012: € 25 million). Income from fees that are only recognised under certain conditions when transactions expire declined year-on-year. Net trading income was negative at €–21 million (2012: € 2 million) due to the first-time use of overnight yield curves (including tenor basis effects) to measure derivatives and to the optimisation of the derivatives portfolio. The main item contained in the net income from financial investments of € 96 million (2012: € 16 million) is the income from the sale of Little Britain Holdings (Jersey) Ltd. This sale is an example of the successful restructuring of non-performing exposures. Net income from hedge relationships of € 4 million (2012: €–3 million) resulted from hedge inefficiencies within the range permitted by IAS 39. The balance of other operating income/expenses was slightly positive, at € 5 million (2012: €–3 million). The expenses allocated to the segment for the bank levy (2013: €–5 million; 2012: €–9 million) were more than offset by rental income.

Provisions for Losses on Loans and Advances Additions and reversals, both of which related to a small number of individual cases only, largely cancelled each other out in the provisions for losses on loans and advances item. In total, additions of €–1 million net were made (2012: net reversal of €5 million). Net additions of €–8 million were made to individual allowances (2012: €–24 million), resulting from a small number of individual cases. A net amount of €–2 million was added to portfolio-based allowances (2012: net reversal of €26 million). These additions were offset by recoveries from written-off loans and advances in the amount of €8 million (2012: €1 million) and reversals of provisions for contingent liabilities and other commitments of €1 million (2012: €2 million).

General Administrative Expenses At €–147 million, general administrative expenses increased compared with the previous year (2012: €–139 million). This reflected additional expenses to strengthen pbb Group's sales units. The cost-income ratio was 44.0% (2012: 52.7%).

Public Sector Finance (PSF) Operating Segment

Key financials **Public Sector Finance**		**2013**	**2012**	**Δ in € million**
Operating performance				
Operating revenues	in € million	28	47	–19
Net interest income and similar income	in € million	62	58	4
Net commission income	in € million	–	–1	1
Net trading income	in € million	–30	8	–38
Net income from financial investments	in € million	–	–2	2
Net income from hedge relationships	in € million	5	–3	8
Balance of other operating income/expenses	in € million	–9	–13	4
Provisions for losses on loans and advances	in € million	–7	–4	–3
General administrative expenses	in € million	–54	–53	–1
Balance of other income/expenses	in € million	1	–1	2
Pre-tax profit/loss	in € million	–32	–11	–21
Key ratio				
Cost-income ratio	in %	>100.0	>100.0	

The Public Sector Finance (PSF) operating segment comprises public sector financing arrangements. The segment includes the public investment finance arrangements in which pbb Group conducts new business, and expiring budget financing. Contrary to expectations, the segment recorded a loss before tax due to negative effects in net trading income arising from the first-time use of overnight yield curves to measure derivatives and from the optimisation of the derivatives portfolio. Without these measurement effects, the result would have been slightly positive, as expected. At €–32 million, the loss was larger than in the previous year as a result of the measurement effects in net trading income (2012: loss of €–11 million).

New public investment finance business within the PSF segment significantly exceeded the prior-year figure of €0.7 billion, at €1.2 billion, thus meeting the forecast. As in the previous year, the new business margins were higher than the average margins in the existing portfolio, allowing pbb Group to increase the profitability of the portfolio. This development highlights the opportunities for pbb Group in public investment finance.

Operating Revenues In the operating revenues item, the positive change in the current net interest income and net commission income items contrasted with the expenses from derivative measurement. Overall, operating revenues amounted to €28 million, lower than the prior-year level (2012: €47 million). Net interest income rose from €58 million in the previous year to €62 million. One reason for this was the increased profitability of the public investment finance portfolio as a result of the positive trend in new business margins. Net interest income also benefited from higher one-off factors, primarily from redemptions of liabilities prior to maturity and prepayment penalties. The commission business plays a subordinate role in the PSF segment, with commission income and expenses balancing each other out (2012: net commission income of €–1 million). The net trading income of €–30 million (2012: €8 million) was impacted by the first-time use of overnight yield curves (including tenor basis effects) to measure derivatives and by the optimisation of the derivatives portfolio. In the previous year, the measurement of the hedged derivatives (including counterparty credit risk and the Bank's own credit risk) had a positive effect. Income and expense from financial investments balanced each other out (2012: net income from financial investments of €–2 million). In the previous year, this item resulted primarily from additions to portfolio-based allowances for securities in the LaR measurement category that were issued by focus countries. Net income from hedge relationships (2013: €5 million; 2012: €–3 million) resulted from hedge inefficiencies of micro (fair value) hedges. The balance of other operating income/expenses was negative in financial year 2013 at €–9 million (2012: €–13 million); this was mainly attributable to the expenses for the bank levy allocated to the segment (2013: €–6 million; 2012: €–15 million).

Provisions for Losses on Loans and Advances As in the previous year, no additions to individual allowances were required in respect of public issuers, as there were no objective indications of impairment within the meaning of IAS 39.59. A net amount of €–7 million was added to portfolio-based allowances as a result of changes in the risk assessment for individual focus countries (2012: €–4 million).

General Administrative Expenses At €–54 million, general administrative expenses were at the prior-year level (2012: €–53 million). Since general administrative expenses exceeded operating revenues as in the previous year, the cost-income ratio remained unchanged at over 100.0%.

Value Portfolio (VP) Operating Segment

Key financials Value Portfolio		2013	2012	△ in € million
Operating performance				
Operating revenues	in € million	102	147	–45
Net interest income and similar income	in € million	–	1	–1
Net commission income	in € million	–	–1	1
Net trading income	in € million	–	–	–
Net income from financial investments	in € million	–	–1	1
Net income from hedge relationships	in € million	–	–	–
Balance of other operating income/expenses	in € million	102	148	–46
Provisions for losses on loans and advances	in € million	–	3	–3
General administrative expenses	in € million	–111	–148	37
Balance of other income/expenses	in € million	–	–2	2
Pre-tax profit/loss	in € million	–9	–	–9
Key ratio				
Cost-income ratio	in %	>100.0	>100.0	

The Value Portfolio operating segment mainly comprises income and expenses arising from the services provided for the FMS Wertmanagement portfolio until the end of September 2013 and from IT services provided to fellow subsidiary DEPFA. The segment also comprises non-strategic portfolios, such as selected structured products. Contrary to the expectations at the start of the year, the segment result in 2013 was not slightly positive, but rather negative, at €–9 million.

Operating Revenues In the reporting period, income was reported only in the balance of other operating income/expenses item. All other operating revenues items amounted to €0 million. The main item contained in the balance of other operating income/expenses is the income from the services provided to FMS Wertmanagement. This income declined from € 106 million in 2012 to €60 million in the reporting period, as the services were essentially no longer provided in the fourth quarter of 2013, as mandated by the European Commission. The second significant item contained in the balance of other operating income/expenses is the income from the IT services provided to DEPFA, which declined year-on-year to €36 million (2012: €40 million).

Provisions for Losses on Loans and Advances No additions to or reversals of provisions for losses on loans and advances were necessary in the 2013 reporting period (2012: reversals of €3 million).

General Administrative Expenses General administrative expenses were considerably lower than in the previous year, at €–111 million (2012: €–148 million). This was due to the discontinuation of the services provided to FMS Wertmanagement at the end of September 2013, which also involved a transfer of pbb Group employees to FMS Wertmanagement Service GmbH. Since general administrative expenses exceeded operating revenues, the cost-income ratio remained at over 100.0%, as in the previous year.

Consolidation & Adjustments

Key financials Consolidation & Adjustments		**2013**	**2012**	△ in € million
Operating performance				
Operating revenues	in € million	18	9	9
Net interest income and similar income	in € million	17	10	7
Net commission income	in € million	–1	–	–1
Net trading income	in € million	–	–	–
Net income from financial investments	in € million	–	–	–
Net income from hedge relationships	in € million	–	–	–
Balance of other operating income/expenses	in € million	2	–1	3
Provisions for losses on loans and advances	in € million	–	–	–
General administrative expenses	in € million	–	–1	1
Balance of other income/expenses	in € million	–	–	–
Pre-tax profit/loss	in € million	18	8	10

Consolidation & Adjustments reconciles the aggregate segment results to the consolidated result. Alongside consolidation adjustments, this item contains certain expenses and income that do not fall within the operating segments' areas of responsibility.

Pre-tax profit in the Consolidation & Adjustments segment was positive, at € 18 million (2012: € 8 million). Net interest income arose predominantly from the investment of equity not allocated to the segments.

Development in Assets

Assets in € million	31.12.2013	31.12.2012[1]	Δ in € million
Cash reserve	3,532	1,937	1,595
Trading assets	1,642	3,325	−1,683
Loans and advances to other banks	5,798	7,995	−2,197
Loans and advances to customers	36,242	49,590	−13,348
Allowances for losses on loans and advances	−148	−325	177
Financial investments	20,892	25,572	−4,680
Property, plant and equipment	1	2	−1
Intangible assets	31	39	−8
Other assets	4,769	7,242	−2,473
Income tax assets	1,165	1,704	−539
Current tax assets	44	53	−9
Deferred tax assets	1,121	1,651	−530
Total assets	**73,924**	**97,081**	**−23,157**

[1] Adjusted due to the retrospective initial application of IAS 19 (revised). Details are given in the note entitled Principles in the notes to the consolidated financial statements

General Development in Assets

pbb Group's total assets as at the balance sheet date amounted to €73.9 billion, down €23.2 billion or 23.9% on the previous year-end (2012: €97.1 billion). The nominal volume of the strategic portfolios of real estate finance paid out and public investment finance paid out also declined lightly (€27.6 billion; 2012: €29.8 billion). Although new business completely offset scheduled and early repayments in the strategic portfolios, the portfolio volume decreased overall due to commitments not completely paid out and currency effects.

The decline in total assets mainly resulted from the repayment of the three-year tender, the transfer of mortgage loans to FMS Wertmanagement and their derecognition from the balance sheet, as well as the strategic reduction of the non-strategic portfolio.

The liquidity of €4.0 billion that was raised in December 2011 and February 2012 under the three-year tender was repaid in full at the first possible opportunities in January and February 2013.

Mortgage loans were synthetically transferred to FMS Wertmanagement with effect from 1 October 2010 to transfer the economic risk, but remained in pbb's cover pool on the balance sheet. The obligation to transfer the resulting cash flows gave rise to a liability to FMS Wertmanagement in the same amount. These loans were transferred to FMS Wertmanagement and derecognised from the balance sheet in August 2013, at which point they had a carrying amount of €6.4 billion (2012: €7.5 billion). As a result, the loans and advances to customers and other liabilities balance sheet items declined.

The other effects arising from the transfer to FMS Wertmanagement continued to decrease in financial year 2013 and are now of only minor importance. For example, holdings of positive fair values of back-to-back derivatives were almost completely liquidated through novations (2012: €1.0 billion). pbb Group no longer holds any securities issued by FMS Wertmanagement, since these have matured. This decreased total assets by €2.2 billion as against 31 December 2012.

Since 16 September 2013, pbb Group has no longer invested excess liquidity for FMS Wertmanagement with the central bank (2012: € 0.5 billion). This resulted in a corresponding reduction in the loans and advances to other banks and liabilities to customers' balance sheet items.

The nominal volume of the non-strategic budget financing portfolios decreased by € 4.9 billion to € 22.8 billion as a result of repayments (2012: € 27.7 billion).

pbb Group further reduced its country exposure to Italy and Portugal in 2013. Its exposure to Spain increased due to the purchase of liquid government bonds with short maturities to top up the public sector cover pool. The Bank had no exposure to Greece, Ireland or Cyprus as at 31 December 2013. The changes and a definition are given in the note Exposure to Selected European Countries.

Total Assets Covenants

As at the balance sheet date, pbb Group complied with all total assets covenants that were imposed by the European Commission in connection with the approval of state aid. Because certain offsetting effects attributable to the transfer of selected positions to FMS Wertmanagement no longer exist, the adjusted total assets as at 31 December 2013 of € 73.9 billion (2012: € 95.4 billion) corresponded to total assets in accordance with IFRSs for the first time and were thus lower than the prescribed upper limit of € 105.0 billion (2012: € 105.0 billion). At € 50.9 billion (2012: € 59.8 billion), strategic total assets – which have been additionally adjusted by the non-strategic public sector financing portfolio – also did not exceed the prescribed upper limit of € 75.0 billion (2012: € 71.0 billion).

Investments

The purpose of pbb Group is to conduct banking business, particularly lending business. Capital expenditures on property, plant and equipment and intangible assets are of relatively minor significance. Nevertheless, pbb Group did invest in these areas in 2013 as well. The IT systems were separated from those at FMS Wertmanagement as part of a project in 2013, which had a negative effect on the Value Portfolio segment's result. The separation from fellow subsidiary DEPFA was also driven forward. Additions of purchased and internally generated software amounted to € 5 million in the reporting period (2012: € 18 million).

pbb Group acquires financial investments primarily for portfolio optimisation, for example to invest liquidity positions and own funds.

Development in Financial Position

Equity and liabilities in € million	31.12.2013	31.12.2012[1]	Δ in € million
Liabilities to other banks	3,522	7,797	−4,275
Liabilities to customers	10,848	11,895	−1,047
Liabilities evidenced by certificates	47,060	52,550	−5,490
Trading liabilities	1,453	3,192	−1,739
Provisions	209	235	−26
Other liabilities	4,722	14,438	−9,716
Income tax liabilities	1,190	1,698	−508
Current tax liabilities	64	64	–
Deferred tax liabilities	1,126	1,634	−508
Subordinated capital	1,440	1,993	−553
Financial liabilities	**70,444**	**93,798**	**−23,354**
Financial equity	**3,480**	**3,283**	**197**
Total equity and liabilities	**73,924**	**97,081**	**−23,157**

[1] Adjusted due to the retrospective initial application of IAS 19 (revised). Details are given in the note entitled Principles in the notes to the consolidated financial statements

Liabilities

Total Group liabilities as at 31 December 2013 amounted to €70.4 billion, after €93.8 billion at the prior-year reporting date. As for the assets side of the balance sheet, the decline mainly resulted from the transfer of mortgage loans to FMS Wertmanagement that were derecognised from the balance sheet, and the repayment of the three-year tender.

The lower funding requirement resulted in decreased holdings of balance sheet liabilities due to the strategic reduction of certain portfolios on the assets side.

Subordinated capital declined to €1.4 billion as at the balance sheet date due to maturities (2012: €2.0 billion).

Market-related effects increased total equity and liabilities, as the fair values of derivatives and of the hedged items measured at fair value rose in fair value hedge accounting, primarily due to lower long-term interest rates. By contrast, the rise in the euro against the US dollar, sterling, the Japanese yen, the Swiss franc and the Swedish krona led to a reduction in total equity and liabilities.

The ratio of secured liabilities to total liabilities was 64.3% (2012: 63.8%).

Capital

Development of Financial Equity The equity attributable to shareholders changed as follows:

Financial position equity in accordance with IFRS in € million	31.12.2013	31.12.2012[1]	Δ in € million
Equity attributable to shareholders	**3,480**	**3,283**	**197**
Subscribed capital	380	380	–
Silent participation	999	999	–
Additional paid-in capital	5,036	5,036	–
Retained earnings	−3,097	−3,166	69
Profits/losses from pension commitments	−41	−46	5
Foreign currency reserve	−30	−29	−1
Revaluation reserve	73	40	33
AfS reserve	−220	−360	140
Cash flow hedge reserve	293	400	−107
Consolidated profit/loss 1.1.–31.12.	160	69	91
Total financial position equity	**3,480**	**3,283**	**197**

[1] Adjusted due to the retrospective initial application of IAS 19 (revised). Details are given in the note entitled Principles in the notes to the consolidated financial statements

Capital Measures pbb's subscribed capital amounted to €380,376,059.67 both at 31 December 2013 and at the prior-year reporting date, and is composed of 134,475,308 registered ordinary no-par-value shares with a notional interest in the subscribed capital of €2.83 per no-par-value share. Hypo Real Estate Holding was the sole shareholder of pbb. There was no authorised or contingent capital as at 31 December 2013.

Financial position equity amounted to €3.5 billion as at the balance sheet date (2012: €3.3 billion). No capital increases or reductions were implemented in financial years 2013 and 2012. The new equity item profits/losses from pension commitments resulted from the mandatory initial application of IAS 19 (revised). This item contains actuarial gains/losses on defined benefit pension commitments. Actuarial gains/losses are the effects arising from the differences between actuarial assumptions and what actually occurs (experience adjustments) plus the effects of changes in the actuarial assumptions. This negative equity item (2013: of €−41 million, 2012: €−46 million) primarily resulted from the significant decline in recent years in the discount rate applicable to defined benefit pension obligations.

No concrete capitalisation measures are planned at present. However, as part of its decision approving state aid, the European Commission specified that pbb must be privatised by the end of 2015.

Regulatory Indicators in Accordance with the German Solvency Regulation In accordance with the waiver rule set out in section 2a of the Kreditwesengesetz (KWG – German Banking Act), pbb is exempted from having to calculate equity and Tier 1 capital ratios at the level of the institution. pbb Group publishes these figures voluntarily on a pro forma basis.

pbb Group's pro forma regulatory capital in accordance with the Solvabilitätsverordnung (SolvV – German Solvency Regulation) is as follows:

Own funds[1]

in € million	31.12.2013	31.12.2012
Core capital (Tier I)	2,825	2,898
Supplementary capital (Tier II)	835	1,179
Equity capital	**3,660**	**4,077**
Tier III capital	–	–
Total	**3,660**	**4,077**

[1] Consolidated in accordance with section 10 a of the KWG; pro forma in accordance with the prepared annual financial statements and following the appropriation of net profit

The capital ratios were calculated on the basis of the definition of equity given in the SolvV and using risk-weighted assets in accordance with Basel II. The pro forma capital ratios are as follows:

Key capital ratios[1]

in %	31.12.2013	31.12.2012
Tier 1 capital ratio[2]	20.1	18.9
Equity capital ratio[3]	26.1	26.7
Own funds ratio (overall indicator)[2]	26.0	26.6

[1] Pro forma in accordance with the prepared annual financial statements and following the appropriation of net profit
[2] Including weighted credit risk positions and capital charges for market risk positions and operational risk, using a scaling factor of 12.5
[3] Including weighted credit risk positions and capital charges for operational risk, using a scaling factor of 12.5

Capital is managed on the basis of the SolvV and the requirements of section 10 of the KWG. In accordance with these, the equity ratio (equity/risk-weighted assets) may not fall below 8.0%. Additionally, Tier 1 capital must amount to at least 50% of equity, meaning that the Tier 1 capital ratio must be at least 4.0%. At the same time, the own funds ratio of at least 8.0%, which is calculated from the ratio of own funds to the sum of risk-weighted assets and the capital charges for market risk positions multiplied by 12.5 must be complied with. These requirements were met throughout the whole of financial years 2013 and 2012.

pbb Group has received regulatory approval to apply the Advanced Internal Ratings-Based Approach (Advanced-IRBA) in full for all portfolios requested to calculate its regulatory capital requirements. The initial application of this approach as at 31 December 2013 increased risk-weighted assets. This increase was almost exclusively attributable to the abolition of the privileged status previously afforded to central and regional governments and other public sector entities, under the Credit Risk Standardised Approach (CRSA), the method previously used.

The calculation of the CET1 ratio is adjusted to the Basel III calculation method in 2014. This will be lower than the previous ratio as a result of the more restrictive CET definition.

Liquidity

Principles and Objectives of the Liquidity and Financial Management The primary objective of pbb Group's financial management is to secure and manage the liquidity of pbb and its subsidiaries in such a way that their financing and funding capabilities are assured at all times. The Treasury division is responsible for central liquidity management at pbb Group, which it does by raising and investing liquidity on the money and capital markets and on the interbank money market, as well as with central banks and other sources of liquidity. By contrast, the liquidity risk strategy, like the waiver rule, is part of HRE's risk strategy.

Maturities Asset/liability management for pbb Group is performed by HRE's Group Asset and Liability Committee (ALCO), which also acts on behalf of pbb Group. The following table compares the remaining terms of the assets and liabilities:

Maturity structure of financial position	31.12.2013		31.12.2012	
in € million	Assets	Equity and liabilities	Assets	Equity and liabilities
Total	**73,924**	**73,924**	**97,081**	**97,081**
up to 3 months	10,174	6,778	14,831	10,425
3 months to 1 year	4,885	5,355	6,702	6,278
1 year to 5 years	23,439	26,598	30,607	28,786
5 years and over	27,966	24,139	32,954	28,746
Other assets[1)2)]/equity and liabilities[1)3)]	7,460	11,054	11,987	22,846

[1)] Adjusted due to the retrospective initial application of IAS 19 (revised). Details are given in the note entitled Principles in the notes to the consolidated financial statements

[2)] Trading assets, allowances for losses on loans and advances, property, plant and equipment, intangible assets, other assets, income tax assets

[3)] Trading liabilities, provisions, other liabilities, income tax liabilities, equity

Liquidity Management Liquidity management within pbb Group is performed centrally by pbb's Treasury division. The sales units are refinanced internally on a one-to-one basis when they enter into new business. This means that risks are bundled and centrally managed. The liquidity ratio is calculated at the level of the individual institution at pbb in accordance with the Liquiditätsverordnung (LiqV – German Liquidity Regulation), and amounted to 3.03 at the balance sheet date (2012: 2.28). This was significantly higher than the statutory minimum of 1.0. Monitoring of compliance with foreign liquidity ratio requirements for operating facilities is also ensured, if this is demanded by local regulatory authorities.

Funding Investors' demand for high-yield investment opportunities increased, boosted by the central banks' monetary policy and historically low interest rates. Unsecured issues benefited from this higher risk appetite. Increasing market volatility as a result of the bailout in Cyprus and concerns about the exit from the current expansionary monetary policy made Pfandbriefe even more attractive to investors.

pbb Group further increased its issuing activities, with a total volume of €7.7 billion (2012: €6.5 billion). Of this amount, €4.5 billion (2012: €3.0 billion) was attributable to benchmark issues. Fixed-income issues predominated. By contrast, new business on the assets side was entered into primarily on a floating rate basis in the reporting period, with the borrowers' interest rate risk generally being hedged with a customer derivative. pbb Group's open interest rate positions are usually hedged by swapping fixed interest rates for floating rates.

pbb Group's issuing activities accounted for around 10% of the issue volume on the German Pfandbrief market in 2013. The Group also underlined its activity on the funding markets by issuing a public sector Pfandbrief with a 15-year term as well as two unsecured benchmark bonds in the total amount of €1.4 billion. In addition, all of the benchmark issues in the reporting period mature after 2015, i.e. after the date prescribed by the European Commission for the privatisation of pbb. Overall, securitised liabilities amounted to €47.1 billion at the balance sheet date (2012: €52.6 billion). Mortgage Pfandbriefe denominated in foreign currency were issued in the amount of GBP 0.4 billion.

Furthermore, pbb Group has offered overnight investments and time deposit investments to private investors since March 2013. The deposit volume at the end of the year was €0.6 billion. In this way, pbb Group has expanded its unsecured funding base.

Benchmark issues

ISIN	Announcement	Settlement	Maturity	Coupon	Volume	Issue price	Currency
DE000A1RFBU5 (unsecured benchmark issue)	17.1.2013	24.1.2013	19.7.2016	2.000%	500 million	99.587%	EUR
DE000A1RFBY7 (mortgage Pfandbrief)	23.1.2013	30.1.2013	30.1.2017	0.875%	500 million	99.785%	EUR
DE000A1RFBU5 (1st tap)	14.2.2013	21.2.2013	19.7.2016	2.000%	360 million	100.382%	EUR
DE000A1R0527 (mortgage Pfandbrief)	11.3.2013	18.3.2013	18.3.2020	1.500%	500 million	99.487%	EUR
DE000A1R0584 (mortgage Pfandbrief)	8.5.2013	16.5.2013	16.5.2016	variable[1]	200 million	99.852%	GBP
DE000A1R06C5 (public Pfandbrief)	22.5.2013	29.5.2013	29.5.2028	2.375%	500 million	99.612%	EUR
DE000A1R0527 (1st tap)	28.5.2013	4.6.2013	18.3.2020	1.500%	250 million	100.835%	EUR
DE000A1PG3M8 (1st tap)[2]	28.5.2013	4.6.2013	20.12.2019	1.875%	75 million	99.589%	GBP
DE000A1R0584 (1st tap)	5.8.2013	12.8.2013	16.5.2016	variable[1]	50 million	99.864%	GBP
DE000A1PG3M8 (2nd tap)[2]	20.8.2013	27.8.2013	20.12.2019	1.875%	50 million	95.493%	GBP
DE000A1X2566 (mortgage Pfandbrief)	21.8.2013	28.8.2013	28.8.2018	1.375%	500 million	99.803%	EUR
DE000A1R06C5 (1st tap)	22.8.2013	29.8.2013	29.5.2028	2.375%	200 million	94.052%	EUR
DE000A1X26E7 (unsecured benchmark issue)	2.9.2013	9.9.2013	11.9.2017	2.250%	500 million	99.799%	EUR
DE000A1RFBY7 (1st tap)	4.10.2013	11.10.2013	30.1.2017	0.875%	100 million	100.127%	EUR

[1] Three-month GBP LIBOR plus 45 basis points
[2] Tap of a mortgage Pfandbrief in the original amount of GBP 250 million on 6 November 2012

Ratings The following table shows the senior unsecured ratings and ratings for pbb's Pfandbriefe:

Senior unsecured ratings and ratings for Pfandbriefe of pbb[1]			31.12.2013			31.12.2012
	Fitch Ratings	Moody's	Standard & Poor's	Fitch Ratings	Moody's	Standard & Poor's
Long-term rating	A–	Baa2	BBB	A–	Baa2	BBB
Outlook	Stable	Negative	Stable	Stable	Negative	Stable
Short-term rating	F1	P–2	A–2	F1	P–2	A–2
Public sector Pfandbriefe	–	Aa1	AA+[3]	–	Aa1	AA+[2]
Mortgage Pfandbriefe	–	Aa2	AA+[3]	–	Aa1[2]	AA+[2]

[1] Ratings from mandated rating agencies
[2] CreditWatch Negative
[3] Stable outlook

The rating agencies may alter or withdraw their ratings at any time. For the evaluation and usage of ratings, please refer to the rating agencies' pertinent criteria and explanations and the relevant terms of use which are to be considered. Ratings should not serve as a substitute for personal analysis. They do not constitute a recommendation to purchase, sell or hold securities issued by pbb.

The ratings trend continues to be heavily influenced by exogenous factors such as the ongoing sovereign debt crisis and changes to rating methodologies or parameters applied by the rating agencies. It only reflects pbb's successful restructuring measures and business success to a certain extent. In light of the changes to bank restructuring legislation that are planned in Europe, and particularly in relation to the possible bail-in of senior unsecured creditors in a banking crisis, rating agencies have announced reviews of the systemic support elements incorporated in senior unsecured ratings. This could have negative effects on credit institutions' ratings. It may also impact covered bond ratings due to the link between these and the issuer's senior unsecured rating. In this context, a number of rating agencies have also announced changes to their covered bond rating methodologies.

The senior unsecured ratings assigned by the mandated rating agencies – Fitch Ratings, Moody's and Standard & Poor's – remained unchanged in financial year 2013. Fitch Ratings affirmed pbb's ratings in March 2013 during a review of ratings for German Pfandbrief banks. Standard & Poor's affirmed its ratings for the Bank in November 2013.

The ratings of pbb's Pfandbrief programmes were affirmed by Standard & Poor's in January 2013. The CreditWatch Negative, which Standard & Poor's had assigned to both programmes following a change in the methodology used, was resolved and replaced by a stable outlook. Following changes in the cover pool in connection with the full transfer of cover pool assets to FMS Wertmanagement, Standard & Poor's affirmed the AA+ rating of the mortgage Pfandbrief programme in September 2013 with a stable outlook. Moody's lowered the rating for mortgage Pfandbriefe from Aa1 to Aa2 in April 2013, thus ending a review for downgrade which resulted from the downgrade of the Bank's senior unsecured rating in December 2012.

After the balance sheet date the following rating actions took place:

In February 2014, Standard & Poor's affirmed the rating of pbb's public sector Pfandbriefe. In the same month, Fitch Ratings affirmed pbb's unsecured ratings.

Further ratings drivers and the impact of potential changes in ratings are described in the Report on Expected Developments.

Off-balance-sheet Obligations Irrevocable loan commitments account for the majority of off-balance-sheet obligations and rose as against 31 December 2012 from € 1,035 million to € 2,569 million due to new business that has not yet been fully paid out. Contingent liabilities amounting to € 25 million at the balance sheet date resulted from guarantees and warranty agreements (2012: € 75 million). The services provided to FMS Wertmanagement were largely discontinued as at 30 September 2013. Hypo Real Estate Japan Corporation, Tokyo, a subsidiary of pbb, is an exception; it provides services for FMS Wertmanagement's Japanese Real Estate Finance portfolio. pbb Group and FMS Wertmanagement also continued to provide each other with services that cannot be otherwise obtained after 30 September 2013 on the basis of what is currently a cost-plus agreement. These relate in particular to the provision of information, the granting of powers of attorney and the provision of services required under supervisory laws. In addition, pbb and FMS Wertmanagement entered into a settlement agreement in the fourth quarter of 2013. Under this agreement, all potential claims by FMS Wertmanagement for damages related to services provided, all past, present and future claims for the reimbursement of costs for the legal transfer of assets (upgrades) that had previously only been transferred or hedged by means of sub-participations, back-to-back derivatives, or financial guarantees, as well as payment obligations by pbb in connection with the transfer of employees to FMS Wertmanagement Service GmbH, are deemed to have been settled.

Summary

pbb Group took further steps towards privatisation in 2013. The target model has been implemented and pbb Group has been successfully positioned on the market as a strategic part of HRE. An additional step will be the separation of the IT systems of pbb Group and DEPFA.

The positive trend is reflected in pbb Group's development in assets, financial position and earnings. A positive pre-tax profit of € 165 million was generated in 2013 (2012: € 124 million). This meant that pbb Group both exceeded its forecast of at least € 100 million made at the start of 2013 and reached its lifted forecast of at least € 150 million announced on 8 October 2013. However, it did also benefit from positive non-recurring income. pbb Group has been profitable for the past three-and-a-half years, a fact which highlights the long-term positive trend.

The decline in assets and liabilities predominantly resulted from the transfer of mortgage loans to FMS Wertmanagement that were derecognised from the balance sheet and that had already been economically transferred in 2010, the repayment of the three-year tender and the strategic reduction of the non-strategic portfolio. The requirements regarding regulatory capital ratios in accordance with the SolvV and regarding liquidity ratios were complied with throughout the whole of financial year 2013. pbb Group calculates these ratios voluntarily on a pro forma basis.

Report on Post-balance Sheet Date Events

On 31 January 2014, pbb signed an agreement with FMS Wertmanagement in which the transfer of positions to FMS Wertmanagement in the course of the establishment of the resolution agency in 2010 was finally settled. As a result of this agreement, pbb will make a payment to FMS Wertmanagement, for which provisions were already established in prior periods. As the agreement is beneficial from HRE's perspective, HRE Holding will reimburse pbb for the expense. This reimbursement will directly increase pbb Group's equity in 2014.

On 26 November 2013, pbb committed to acquiring all of the shares of RPPSE Espacio Oviedo S.L.U., Madrid. The shares were purchased for € 1 on 25 February 2014 by IMMO Invest Real Estate GmbH, Munich, a subsidiary of pbb. As the special purpose entity was already consolidated as at 31 December 2013 this had no impact on pbb Group's development in assets, financial position and earnings.

Dr Alexander Groß left the Supervisory Board of pbb effective 25 February 2014.

The Supervisory Board of pbb appointed Andreas Schenk as a member of the Management Board effective 1 March 2014. As the Chief Risk Officer (CRO) on the Management Board, Andreas Schenk is responsible for overall risk management.

The Supervisory Board appointed Andreas Arndt as Chief Financial Officer effective 15 April 2014. He will be responsible for the CFO department and its finance, operations and legal areas. Alexander von Uslar will leave the Management Board.

Risk and Opportunity Report

The risk and opportunity report shows the risks and also the opportunities identified for the individual risk types within the framework of the implemented risk management and risk controlling system. With regard to risks and opportunities relating to all areas of the Company and also general Company-specific risks and opportunities, please refer to the details in the report on expected developments.

Organisation and Principles of Risk and Capital Management

HRE has set up a Group-wide risk management and risk controlling system which represents as well an important precondition for the application of the so-called waiver according to Section 2a KWG. All tasks in accordance with Section 25a KWG for uniform risk identification, measurement and limiting as well as risk management are defined centrally by HRE. Operational implementation is the responsibility of the respective subsidiary and thus also of pbb. This risk and opportunity report also covers opportunities within the framework of a quality assessment.

Organisation and Committees

The principles, methods and processes of the risk management system of HRE Group are specified centrally by risk management and controlling of HRE Holding and are applied in pbb Group. The committees detailed in the following have been set up at the HRE Group level with the involvement of the respective decision-makers of pbb Group.

The Management Board of pbb is responsible for the risk management system, and is responsible for taking decisions relating to the strategies and the main issues of risk management and risk organisation of pbb Group. The risk management system comprises the plausible and systematic identification, analysis, valuation, management, documentation, monitoring and communication of all major risks.

The following are major components of the risk management system for which the Management Board is responsible:

> Defining, updating and communicating business and risk strategies as the basis of business activities and risk acceptance within pbb Group
> Defining and improving organisation structures within pbb Group and in particular for risk management, which ensures that all major risks are managed and monitored
> Adopting credit competences as a decision-making framework along the credit processes within pbb Group
> Taking decisions regarding (portfolio) management measures outside the competences which have been transferred

The Management Board of pbb notifies the Supervisory Board of pbb with regard to significant changes in the business and risk strategies as well as the risk profile of pbb Group. The Risk Management and Liquidity Strategy Committee (RLA) of the Supervisory Board is mainly responsible for controlling the overall risk situation and for monitoring, establishing and improving an efficient risk management system, and is also responsible for the liquidity management and assurance of pbb Group and resolves upon necessary credit approvals for credit decisions. The Management Board notifies this committee of all increases to individual allowances and the creation of new individual allowances in excess of €5 million and has also notified this committee at regular intervals of major exposures with higher levels of risk.

The **Group Risk Committee (RC)** of HRE, acting simultaneously for pbb, consists of the Chief Risk Officer (CRO; Chairman) and the Chief Financial Officer (CFO) of HRE Holding acting as CRO and CFO of pbb simultaneously as well as the Chief Risk Officer (CRO) of DEPFA Bank plc and the Chief Credit Officer (CCO) of pbb as well as the Head of Risk Management & Control. In general, the committee meets on a monthly basis and discusses the risk development of the Bank, adopts guidelines/policies, methods for risk measurement, the related parameters as well as methods of monitoring all risk types. The Risk Committee is responsible for the development of standard guidelines of risk management and risk controlling across the Group and also monitors the development of the risk-bearing capacity, economic capital, the risk cover funds as well as the credit portfolio and the compliance with limits. The Risk Committee discusses the portfolios of HRE Group and hence of pbb Group.

HRE's **Group Asset and Liability Committee (ALCO),** which also serves pbb, meets monthly. It is chaired by the member of the Management Board responsible for Treasury and Asset Management and comprises the CRO, the CFO/COO and the managers of the Treasury, Finance and Risk Management & Control divisions. Its tasks include liquidity management, asset/liability management for HRE and pbb Group, defining long-term financing strategies, capital management, management of regulatory capital ratios and market risk management. The ALCO does not make any credit decisions or set any limits for other risk categories. This committee is also responsible for preparing decision-making documents for liquidity and refinancing strategies which, following discussions in the Risk Committee, are decided in the same way as acquisitions and disinvestments in the Management Board of HRE respectively pbb.

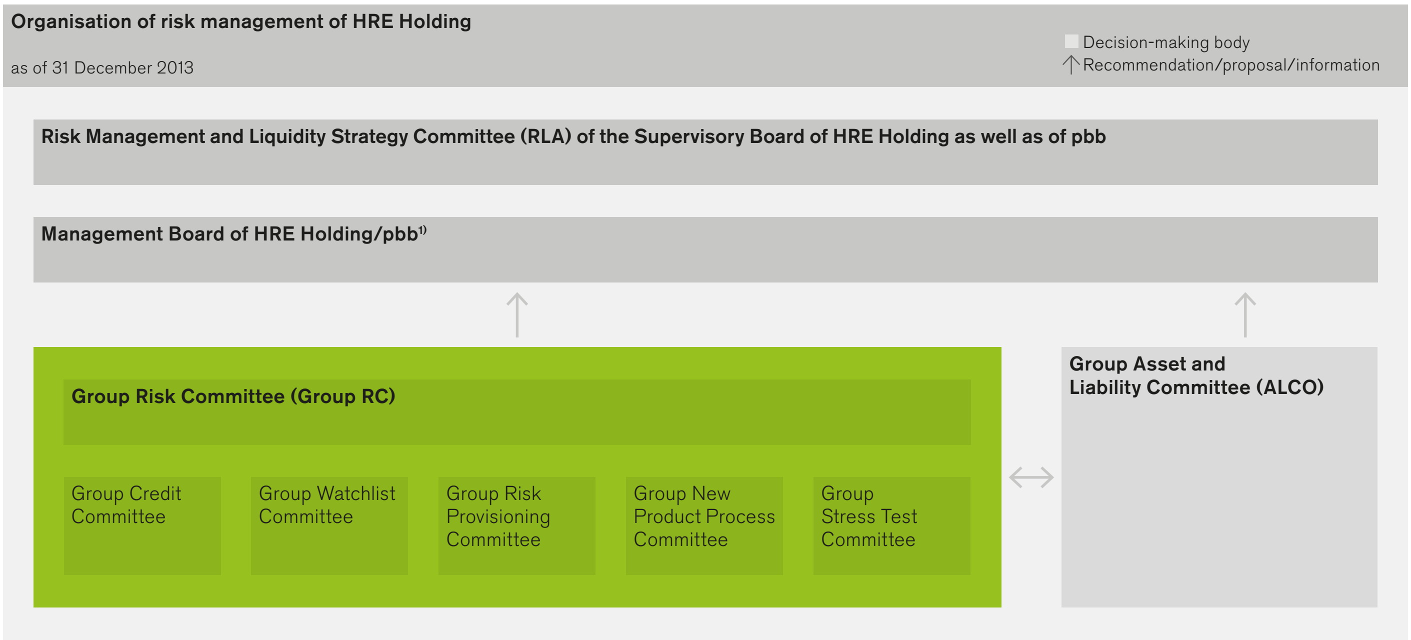
The **Group Credit Committee** of HRE, acting simultaneously for pbb, comprises the CRO (Chairman), the Chief Credit Officer (CCO), the Senior Credit Executives as well as representatives of the front office. The front office representatives have a voting right as part of front office responsibility. As a general rule, the committee meets at least once a week and takes credit decisions on new business, prolongations and material changes that fall within the scope of its authority. It also votes on all credit decisions which are in the responsibility of the Management Board of pbb and which have to be approved by the Risk Management and Liquidity Strategy Committee. The Credit Committee ensures that the credit decisions are consistent with the prevailing business and risk strategy.

The **Group Watchlist Committee** of HRE, acting simultaneously for pbb, meets every month. All exposures of pbb Group identified by the early warning system are discussed and, if appropriate, individual measures are decided there; these measures have to be subsequently implemented by the relevant departments. Where necessary, the committee takes decisions regarding the need to transfer exposures to CRM Workout, which then takes the necessary steps for restructuring and workout on the basis of an exposure strategy. All necessary credit decisions are taken by the key personnel in line with the allocation of credit powers or in the Credit Committee.

If there are any indications of an objective impairment of an exposure, the extent of the impairment is first determined and the result is presented in the **Group Risk Provisioning Committee**. The committee takes decisions within the framework of a predefined set of allocated powers and in line with the IFRS/HGB regulations, and provides recommendations regarding the creation and reversal of provisions for losses on loans and advances as well as any necessary salvage acquisitions. The recommendations made by the committee have to be decided by the Management Board of pbb in line with the relevant set of rules governing powers.

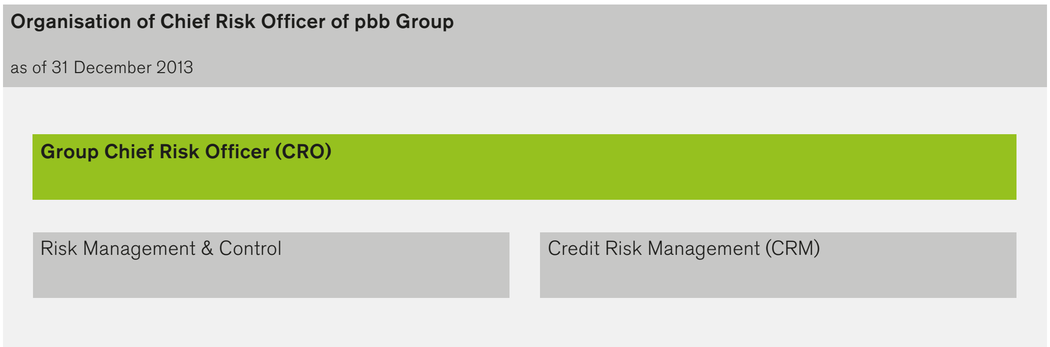
The **Group New Product Process Committee** ensures that, before business commences with new products or in new markets, the resultant risks as well as the related impact on processes, controls and the infrastructure are systematically analysed and addressed. Operations with new products or in new markets are only commenced when they have been approved by the New Product Process Committee.

The **Group Stress Test Committee**, which is a sub-committee of the Group Risk Committee, is responsible for the methodology, performance and monitoring of the internal stress tests.


Organisation of risk management of HRE Holding
as of 31 December 2013
□ Decision-making body
↑ Recommendation/proposal/information
Risk Management and Liquidity Strategy Committee (RLA) of the Supervisory Board of HRE Holding as well as of pbb
Management Board of HRE Holding/pbb¹⁾
Group Risk Committee (Group RC)
Group Credit Committee
Group Watchlist Committee
Group Risk Provisioning Committee
Group New Product Process Committee
Group Stress Test Committee
Group Asset and Liability Committee (ALCO)

[1] Due to existing waiver according to Section 2a of the German Banking Act

Group Chief Risk Officer (CRO) In addition to the above-mentioned committees, the following organisation units of the Group CRO, who is also CRO of pbb, form an integral part of the risk management system of HRE, in which pbb Group is included:


Organisation of Chief Risk Officer of pbb Group
as of 31 December 2013
Group Chief Risk Officer (CRO)
Risk Management & Control
Credit Risk Management (CRM)

The organisation of the CRO function comprises the following monitoring and back-office entities on pbb Group level:

- The unit Risk Management & Control, which is also responsible for monitoring and managing market, credit, operational and liquidity risks as well as the risk-bearing capacity of pbb Group and which is also responsible for Group-wide uniform risk measuring methods, risk reports and credit processes
- The units of the Credit Officer of pbb Group, which are each responsible for the analysis of new business and portfolio management. CRM pbb also comprises the Workout (Real Estate) unit, which is responsible for the restructuring and workout of all critical exposures in the Real Estate Finance segment, and the central unit Credit Processes, which is responsible in particular for the organisation of the Credit Committee and for updating credit processes.

Property Analysis & Valuation, which is responsible for the analysis and uniform valuation of the collateral properties using market and loan-to-value methods, is under the control of the CRO. In addition to the CRO function, the Compliance/Corporate Governance entity and the Group Internal Audit entity (independent) complement the risk management system of pbb Group. The area of responsibility of Group Internal Audit comprises the regular as well as the event-driven audit of processes and systems as well as significant transactions. This also includes the revision of the risk management system. Regarding legal issues Risk Management is also supported by the Legal department.

Risk Strategy and Policies

The risk strategy of pbb Group is based on the business strategy, risk inventory and the results of the Group-wide financial planning process. It is applicable for the operating segments and legal entities of pbb Group. The risk strategy was revised in March 2013, adopted by the Management Board of pbb and presented to the Risk Management and Liquidity Strategy Committee of the Supervisory Board of pbb and afterwards to the Supervisory Board plenum to be noted. The risk strategy was amended in July 2013, mainly to incorporate minor updates.

The risk strategy reflects the strategic focus of pbb Group as a specialist for real estate finance and public investment finance in Germany and selected countries in Europe with Pfandbrief-oriented refinancing. It is reviewed at least annually and updated if applicable.

The operationalisation of the risk strategy is carried out via risk policies for the individual operating segments as well as for all major risk types (credit risk, market risk, liquidity risk, business risk, property risk and operational risk); these risk policies describe risk measurement, risk monitoring, risk management, the limit process as well as the escalation process if a limit is exceeded. The policies are regularly reviewed and updated where necessary.

Risk Reporting

Risk reporting reflects the structure of the operating segments. The Management Board of pbb receives regular risk reports which include an extensive overview as well as detailed information concerning the risk situation for each risk type and company as well as other management-relevant information. The supervisory bodies are also notified of risk-relevant issues at regular intervals. In addition, special reports are prepared on an ad hoc basis or at the request of the Management Board or Supervisory Board; such special reports consider specific and acute risk issues, for instance in relation to critical markets, products or counterparties.

Risk Quantification and Risk Management

The risk-bearing capacity analysis quantifies credit risk, market risk, business risk, real estate risk and operational risk, aggregates them to produce an overall risk figure and compares them with the risk cover amount under the risk-bearing capacity approach. The liquidity risk is quantified on the basis of the liquidity position. The individual calculation methods are described in detail in the risk report in the chapters «Result of Risk-bearing Capacity Analysis» respectively «Liquidity Risk».

Other risk types that are considered material by the regular internal risk inventory, such as regulatory risk and risks that are not considered material are not quantified using risk models. These risks are managed and limited using regular, detailed reports and clear instructions, such as compliance and corporate governance rules.

At the portfolio level and at the level of individual transactions, risk in pbb Group is managed by:

1. Monitoring the risk-bearing capacity of pbb Group by comparing economic capital and the risk cover amount under the risk-bearing capacity approach. In addition, the risk-bearing capacity is managed in detail by using a limit system for risk cover potential and economic capital for different risk types or segments.
2. Monitoring and analysis of the risk-weighted assets (RWA) of pbb Group at the portfolio level by means of stress tests which are intended to ensure that the core equity Tier 1 ratio does not fall below 9%.
3. Operational risk management via
   - > the use of Basel-II-compliant risk parameters in lending business of pbb Group. The Basel-II-compliant management approach shows the average expected loss at the borrower level, and is therefore a major component for the early recognition of risks and ongoing profitability monitoring. The parameters are reviewed and recalibrated annually.
   - > A limit system for counterparty and issuer risks on the basis of a standard application which has been tested in the market with a risk measurement method that is uniform throughout the Group.
   - > Intensive monitoring and management of individual exposures.
   - > Monitoring the risk of losses by way of appropriate impairment triggers in accordance with IAS 39.
4. Daily monitoring of market risk.
5. Daily monitoring of liquidity risk.
6. Monitoring of operational risk.

Economic Capital and Monitoring the Risk-bearing Capacity

In accordance with Section 25 a (1) KWG, credit institutions are obliged to set up appropriate and effective procedures in order to ensure that their risk-bearing capacity can be determined and assured in the long term. These procedures complement the regulatory procedures defined in the Solvency Regulation. The Bank's own risk-bearing capacity calculation is the subject of regulatory reviews («Supervisory Review and Evaluation Process», SREP).

pbb Group has implemented a risk-bearing capacity analysis based on the Internal Capital Adequacy Assessment Process (ICAAP). The Internal Capital Adequacy Assessment rests upon the concept of economic capital.

Economic capital is defined as the quantity of capital required by a bank in order to cover the largest potential total loss with a defined probability (the confidence level) over a time horizon of one year. There have been the following enhancements in 2013. As well as improving the method used to quantify real estate risk, pbb Group has developed a model to calculate operational risk, the key inputs for which are internal loss data.

Alongside the classic risk types – market, credit and counterparty, business and operational risk – the risk inventory again identified real estate risk as material and quantifiable in 2013. As a result, five separate risk types have been included in the ICAAP and are backed by capital.

A going-concern approach has been developed already in 2012 as the primary steering approach for demonstrating the risk-bearing capacity of pbb Group; this has been completely integrated in the ICAAP. Unlike the previous gone-concern approach, this steering approach does not focus on the theoretical event of the institute being liquidated; instead, it focuses explicitly on the going-concern assumption and also assumes that the regulatory minimum capital ratios are met. In addition to protecting regulatory minimum capitalisation, the going-concern approach also comprises an extensive early warning system which generates corresponding warning signals early before the minimum ratios are attained.

The gone-concern approach within pbb Group has been developed in two complementary perspectives which support in parallel the leading going-concern approach. Firstly, there is the instantaneous liquidation perspective which, in a theoretical liquidation case, does not assume opportunistic winding up of the portfolios unlike demanded by the German Pfandbrief Act and instead is based on the assumption of the immediate sale of, inter alia, the securities of the banking book. According to this assumption and in addition to the above-mentioned major risks the instantaneous liquidation perspective also takes account of credit spread risks arising from securities in the banking book for calculating the economic capital and deducts the hidden losses attributable to these securities for determining the available financial resources. Secondly, pbb Group has developed a strategic gone-concern perspective which focuses on strategic business for calculating the economic capital. Risks from the Budget Finance portfolio and the Value Portfolio which are earmarked for being streamlined are covered by way of a buffer. A confidence level of 99.91% was calculated for both scenarios. This confidence level is based on the average probability of default of companies which have been awarded good long-term credit ratings by external rating agencies, namely A– at Standard & Poor's and A–/A3 at Fitch Ratings and Moody's, and is consistent with the fundamentally conservative parameters in the risk models. The methods of calculating the economic capital for the individual risk types as well as current parameters are described in greater detail in the chapter «Result of Risk-bearing Capacity Analysis». No economic capital is calculated for the liquidity risk. This risk type is addressed and limited by a separate management approach.

In order to assess the adequate capitalisation of the capital backing of pbb Group in the relevant approach, the amount of economic capital is compared with the respective available financial resources. Under the leading going-concern scenario, for example, the available risk cover amount largely comprises the core Tier 1 capital available over a period of at least one year, less the capital required to meet the regulatory minimum capital ratios, after adjustment for negative RWA trends. The remaining core Tier 1 capital is suitable for absorbing potential losses and for maintaining a corresponding risk buffer. Under the gone-concern approach, both equity in accordance with the IFRS and subordinate items with a term of more than one year are used to determine the risk cover amount, less hidden liabilities relating to securities in the banking book. In order to verify the risk-bearing capacity, the economic capital must be completely covered by the available financial resources.

The results of the risk-bearing capacity analysis and of the stress tests are regularly presented to the central Management Board and the Group Risk Committee. The results are discussed there and if necessary management measures are defined.

Risk Types

pbb Group distinguishes the following major risk types for its business activities:
> Credit risk (Counterparty risk)
> Market risk
> Liquidity risk
> Operational risk
> Business risk (partial consideration within the scope of the risk-bearing capacity analysis)
> Property risk (consideration within the scope of the risk-bearing capacity analysis)

The following are major risk types of pbb Group which are not quantified but which are limited by means of suitable reports, guidelines and policies:
> Strategic risks
> Reputational risks
> Regulatory risks

Credit Risk (Counterparty Risk)

Definitions

The counterparty risk in general is defined as the risk of an unexpected default or decline in the fair value of a receivable or a derivative, resulting from a deterioration in the hedging situation or deterioration in the creditworthiness of a country or a counterparty.

The counterparty risk comprises the credit risk, counterparty default risk, replacement risk, repayment risk, issuer risk, country risk, concentration risk and fulfilment risk which in the Risk Strategy of pbb Group are defined as follows:
> Credit risk is defined as the risk which considers loans and traditional credit products as such. A major factor determining the credit risk is the ability of the borrower to fulfil his financial obligations as well as the value of collateral in the case of a borrowers' default. Declines in the fair value as a result of rating changes are taken into consideration for calculating the credit risk.
> Counterparty default risk is defined as the risk of a potential unexpected default or decline in the fair value of a claim or a derivative. This is due to a deterioration in the creditworthiness of a counterparty or a deterioration of the hedging situation. The counterparty default risk includes the replacement risk and the repayment risk.
> Issuer risk is defined as the risk in relation to bonds and other securities. In particular, it refers to the ability of the issuer to meet his financial obligations and also relates to the value of collateral in the event of the default of an issuer. Declines in the fair value as a result of rating changes are taken into consideration for calculating the issuer risk.
> Country risk arises from changes in the values of international exposures due to country-specific political and economic conditions. It essentially comprises the risk that arises in connection with business activities in certain countries. The country risk includes the conversion risk, transfer risk and sovereign default risk.
> Concentration risk is defined as the risk of cluster formation in relation to a risk factor or counterparties, or a strongly correlated group of risk factors or counterparties.
> Fulfilment risk is defined as the risk that the Bank makes a payment or delivers an asset which has been sold to a counterparty but does not receive a payment or the purchased asset.

Credit Risk Strategy and Principles

pbb Group has broken down the overall credit portfolio into the segments Real Estate Finance, Public Sector Finance, Value Portfolio and «Consolidation & Adjustments». The strategic business is attributable to Real Estate Finance (REF) and Public Investment Finance (PIF) as part of the Public Sector Finance portfolio. The risk strategy of pbb Group also reflects this structure.

New business in the Real Estate Finance segment largely focuses on Pfandbrief-eligible financing of commercial real estate with sustainable cash flow in selected European countries. The main target customers of these operations are professional investors, institutional clients, real estate funds or selected developers.

In the Public Sector Finance segment, new business of pbb Group focuses on Pfandbrief-eligible financing of public investment financings in selected European countries.

New business is to be refinanced with matching maturities where possible, mainly using Pfandbrief issues.

Credit Risk Reports

The credit risk reports provide information about the following main components:

- The HRE Group Risk Report contains the development in volumes as well as relevant credit risk management indicators such as the development of the expected loss as well as the unexpected loss via value at risk (VaR). The report shows the credit risk at HRE Group level and also at the level of pbb Group in the context of the overall bank risk and the risk-bearing capacity, it reports limit utilisations and violations of existing limits, and also identifies risk concentrations. Key indicators, such as the development of the exposure at default (EaD), the expected loss (EL), the credit value at risk (Credit VaR) as well as problem loans are integrated in this report and are discussed by the Management Board; the report is also submitted to the Risk Management and Liquidity Strategy Committee (RLA) of the Supervisory Board to be noted.
- For decisions relating to new business and adjustments of terms, major parameters, contents and analyses are presented to the Credit Committee and discussed.
- In the active business, further regular reports support operational management with regard to the management and timely recognition of risks at the sub-portfolio level.
- Unusual developments which might result in a major deterioration in the risk position of an individual exposure are reported to a wider group up to the CRO by way of so-called «Credit Issue Notes».

Credit Risk Quantification via Economic Capital and Risk-weighted Assets under Basel II

Credit Portfolio Model For calculating the economic credit risk capital (credit risk VaR) pbb Group uses a credit portfolio model which is described in greater detail in the section «Result of Risk-bearing Capacity Analysis».

Stress Tests The stress tests for economic capital in credit risk are described in greater detail in the section «Result of Risk-bearing Capacity Analysis».

In addition to the stress tests for economic capital, there are also RWA reverse stress tests. They investigate the extent to which a certain risk parameter (e.g. rating, loss-given default (LGD), currency) can change before the minimum core equity Tier 1 ratio of 9% is no longer met. Tolerance change levels have been defined for all tested risk parameters; these levels must not be violated if the test of pbb Group is to be successfully completed.

Credit Risk Quantification According to Basel II pbb Group has received the regulatory approval to apply the so-called Advanced Internal Rating-Based Approach (Advanced IRBA) for determining the regulatory capital backing.

Credit Risk Management and Monitoring

Credit Risk Management At the portfolio level, the intended portfolio structure is defined in the risk strategy by means of structure components. The limits are also based on the available financial resources, and include for pbb Group for example:

> Limiting of country risks

> Definition of strategic risk parameters (e.g. target customers, regions, financing duration)

The following reports and measures are key elements for monitoring compliance with the defined limits and the intended risk and return parameters at the portfolio level and also at the level of individual transactions:

> Analysis of portfolio developments of HRE Group and therefore as well for pbb Group in the Group Risk Committee

> Determining the credit risk VaR at the portfolio level by way of a credit portfolio model and partly limiting at the segment level; analysis of concentration risks and various stress tests

> Central Group-wide monitoring of risk concentrations by way of special, regular and ad hoc evaluations, such as regional or product-specific evaluations

> Continuous analysis of the portfolio and the relevant markets by the local Credit Risk Management units

> Regular evaluation of the collateral

> Special reports for exposures which are potentially at risk (e.g. «credit issue notes»)

> Calculation of a risk-adjusted margin using a defined RaRoC for new business

The credit competences also define the decision-making powers of the individual credit risk managers for prolongations in existing business, depending on the counterparty group and expected loss class.

Credit Risk Management and Monitoring At the level of individual transactions, the credit process guidelines define the necessary steps of assessing risk for new business, prolongations as well as the procedures for transferring exposures to the watchlist or workout.

Core processes of credit risk management and monitoring as well as the relevant areas of the CRO function which are involved are described in the following:

The CRM entities carry out the initial risk analysis for new business and annual risk analysis for existing business. Probability of default (PD) and loss given default (LGD) rating tools, which are developed by Credit Risk as part of Risk Management and Control (RMC) and annually validated and calibrated, are used for valuation purposes and for preparing the credit decision in new and prolongation business. Property Analysis & Valuation provides support for analysing and valuing the securities.

The Legal department, where appropriate together with external lawyers/lawyers' offices, is responsible for the contract and collateral organisation.

Defined early warning indicators are constantly monitored by CRM. If any problems are identified, an exceptional test is performed on the credit default risk (including a review of the value of collateral) and appropriate alternative actions are identified. Such cases are also included in a monthly monitoring cycle and presented in the Group Watchlist Committee.

If there are any objective indications of an impairment, the extent of such an impairment is determined. In the Group Risk Provisioning Committee (see also overview for organisation and committees), the results are discussed and, where necessary, decisions are taken with regard to creating or reversing impairments.

A restructuring plan or a workout plan for critical and impaired exposures is drawn up. The decision regarding restructuring or workout takes account of scenario analyses for the potential development of the borrower, the collateral or the relevant market. These are presented and approved in the Group Credit Committee, if necessary.

Critical exposures (watchlist) as well as restructuring and workout cases (non-performing loans) are reported on an aggregate basis monthly in the Group Risk Report and in the Group Risk Committee and also, upon request, in special analyses to the Management Board and Supervisory Board.

Hedging and Minimising Risk by Collateral

In the Real Estate Finance segment, financing arrangements are normally backed by property charges. On the occasion of the regular credit reports for existing financing arrangements or as part of the decision-making process in the case of new financing, the LTVs (loan-to-value) as well as the property (micro and macro location, rental situation, condition of property) and market circumstances are regularly discussed and are also taken into consideration as part of the assessment process for individual loans. On average, the loss-given default (LGD) is 15% for real estate financing arrangements which have not defaulted (31 December 2012: 17%). For the entire real estate finance portfolio, the LGD average is 16% (31 December 2012: 18%). These improvements in the average ratios are attributable to portfolio disposals and improvements at the level of individual transactions (ongoing repayments, larger partial repayments), among other things.

In addition to the property charge, the financing security also generally comprises rent assignation and the assignation of insurance claims (in the respective form of the various jurisdictions), accompanied by extensive notification and consultation obligations of the borrowers. Apart from the property charges, only a few more selected securities are considered to be of value in the credit assessment process, and in particular this is applicable for cash security, bank guarantees as well as guarantees of public-sector institutions. Corresponding knock-downs are recognised in relation to foreign currency security in order to take account of potential exchange rate risks.

In the Real Estate Finance segment, the real estate is valued under the following quality aspects:

a) When the loan is initially granted:

> For all real estate security, an internal report (property report) is prepared in the course of the loan decision-making process, and an external appraisal is generally obtained (this is always the case outside Germany) – before the loan is paid out. The procedures ensure that two views of the property are taken into consideration in the decision-making process. The first view is external and focuses solely on the property (as a complete market and lending value appraisal). The second view is internal within the framework of the financing arrangement; it compares the property risks with the financing structure.

> All internally prepared reports and appraisals are consistent with the principle of dual control. At least one senior property analyst who is an MRICS (certified member subject to the supervision of the Royal Institution of Chartered Surveyors) and/or who has passed the HypZert examination (certification by HypZert GmbH as a real estate valuer for financial purposes) is responsible for the report or the appraisal.

> All fair values and collateral values are calculated or at least reviewed by a senior property analyst who has passed the HypZert (F) examination (certification as a real estate valuer for financial purposes), or outside of Germany, the HypZert (MLV) examination (certification as a real estate valuer for mortgage lending valuation).

> When an order is placed for external appraisals, the MRICS and/or HypZert qualifications are also required as minimum standards. Other appraisals or comments are not recognised.

> In addition, the choice of external service providers in the field of real estate valuation is subject to strict selection criteria which are constantly monitored by the Bank and which are demonstrably checked every year.

> Every externally engaged appraisal, which has to be prepared in line with the principle of dual control, is again checked by an internal senior appraisal expert with the above qualifications before the data are entered into the Bank's internal system.

b) During on-going monitoring by the property analysis department:

> As part of the credit monitoring process, the economic value of the security is generally reviewed annually; this includes an assessment of the main factors which influence the real estate value (rental income, market changes, changes in the building condition). In Germany, the initial assessment is performed by CRM. A standardised catalogue of questions for capturing individual property changes, indexed market values based on time series, which are designed to identify changes in the market, and a market volatility model that provides additional information on changes in regional real estate markets are available for monitoring purposes. If this initial assessment indicates an expected change in the market value, a PAV employee conducts a more detailed assessment in a second step. In all other European countries, on an annual basis the PAV division directly performs the monitoring applying the quality standards for the second-level monitoring. The property analyst reviews the individual property characteristics on the basis of up-to-date documentation and takes any market changes since the last market value appraisal into account in his or her assessment. If necessary, the property is also inspected. This second stage of the assessment is used to confirm the previous market value. If there are indications that the various factors point to a change in market value, a revaluation is arranged immediately. Standard procedure is for the market values of properties with a market value of over €5 million and loans over €3 million to be reappraised at least every three years. Differences in the values or the security are recognised in the bank systems for risk assessment purposes.

> In the market value calculation process which takes place every three years, the quality standards which are applied are the same as those applied in the new business process. Again, the MRICS and/or HypZert qualifications are the minimum qualifications required for preparing appraisals or comments.

c) General:

> The procedures for ensuring the personal quality standards for the property analysts or engaged external appraisal experts in line with the prevailing regulations (HypZert/MRICS) is carried out by the respective monitoring authorities independently of the Bank; these processes are internationally recognised. Corresponding evidence is checked by the Bank.
> The process of engaging external services is carried out independently of the actual valuation management process in order to ensure maximum independence. Externally prepared appraisals or comments in which there is a suspicion that the person preparing the appraisal or comment might not be neutral are not recognised in any way and are also not used for the Bank's own internal purposes for the further process of preparing an appraisal.
> External appraisals are internally checked and are subject to quality assurance measures.
> Development financing arrangements are constantly monitored by our specialists (control of building status and costs). In addition, well-known external specialist companies are also involved in construction controlling (technical control, cost control) on an ad-hoc basis in the case of complex development financing.

In the Public Sector Finance field and especially in Public Investment Finance other financial securities and guarantees in particular are also accepted as collateral (e.g. credit insurances, contractual guarantees from public authorities, fixed-income securities, purchase of receivables, etc.). Additionally, in Public Investment Finance there exist legal framework requirements as the maintenance obligation, which allow recourse on a public sector entity.

Credit Portfolio

The entire credit portfolio of pbb Group was calculated by using a standard method in line with the Basel-II-compliant exposure at default (EaD).

The EaD recognises the current utilisation as well as pro rata credit interest in relation to which a borrower may default before an exposure is defined as having defaulted (max. default of 90 days), as well as those credit commitments which a borrower will still be able to utilise in future despite a major deterioration in creditworthiness. In the case of derivatives, the EaD is defined as the sum of the current market value and the regulatory add-on, which constitutes a cushion for future potential increases of the market value.

The Group-wide EaD of the credit portfolio amounted to €67.5 billion as of 31 December 2013 (EaD 31 December 2012: €76.2 billion). This figure includes the EaD with respect to FMS Wertmanagement which is not considered to be part of the core exposure of the pbb Group, and which further declined from €0.2 billion as of the end of 2012 to €0.01 billion. This amount is attributable to so-called back-to-back transactions. This is due to the fact that it was initially not possible to arrange the transfer of beneficial ownership for most of the derivatives earmarked to be transferred to FMS Wertmanagement in 2010, which meant that the market price risks of the derivatives were transferred to FMS Wertmanagement by way of concluding derivatives with identical conditions between pbb Group and FMS Wertmanagement.

In addition, the credit portfolio EaD of €67.5 billion also included assets with an EaD of €0.6 billion (31 December 2012: €0.7 billion) which have been selected to be transferred to FMS Wertmanagement but which were not able to be transferred via the originally envisaged method as a result of various considerations, including considerations of tax law. In 2010, the credit risks of these assets was transferred by means of guarantees provided by FMS Wertmanagement, so that HRE ultimately retains a counterparty risk with regard to FMS Wertmanagement in connection with these positions.

To properly reflect the actual economic risk in HRE Group, the above-mentioned EaDs which are not considered as core exposure and which are attributable to back-to-back transactions with FMS Wertmanagement as well as the positions guaranteed by FMS Wertmanagement have been detailed merely for information purposes in the following overviews of the portfolio development and structure by means of footnotes.

Considering the above-mentioned restrictions the EaD for the total exposure of pbb Group amounted to €66.9 billion as of 31 December 2013 (31 December 2012: €75.3 billion).

Overview of the Total Exposure of pbb Group: €66.9 billion EaD The credit portfolio is broken down into the following segments:

> Real Estate Finance (REF)
> Public Sector Finance (PSF)
> as well as the non-strategic segment Value Portfolio (VP) which is earmarked for being wound down

In addition to the internal reconciliation and consolidation positions, «Consolidation & Adjustments» shows the EaD for transactions which are not directly attributable to the operating segments. These are basically asset positions for asset and liability management.

As of 31 December 2013, 75% of the EaD in «Consolidation & Adjustments» was attributed to the rating classes AAA to AA– and 15% of the EaD was attributed to the rating classes A+ to A–. 10% of the EaD was in the rating classes BBB+ and worse. 99% of the exposures in the ratings categories BBB+ and worse were classified as investment grade.

Total portfolio: EaD according to business segments

in € billion	31.12.2013[1]	31.12.2012[2]	Δ in € bn
Real Estate Finance	22.5	23.7	–1.2
Public Sector Finance	32.9	38.9	–6.0
Value Portfolio	0.1	0.3	–0.2
Consolidation & Adjustments	11.4	12.4	–1.0
Total	**66.9**	**75.3**	**–8.4**

[1] In addition €0.6 billion EaD with regard to the counterparty FMS Wertmanagement including guaranteed positions of €0.6 billion (PSF: €0.03 billion; VP: €0.6 billion)
[2] in addition €0.9 billion EaD with regard to the counterparty FMS Wertmanagement including guaranteed positions of €0.7 billion (PSF: €0.2 billion; VP: €0.7 billion)

As of 31 December 2013 the total exposure at default (EaD) of pbb Group decreased compared to year-end 2012 by €8.4 billion to €66.9 billion. The relative proportion of the EaD accounted for by the Real Estate Finance segment rose overall (34%; year-end 2012: 31%), whereas there were slight percentage decreases in the Public Sector Finance segment (49%; year-end 2012: 52%) and the Value Portfolio segment (0.2%; year-end 2012: 0.4%). The proportion of the EaD accounted for by «Consolidation & Adjustments» remained relatively constant compared with the prior-year reporting date, at 17%.

The portfolio of PSF had an EaD of €32.9 billion as of 31 December 2013 (31 December 2012: €38.9 billion); of this figure €8.3 billion (31 December 2012: €8.4 billion) was attributable to the strategic Public Investment Finance portfolio. From the remaining portfolio an EaD of €23.5 billion (31 December 2012: €28.6 billion) was related to the non-strategic portfolio of budget financing earmarked for streamlining. The residual amount was attributable to netting positions with financial institutions.

Risk Parameters **Expected Loss** The expected loss (EL), which is calculated on the basis of the annual probability of default (PD), the loss-given default (LGD) and the exposure at default (EaD), is stated as €168 million as of 31 December 2013 using the parameters defined under Basel II (31 December 2012: €125 million). The increase in the expected loss is primarily attributable to the default of two larger refinancing arrangements in the Real Estate Finance segment, as well as to the rating downgrade of a regional government in Portugal.

The expected loss for a time period of one year is calculated for the entire exposure, with the exception of trading book positions and non-performing loans for which an individual allowance has already been recognised. The figure was split to the segments as follows:

Total exposure: expected loss by business segments

in € million	31.12.2013	31.12.2012	△ in € million
Real Estate Finance	136	103	+33
Public Sector Finance	31	21	+10
Value Portfolio	–	–	–
Consolidation & Adjustments	1	1	–
Total	**168**	**125**	**+43**

It has to be stated that future changes, for instance in the economy, may result in changes in the EL figures stated above. This is a further reason why realised losses can differ from the expected losses.

Economic Credit Risk Capital The economic capital for credit risk is calculated with the credit portfolio model. It amounted to €237 million (31 December 2012: €226 million) in the going-concern approach thus considering a confidence level of 95% and a period of one year, disregarding diversification effects to other risk types. Details regarding the calculation are set out in the section «Result of Risk-bearing Capacity Analysis».

Regional Breakdown of the Portfolio At the reporting date, the main focus of the exposure of pbb Group was unchanged on Western Europe. Germany continued to account for most of the overall exposure, with 49% (€32.8 billion). The main items in the category «Other Europe», which accounted for approximately 15% (€9.9 billion) of the overall portfolio, were Austria (€5.9 billion; 31 December 2012: €6.3 billion) and Sweden (€1.2 billion; 31 December 2012: €1.6 billion) followed by Belgium (€0.5 billion; 31 December 2012: €0.5 billion).

The €0.6 billion decline in the category «Other Europe» was mainly due to maturing loans in Sweden (€1.2 billion; 31 December 2012: €1.6 billion) and maturing loans and borrower's note loans in Austria (€5.9 billion; 31 December 2012: €6.3 billion). In contrast, new business in Denmark and Finland led to an increase within the category «Other Europe».

The decline in the exposure in France as against year-end 2012 to €5.3 billion (31 December 2012: €7.6 billion) is mainly due to the early repayment of a borrowers' note loan from the public sector cover pool. This was largely offset, with the remaining assets required for the public sector cover pool being met by buying liquid European government bonds from Spain and France with short maturities. New business in the UK exceeded the items due, resulting in a net increase of €0.3 billion.

Compared with the previous year the percentage of the category «Emerging Markets» in accordance with the IMF definition remained stable and mainly comprised Poland with €2.0 billion (31 December 2012: €2.0 billion) and Hungary with €0.8 billion (31 December 2012: €0.7 billion).

Total portfolio: EaD by regions

in € billion	**31.12.2013**[1]	**31.12.2012**[2]	Δ in € bn
Germany	32.8	36.7	−3.9
Other Europe[3]	9.9	10.5	−0.6
France	5.3	7.6	−2.3
Spain	4.9	4.6	+0.3
Great Britain	4.2	3.9	+0.3
Italy	3.1	3.3	−0.2
Emerging markets[4]	2.9	3.0	−0.1
Other	1.7	2.2	−0.5
Portugal	1.4	1.6	−0.2
USA	0.4	0.7	−0.3
Japan	0.3	1.1	−0.8
Ireland	0.0	0.1	−0.1
Total	**66.9**	**75.3**	**−8.4**

[1] In addition €0.6 billion EaD with regard to the counterparty FMS Wertmanagement including guaranteed positions of €0.6 billion. The figures without guaranteed positions were fully attributable to Germany (€0.01 billion), the guaranteed positions related to Germany (54%, €0.3 billion) and Italy (46%, €0.3 billion)

[2] In addition €0.9 billion EaD with regard to the counterparty FMS Wertmanagement including guaranteed positions of €0.7 billion. The figures without guaranteed positions were fully attributable to Germany (€0.2 billion), the guaranteed positions related to Germany (53%, €0.4 billion) and Italy (47%, €0.3 billion)

[3] Comprises among others Austria, Belgium, Switzerland, Sweden, Denmark, Finland and the Netherlands

[4] Emerging markets in accordance with the IMF definition

Depending on the results of the internal rating process, maximum limits in certain rating ranges are defined for each individual country or groups of countries; these limit the business operations of pbb Group. All country ratings and country limits are reviewed at least once every year by Risk Management & Control.

Issuer Risk The bonds, borrowers' note loans and structured loans in the portfolio are broken down according to region for the purpose of classifying the EaD according to issuer risk. The EaD is attributed on the basis of the domicile of the issuer. The EaD according to issuer risk amounted to €36.0 billion as of 31 December 2013, and was thus lower than the corresponding figure at the end of 2012 (€43.5 billion). Western Europe accounted for most of the exposure, whereby Germany accounted for the highest figure (€ 14.2 billion; 31 December 2012: € 18.3 billion).

The main country under «Other Europe» was Austria (€5.8 billion; 31 December 2012: €6.2 billion), followed by Belgium with €0.5 billion (31 December 2012: €0.5 billion). The decline in the «Other Europe» item is almost solely attributable to Austria and is due to maturing bonds and the repayment of borrower's note loans (€–0.4 billion).

The largest decline in the portfolio in terms of the issuer risk broken down according to regions was seen in Germany, and is due to the repayment of promissory note loans and bonds which fell due (€–4.1 billion). The decline in the exposure in France as against year-end 2012 to €2.7 billion (31 December 2012: €5.0 billion) is mainly due to the early repayment of a borrowers' note loan from the public sector cover pool. This was largely offset, with the remaining assets required for the public sector cover pool being met by buying liquid European government bonds from Spain and France with short maturities.

With regard to the breakdown of issuer risk according to segments, the Public Sector Finance segment accounted for 87% of the EaD at the end of 2013 (December 2012: 85%) and Consolidation & Adjustments accounted for 13% (December 2012: 15%).

Total portfolio: issuer risk according to regions

in € billion	31.12.2013[1]	31.12.2012[2]	Δ in € bn
Germany	14.2	18.3	–4.1
Other Europe[3]	7.2	7.5	–0.3
Spain	4.4	4.0	0.4
Italy	2.9	3.1	–0.2
France	2.7	5.0	–2.3
Other	1.6	2.0	–0.4
Portugal	1.4	1.6	–0.2
Emerging markets[4]	1.1	1.2	–0.1
Great Britain	0.3	0.3	–
Japan	0.2	0.5	–0.3
Total	**36.0**	**43.5**	**–7.5**

[1] In addition €0.3 billion EaD with regard to the counterparty FMS Wertmanagement representing guaranteed positions which were fully attributable to Germany
[2] In addition €0.4 billion EaD with regard to the counterparty FMS Wertmanagement representing guaranteed positions which were fully attributable to Germany
[3] Comprises among others Austria, Belgium, Switzerland, Sweden, Denmark, Finland and the Netherlands
[4] Emerging markets in accordance with the IMF definition

Real Estate Finance: € 22.5 billion EaD Portfolio Development and Structure The EaD of the Real Estate Finance portfolio of the pbb Group declined by € 1.2 billion compared with 31 December 2012. The customer derivatives included in the portfolio reported an EaD of € 0.4 billion as of 31 December 2013 compared with an EaD of € 0.7 billion at the end of 2012.

Whereas the absolute figure for Great Britain increased slightly compared with the previous year reference date, there was a decline in the absolute figure for Japan, France, «Other Europe» as well as for «Emerging Markets». The exposure of Germany, Spain, Italy and Portugal remained stable. The decline of the EaD in Japan was mainly due to repayment of loans (€ 0.1 billion; 31 December 2012: € 0.6 billion) and the decline in «Other Europe» mainly due to maturing loans in Sweden (€ 1.1 billion; 31 December 2012: € 1.6 billion).

Real Estate Finance: EaD by regions[1]

in € billion	31.12.2013[2]	31.12.2012[3]	△ in € bn
Germany	12.1	12.1	–
Great Britain	3.6	3.4	+0.2
Other Europe[4]	2.4	2.8	−0.4
France	1.8	2.2	−0.4
Emerging markets[5]	1.8	1.9	−0.1
Spain	0.5	0.5	–
Italy	0.2	0.2	–
Japan	0.1	0.6	−0.5
Portugal[6]	0.0	0.0	–
Total	**22.5**	**23.7**	**−1.2**

[1] In the Real Estate Finance segment, there was no exposure to the counterparty FMS Wertmanagement
[2] Breakdown including customer derivatives of approx. € 0.4 billion
[3] Breakdown including customer derivatives of approx. € 0.7 billion
[4] Comprises among others Austria, Belgium, Switzerland, Sweden, Denmark, Finland and the Netherlands
[5] Emerging markets in accordance with the IMF definition
[6] In Portugal € 0.03 billion EaD in the segment Real Estate Finance

The introduction of the «mixed use» category led to shifts within the property types, mainly between the office buildings, retail and mixed use categories. The category «Mixed use», which reflects the mixed use of a property, has been shown separately now.

The breakdown of the portfolio by property type as at 31 December 2013 changed only slightly as against year-end 2012, taking into account the introduction of the «mixed use» category. The main items were the property types «Office buildings» with € 7.0 billion EaD or 31 % of the overall REF portfolio (31 December 2012: € 7.5 billion or 32 %) and «Retail» with € 6.2 billion EaD or 28 % of the REF portfolio (31 December 2012: € 6.9 billion or 29 %). The percentage of properties with residential use remained more or less stable at 22 % compared to the end of 2012 (21 %). Worth mentioning is also the percentage of 8 % of the property type «Logistics/Storage» (31 December 2012: 12 %).

Real Estate Finance: EaD by property type[1] in € billion	**31.12.2013**	**31.12.2012**	∆ in € bn	**31.12.2012**[2]
Office buildings	7.0	8.5	−1.5	7.5
Retail	6.2	6.1	+0.1	6.9
Housing construction	4.9	5.0	−0.1	5.0
Logistics/storage	1.8	1.7	+0.1	2.8
Other	1.2	1.1	+0.1	1.2
Mixed use	1.0	1.0	–	–
Hotel/leisure	0.4	0.3	+0.1	0.3
Total	**22.5**	**23.7**	**−1.2**	**23.7**

[1] In the Real Estate Finance segment there was no exposure to the counterparty FMS Wertmanagement
[2] Basis of figures: Annual Report of pbb Group as of 31 December 2012

At the end of the year 2013 the portfolio was still dominated by investment financing (92%; 31 December 2012: 94%). Higher risk construction projects in the building phase (construction financing) only accounted for 5% of the EaD (31 December 2012: 3%). Real Estate Finance for which the capital is serviced mainly out of the current property cash flow is shown under investment financing.

Real Estate Finance: EaD by loan type[1] in € billion	**31.12.2013**	**31.12.2012**	∆ in € bn
Investment financing	20.6	22.3	−1.2
Construction financing	1.2	0.6	+0.6
Customer derivatives	0.4	0.7	−0.2
Other	0.2	0.1	+0.1
Total	**22.5**	**23.7**	**−0.3**

[1] In the Real Estate Finance segment there is no exposure to the counterparty FMS Wertmanagement

Risk Parameters Using the parameters defined under Basel II, the expected loss for the Real Estate Finance portfolio was €136 million as of 31 December 2013 (31 December 2012: €103 million). The increase in the expected loss is primarily attributable to the default of two larger loans.

Public Sector Finance: € 32.9 billion EaD Portfolio Development and Structure The portfolio of the Public Sector Finance segment (PSF) had an EaD of € 32.9 billion as of 31 December 2013 (31 December 2012: € 38.9 billion); of this figure, € 8.3 billion were attributable to the strategic portfolio of Public Investment Finance (31 December 2012: € 8.4 billion). From the remaining portfolio an EaD of € 23.5 billion was related to the non-strategic portfolio of budget financing earmarked for streamlining (31 December 2012: € 28.6 billion). The residual amount was attributable to netting positions with financial institutions.

Most of the exposure was reported for Western Europe with an emphasis on Germany. The percentage of the countries in this segment remained stable with smaller exceptions. The major part of «Other Europe» represented as in the year before Austria with € 5.7 billion (31 December 2012: € 5.9 billion). The EaD in Italy, Portugal and Spain decreased slightly due to a reduction of deals in these countries. The decline in the exposure in France as against year-end 2012 to € 2.9 billion (31 December 2012: € 5.0 billion) is mainly due to the early repayment of a borrowers' note loan from the public sector cover pool. The exposure in the USA related entirely to financial institutions located in the USA.

Public Sector Finance: EaD by regions

in € billion	31.12.2013[1]	31.12.2012[2]	Δ in € bn
Germany	12.0	13.8	−1.8
Other Europe[3]	7.1	7.2	−0.1
Spain	3.7	4.1	−0.4
France	2.9	5.0	−2.1
Italy	2.9	3.1	−0.2
Portugal	1.4	1.6	−0.2
Other	1.1	1.5	−0.4
Emerging markets[4]	1.1	1.1	–
Japan	0.3	0.4	−0.1
Great Britain	0.2	0.5	−0.3
USA	0.2	0.5	−0.3
Ireland[5]	0.0	0.1	−0.1
Total	**32.9**	**38.9**	**−6.0**

[1] In addition € 0.03 billion EaD with regard to the counterparty FMS Wertmanagement, which was fully attributable to Germany; including guaranteed positions of € 0.01 billion

[2] In addition € 0.2 billion EaD with regard to the counterparty FMS Wertmanagement, which was fully attributable to Germany; including guaranteed positions of € 0.01 billion

[3] Comprises among others Austria, Belgium, Switzerland, Sweden, Denmark, Finland and the Netherlands

[4] Emerging markets in accordance with the IMF definition

[5] The EaD in Ireland amounted to € 0.02 billion

The position «Public Sector Borrowers» included receivables due from sovereigns (35%), public sector enterprises (21%) and municipalities (44%).

Public Sector Finance: EaD by counterparty structure

in € billion	31.12.2013[1]	31.12.2012[2]	Δ in € bn
Public sector borrowers	23.4	27.3	−3.9
Financial institutions[3]/insurance companies	6.6	8.2	−1.6
State-regulated companies[4]	2.9	3.4	−0.5
Total	**32.9**	**38.9**	**−6.0**

[1] In addition €0.03 billion EaD with regard to the counterparty FMS Wertmanagement, which was fully attributable to Germany; including guaranteed positions of €0.01 billion
[2] In addition €0.2 billion EaD with regard to the counterparty FMS Wertmanagement, which was fully attributable to Germany; including guaranteed positions of €0.01 billion
[3] Financial institutions with a state background or state guarantee
[4] Water utilities, power supply utilities, etc.

As of the reporting date, the PSF segment again included a high proportion of public sector borrowers, which is reflected in the rating. 50% (31 December 2012: 58%) of the EaD was attributable to the rating classes AAA to AA–. The rating classes A+ to A– accounted for 18% of the EaD (31 December 2012: 14%). The figure for positions rated BBB+ or worse declined in absolute terms but rose as a percentage, from 28% in December 2012 to 32% in December 2013, due to the disproportionately strong decline in positions rated AAA to AA–.

Public Sector Finance: EaD by internal ratings

in € billion	31.12.2013[1]	31.12.2012[2]	Δ in € bn
AAA to AA–	16.4	22.5	−6.1
A+ to A–	6.1	5.5	+0.6
BBB+ and worse	10.4	10.9	−0.5
Total	**32.9**	**38.9**	**−6.0**

[1] In addition €0.03 billion EaD to the counterparty FMS Wertmanagement, which was fully attributable to the rating classes AAA to AA–
[2] In addition €0.2 billion EaD to the counterparty FMS Wertmanagement, which was fully attributable to the rating classes AAA to AA–

Risk Parameters The expected loss for the portfolio of the Public Sector Finance segment was €31 million over the one-year period (31 December 2012: €21 million). The increase is attributable to the rating downgrade of a regional government in Portugal.

Value Portfolio: €0.14 billion EaD Portfolio Development and Structure The Value Portfolio comprises non-strategic portfolios of pbb Group as well as a part of the transactions which exist with the counterparty FMS Wertmanagement. The portfolio structure is inter alia affected by derivative business with financial institutions.

The continued strategic decline of €0.16 billion in the exposure as of 31 December 2013 compared with 31 December 2012 was mainly attributable to the decrease of the exposure of almost all countries – especially of Germany and the USA. In the remaining portfolio as of 31 December 2013 the focus was also on Germany. The exposure in the USA was almost completely eliminated. The increase in the «Other» category was due to internal reclassification.

Value Portfolio: EaD by regions

in € billion	31.12.2013[1]	31.12.2012[2]	△ in € bn
Germany	0.12	0.16	−0.04
Other Europe[4]	0.01	0.01	–
Other	0.01	0.00	+0.01
USA[3]	0.00	0.11	−0.11
Great Britain	0.00	0.01	−0.01
Ireland	0.00	0.01	−0.01
France[3]	0.00	0.00	–
Total	**0.14**	**0.30**	**−0.16**

[1] In addition €0.6 billion EaD to the counterparty FMS Wertmanagement, which were fully guaranteed; the guaranteed positions related to Germany (52%) and Italy (48%)
[2] In addition €0.7 billion EaD to the counterparty FMS Wertmanagement, which were fully guaranteed; the guaranteed positions related to Germany (54%) and Italy (46%)
[3] Because of the rounding of the second position after the decimal point the following exposure is not shown in the table: exposure against France: €0.001 billion; USA: €0.003 billion
[4] Comprises Switzerland, Sweden and the Netherlands

Value Portfolio: EaD by counterparty structure

in € billion	31.12.2013[1]	31.12.2012[2]	△ in € bn
Financial institutions/insurance companies	0.05	0.18	−0.13
Companies	0.05	0.07	−0.02
Public sector borrowers	0.04	0.05	−0.01
Total	**0.14**	**0.30**	**−0.16**

[1] In addition €0.6 billion EaD to the counterparty FMS Wertmanagement, which were fully guaranteed; the guaranteed positions related to Germany (52%) and Italy (48%)
[2] In addition €0.7 billion EaD to the counterparty FMS Wertmanagement, which were fully guaranteed; the guaranteed positions related to Germany (54%) and Italy (46%)

Risk Parameters The expected loss for the value portfolio amounted to €0.1 million as of 31 December 2013 using the parameters defined under Basel II (31 December 2012: €0.2 million).

Structured Products

pbb Group's residual holdings in fully state-guaranteed collateralised debt obligations had a notional value of €0.7 billion as of 31 December 2013 (31 December 2012: €0.8 billion) and an actual fair value of €0.7 billion (31 December 2012: €0.7 billion).

The residual holdings of pbb Group of non-state-guaranteed structured securities, namely credit-linked investments in the form of collateralised debt obligations (CDOs in the narrower sense of the term), remained stable in comparison with the end of the year 2012 with a notional value of €0.1 billion. The fair value of these securities which were almost completely written down and securitise credit risks amounted to €4 million as of 31 December 2013 (31 December 2012: €8 million).

The valuation of assets was essentially based on market values.

Consolidated Special-purpose Vehicle without Capital Share in pbb Group

The special-purpose vehicle is an ABS structure which has been completely written down so that no further risks can result for pbb Group from this special-purpose vehicle (31 December 2013: nominal €0.4 billion, 31 December 2012: nominal €0.4 billion). The consolidation of the special-purpose vehicle had resulted in particular in a balance sheet extension of €0.3 billion (31 December 2012: €0.4 billion). However, from the risk point of view, there had not been an increase in the volume. Accordingly, the volume exposed to risk was €0.3 billion lower (31 December 2012: €0.4 billion).

Watchlist and Non-performing Loans

Early Warning System The early warning system of pbb Group has defined triggers (= criteria) for including loans in the watchlist and for being classified as workout loans (e.g. past due payments, failure to meet covenants – e.g. loan-to-value (LTV), interest service coverage (ISC)). The system constantly monitors whether a trigger has been set off. In the event of any problems being identified, the counterparty is analysed and, where appropriate, promptly transferred to restructuring or workout loans. Watchlist and non-performing loans (restructuring and workout loans) are defined as follows:

> Watchlist Loans Payments past due by more than 60 days or another defined early warning signal is triggered.
> Restructuring Loans Payments past due by more than 90 days or another defined early warning signal is triggered.
> Workout Loans There are no indications that the loan can be restructured. Enforcement measures have been/will be introduced, respectively individual allowances have been created or are planned.

Non-performing loan processing is also responsible for carrying out an impairment test in line with the relevant accounting regulations.

Development of Watchlist and Non-performing Loans of pbb Group

Watchlist and non-performing loans of pbb Group[1]	31.12.2013				31.12.2012				
EaD in € million	REF	PSF	VP	Total	REF	PSF	VP	Total	Δ in € million
Workout loans	6	–	–	6	11	–	–	11	−5
Restructuring loans[2]	932	–	2	934	1,076	–	3	1,079	−145
Non-performing loans[2]	**938**	**–**	**2**	**940**	**1,087**	**–**	**3**	**1,090**	**−149**
Watchlist loans	142	454	–	596	857	641	–	1,498	−902
Total	**1,080**	**454**	**2**	**1,536**	**1,944**	**641**	**3**	**2,588**	**−1,052**

[1] Reported in accordance with the supervisory treatment, including a Spanish financing arrangement that must, however, be consolidated in accordance with IFRS

[2] In addition €6 million EaD as of 31 December 2012 and as of 31 December 2013 in the segment Consolidation & Adjustments

The watchlist and non-performing loans decreased by a total of € 1,052 million net.

Watchlist loans declined by € 1,014 million gross[1] or € 902 million net. € 552 million relates to loans settled or transferred back to standard processing in the REF segment, of which € 423 million is attributable to only two loans. In the PSF segment, a Spanish bond in the amount of € 100 million was repaid as scheduled. In addition, € 86 million was transferred back to standard processing from intensive care. € 275 million had to be downgraded to non-performing loans. Additions amounted to € 112 million, of which € 71 million was due to the transfer of one customer back to watchlist loans from non-performing loans.

Problem loans declined by € 475 million gross or € 149 million net. Loans totalling € 475 million were successfully restructured or repaid including one fully covered receivable in the amount of € 116 million, which was eliminated by utilising a valuation allowance recognised in other comprehensive income. Exposures totalling € 326 million had to be transferred to non-performing loans, of which € 275 million came from intensive care and € 51 million from standard processing.

Impairments and Provisions

Individual Allowances and Portfolio-based Allowances All financial assets which are not evaluated at fair value through profit or loss are subject to a regular impairment test. An assessment is first made to determine whether there is an objective indication of an impairment. The extent of any such impairment is then calculated as the difference between the carrying amount, at AfS assets (AfS = available for sale) plus AfS reserve, and the present value of the cash flows expected in future.

Portfolio-based allowances are calculated using risk parameters which are compliant with Basel II, such as probability of default (PD) and loss-given default (LGD). The resultant expected loss in relation to a time horizon of one year is scaled using an IFRS-compliant conversion factor to the period which on average is required for identifying the impairment event in the pbb.

If differences are identified between long-term average values for the parameters PD and LGD on the one hand and the current figures on the other as a result of the market environment in some portfolios of the operating segments, these are taken into consideration accordingly.

[1] Excluding opposite effects

The individual allowances are approved in the Group Risk Provisioning Committee.

Risk Provisioning of pbb Group An overview of the development in provisions for losses on loans and advances and provisions is set out in the notes.

Coverage for Non-performing Loans[1)]

The coverage ratio is defined as the ratio between the provisions created in relation to the non-performing exposures (including the residual volume of structured products as part of the value portfolio) and the EaD or, with regard to the structured products, the nominal amount.

The non-performing loans in the Real Estate Finance segment were covered by 26% (31 December 2012: 35%). The decline is primarily due to the relatively large decrease in valuation allowances compared to the volume of problem loans as a result of the utilisation of a valuation allowance recognised in other comprehensive income to eliminate a fully covered financing arrangement in the REF segment.

The non-performing loans in the Real Estate Finance segment were covered by 19% (31 December 2012: 30%). As in the year before there were no non-performing loans in the Public Sector Finance segment as of 31 December 2013. In the Value Portfolio the non-performing loans were covered by 96% (31 December 2012: 92%).

Opportunities

The parameters for the risk dimensions for the credit risk are defined using statistical methods on the basis of numerous historical observations. The risk measures also depend on assumptions relating to future developments of micro-economic factors as well as developments on the credit markets. It is in the nature of things and is also in line with historical experience that there is a certain probability that such economic conditions perform more positively than originally assumed and that the potential losses arising from the credit risk therefore tend to be less than originally quantified by the risk measures. Such potentially positive developments then represent opportunities for pbb Group which can be utilised for reducing risk.

In specific terms, there are opportunities if fewer loans in future are affected by a default in performance than had originally been assumed as part of the risk quantification process.

There are also opportunities if there are in future fewer migrations to less positive rating categories than originally assumed.

There are also opportunities if the loss ratios of non-performing loans in future are lower than was originally assumed as part of the risk quantification process. Lower loss ratios may be triggered by various positive developments. Firstly, it is possible that the process of disposing of securities might generate higher proceeds than was originally assumed in the risk quantification process. Secondly, it is possible that a higher percentage of non-performing loans subsequently become performing loans again without any losses than had been the case in the past.

[1)] Reported in accordance with the supervisory treatment, including a Spanish financing arrangement that must, however, be consolidated in accordance with IFRS.

In addition to positive developments in terms of default rates and loss ratios, there are also opportunities in the context of the credit risk if the exposure values decline in the portfolio. This can for instance be the case if borrowers redeem or repay their loans more quickly than would have been expected on the basis of contractual agreements or on the basis of past experience. Exposure values can decline in the derivative portfolio if changes in certain market parameters, such as interest rates or exchange rates, mean that there is a decline in the market values of those positions which are associated with a replacement risk.

According to the given structure of maturities of the existing portfolio in the Public Sector Finance segment a decline in EaD of €0.2 billion can be expected for the financial year 2014 with regard to Slovenia, Portugal and Spain. This reduction in exposure means that there is an opportunity of being less affected by potential further rating downgrades in the above-mentioned countries.

Market Risk

Definition

Market risk is defined as the risk of a loss of value resulting from the fluctuation of the market prices of financial instruments. Transactions of pbb Group are mainly exposed to the following risk types:
> Credit spread risk
> General interest rate risk
> Inflation risk
> Foreign currency risk
> Collateral currency risk (basic risk)

Market Risk Strategy

pbb Group follows the following fundamental principles in relation to market risks:
> Transactions may be conducted only in financial instruments which are measured independently via a model or for which market prices are observable and they must have successfully passed through the new product process.
> All transactions are subject to daily income statement and risk monitoring by Risk Management & Control.

Organisation of Market Risk Management

The transactions are monitored by Risk Management & Control which is separated from trading in the structure organisation right through to the level of the management.

Market Risk Reports

Risk Management & Control daily prepares extensive market risk reports for various recipients:
> The daily market risk report is addressed particularly to the Management Board. It shows market risk value at risks (VaR), limit utilisations and economic performance figures on all levels of the portfolio structure
> Daily sensitivity reports comprise analyses for the main risk factors at various levels. They are also made available to the Management Board.

Measurement and Limiting of Market Risk

Market Risk Value at Risk Risk Management & Control uses a variance-covariance approach to calculate the market risk VaR at the overall and sub-portfolio level on a daily basis. All positions are taken into account, whereby the credit spread VaR from positions which are included in the IFRS category Loans & Receivables is not taken into consideration within market risk, but in credit risk.
> The correlations and volatilities which are used are based on historical time series of the previous 250 trading days, that are included in the calculation on an equally weighted basis.
> The historically observed correlations are used when the individual market risk components are aggregated to an overall VaR, which constitutes the basis for the limit monitoring.
> For the daily operational risk management, the VaR relates to a holding period of ten days and a one-sided 99% confidence interval.

On 31 December 2013 the market risk VaR amounted to €74 million. The comparison figure as of 31 December 2012 was €104 million. In the period under review there were no limit violations. The market risk limit remained constant throughout 2013, at €150 million.

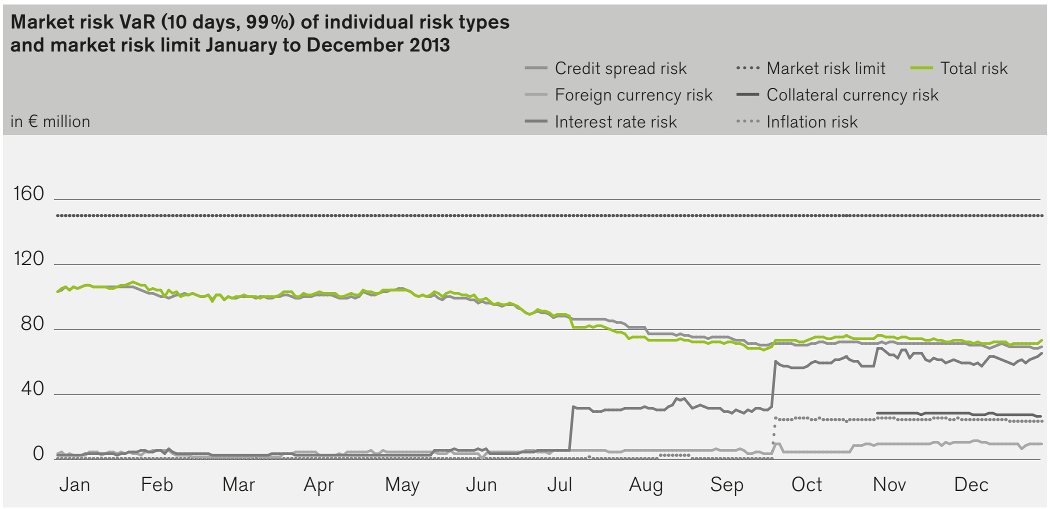
In 2013 the development in the market risk VaR was mainly affected by the change in credit spread volatilities. After remaining relatively constant in the first half of 2013, market risk VaR declined in the third quarter of 2013 as a result of lower credit spread volatility before again staying relatively constant in the last quarter. In addition, changes occurred that did not lead to a material change in overall market risk VaR due to diversification effects between the individual types of market risk, but that had a significant impact on some individual types of market risk. Value-at-risk measurement was expanded to include cross-currency basis risk and (single-currency) tenor spread risk in 2013. Both types of market risk only had a relatively low value at risk, at €7 million for cross-currency basis risk and €0.4 million for tenor spread risk at the respective introduction dates.

The equity contribution items that were previously reported separately have been included in value-at-risk limit setting since July 2013. This led to a significant increase in interest rate VaR as at the introduction date. In September 2013, an inflation-linked swap was unwound and the associated inflation-linked bond was transferred to the equity contribution register, which led to another significant increase in interest rate VaR and inflation VaR.

Overnight yield curves (including tenor basis effects) were used for the first time in the measurement relevant to the sensitivity analysis. As a result, the calculation of value at risk also takes into account risks arising from the divergence of the currency of the hedged item and the collateral (collateral currency risk).

The following diagram illustrates the development of the market risk VaR as well as the VaR for the individual risk types compared with the market risk limit during the year.

Market risk VaR (10 days, 99%) of individual risk types and market risk limit January to December 2013



The VaR assessment is complemented by further instruments such as sensitivity analyses, back testing as well as stress testing.

Sensitivity Analyses Sensitivity analyses quantify the impact of a change in individual market parameters on the value of the positions. For instance, the credit spread sensitivity provides an indication of the change in economic present value which results from an isolated change of one basis point in the credit spreads which are relevant for measurement purposes.

Stress Testing Whereas the VaR measurement simulates the market risk under «normal» market conditions and cannot be used as a measure for a potentially maximum loss, stress scenarios show the market risk under extreme conditions. At pbb Group hypothetical stress scenarios are calculated on a monthly basis for major key risk drivers. In addition historical stress scenarios are simulated. For example, a parallel shift of 200 basis points upwards in the interest rate curve for all positions of pbb Group would have resulted in a loss of approximately €452 million as of 31 December 2013 (year-end 2012: €208 million). The higher market value losses compared with the previous year are mainly due to the increase in interest rate sensitivity in the equity contribution register, which is primarily attributable to unwinding of the swap and the transfer of the associated inflation-linked bond to the equity contribution register as described above. An opposite parallel shift of 200 basis points downwards in the interest rate curve would have resulted in a market value gain of €307 million (year-end 2012: €87 million). The asymmetrical relationship between the potential gain or loss primarily reflects the fact that the shift of 200 basis points described above is only performed at a maximum up to an interest rate of 0%. The Management Board and the corresponding executive bodies are regularly notified of the results of the scenario analyses.

Back Testing The quality of the methods used to measure risk is continually reviewed and, where necessary, optimised on the basis of the daily comparison between the VaR figures and the subsequent actual changes in the present value of the portfolio. pbb Group has adopted the Basel Capital Accord's traffic light system for the quantitative analysis of its risk model. This counts the number of statistical (negative) outliers detected in backtesting within a period of 250 trading days. Overall, one outlier was observed in 2013, which was attributable to an unusually strong credit spread and exchange rate movement. pbb's risk model therefore achieved a traffic light rating of «green» under the Basel Capital Accord's traffic light system.

Economic Market Risk Capital For calculating the economic market risk capital, the market risk VaR for the going-concern approach is calculated for a period of one year and for a confidence level of 95%. The economic capital for market risks of pbb Group, disregarding diversification effects for other risk types, amounted to €185 million as of 31 December 2013 (31 December 2012: €171 million).

Reflection and Recognition of Economic Hedges as On-balance-sheet Hedges

Hedge accounting is defined as the special accounting regulations for hedges of IAS 39, the aim of which is to ensure that the changes in value of the hedged underlyings and hedging instruments cancel each other out to a large extent. The criteria of IAS 39 must be satisfied for the on-balance-sheet recognition of hedges. These criteria, such as the requirements relating to the effectiveness of a hedge, are to a certain extent not consistent with the methods used in bank management. There may therefore be differences between the economic hedges and the on-balance-sheet hedges.

Market Risk Management, Monitoring and Reduction

pbb Group uses a three-pillar approach for managing and monitoring the market risk:
> Management of the position in Treasury
> Risk measurement and monitoring compliance with limits by Risk Management & Control
> Escalation processes across all decision-making committees right through to the Management Board

For all positions market risk is monitored by a combination of value-at-risk (VaR) limits and monitoring of sensitivities by trade-independent Risk Management & Control.

General Interest Rate Risk Due to the effects mentioned above (inclusion of the equity contribution and unwinding of the swap and transfer of the associated inflation-linked bond to the equity contribution register) the overall interest rate risk rose significantly in 2013. It amounted to €65 million as at 31 December 2013, well above the figure as at 31 December 2012 (€2 million). Including the equity contribution register, the figure as at year-end 2012 would have been €17 million. The average interest rate risk in 2013 was €25 million (maximum €68 million, minimum €2 million). In the previous year, the interest rate risk averaged €3 million (maximum €11 million, minimum €1 million). Excluding the equity contribution register, the general interest rate risk remained low throughout 2013.

As in the previous year, non-linear interest rate risks from capital market transactions were negligible (year-end 2013: €0.4 million).

Credit Spread Risk The credit spread risk shows the potential change in the present value of exposures as a result of changes to the corresponding credit spread. Most of the credit spread risk was attributable to assets eligible as cover for Pfandbriefe. The Bank has risk measurement systems for calculating credit spread risk for all relevant exposures. Subject to VaR limitation are only the credit spread risks of AfS and dFVTPL stocks but not the LaR positions.

The credit spread VaR for the AfS and dFVTPL portfolios at the end of December 2013 declined year-on-year to €69 million, mainly as a result of lower credit spread volatility (year-end 2012: €103 million).

Other Market Risks Collateral currency risk has been measured since the changeover to present value calculation on the basis of OIS yield curves and amounted to €27 million as at 31 December 2013. Inflation risk rose significantly, mainly as a result of the unwinding of the inflation-linked swap described above, and amounted to €23 million as at 31 December 2013. The present value of the foreign currency risk was €9 million as at 31 December 2013, while tenor spread risk was €2 million as at year-end 2013. The Bank is not exposed to share price or commodity risk. Financial derivatives are mainly used for hedging purposes.

Opportunities

As detailed above, the sensitivities result in a VaR, i.e. a possible future (economic) loss in the event of an unfavourable market development. It has to be mentioned that these sensitivities may also result in economic gains in the event of a positive market development. Accordingly, the assets of the cover pools for instance result in high negative credit spread sensitivities which pose a risk. In the event of a reduction of the relevant credit spreads, these credit spread sensitivities result in economic profits, which again constitute an opportunity.

Within the framework of the hypothetical stress scenarios of pbb Group an opposite parallel shift of 200 basis points downwards in the interest rate curve would comprise the opportunity for a market value gain of €307 million.

Outlook

As set out in the risk strategy, foreign currency, inflation and interest rate risk (excluding the equity contribution) have to remain on a low level or to be reduced if new business were to cause market risk to increase too strongly. Credit spread risks are due to the assets in the cover pools for the German Pfandbrief and are thus an inherent factor for the business model of pbb.

Liquidity Risk

Definition

Liquidity risk is defined as the risk of not being able to meet the extent and deadlines of existing or future payment obligations in full or on time.

Liquidity Risk Strategy

The liquidity risk strategy is a key component of the risk strategy of pbb Group and is broken down into various modules. This ensures that the short- as well as the mid-term funding of pbb Group is monitored and controlled by means of a limit system. The limits are defined as part of the annual business planning process.

Organisation of Liquidity Risk Management

Risk Management & Control identifies, measures, reports and monitors the liquidity risk of pbb Group. Management of liquidity risk is the responsibility of the Treasury department of pbb Group which is independent of Risk Management & Control. The processes and methods which are used are regularly reviewed by the Group Risk Committee and the Group Asset and Liability Committee of HRE. Liquidity Risk cannot be calculated and reported by business segments.

Liquidity Risk Report

The liquidity management reports are prepared daily and reported to the entire Management Board as well as to the Deutsche Bundesbank and to the Bundesanstalt für Finanzdienstleistungsaufsicht. The reports contain the daily liquidity situation as well as projections on the basis of contractual cash flows and assumptions made in relation to future events which will influence the probable liquidity development.

Measuring and Limiting Liquidity Risk

A system for measuring and limiting short-term and medium-term variances within the cash flows has been installed in order to manage liquidity risks. Contractual cash flows as well as optional cash flows are recognised. These data are regularly subject to back testing.

The liquidity position resulting from the contractual and optional cash flows is measured in different scenarios. In this context different liquidity positions are calculated on a daily basis. The three liquidity positions assume:

> Constant market and refinancing conditions (base scenario)
> Risk scenario (modified (historic) stress scenario)
> Liquidity stress ((historic) stress scenario)

In the risk and (historic) stress scenario, possible customer behaviour is for instance simulated in «stress situations». Historical time series are used to calculate 95% and 99% quantiles.

For the liquidity risk for the various liquidity scenarios a limit for a period of 12 months respectively a trigger of 24 months (base scenario) has been defined. At the end of 2013 the Limits were adjusted and defined for six months.

The limit system consists of:

> Limit relating to the liquidity stress profile for pbb Group (risk scenario and (historic) stress scenario) and trigger for the base scenario

In addition to reporting, pbb Group uses stress tests for investigating the effect of additional stress events on the liquidity position; these stress tests are conducted at regular intervals.

Scenario analyses are performed to simulate the potential impact of crises attributable to macroeconomic, monetary policy and political causes on the liquidity situation.

The scenarios are reported to the Management Board of Deutsche Pfandbriefbank AG as well as to external bodies, e.g. Deutsche Bundesbank.

Liquidity Risk Monitoring and Management

Monitoring of the liquidity risks is assured by the daily reporting of the liquidity situation and a defined escalation process. A liquidity emergency plan has also been adopted in this context; this plan forms the specialist and organisational framework for the treatment of liquidity shortages.

Liquidity risk management is based on various interconnected components which are based on a «liquidity risk tolerance» defined by the Management Board. This ensures that pbb Group has adequate liquidity reserves.

Hedging and Reduction of Liquidity Risk

A risk tolerance system is used to limit the liquidity risk. Risk tolerance is integrated in the liquidity management process by means of triggers (limit system) in order to ensure a «survival period» for pbb Group in stress conditions.

The limits applicable for risk tolerance are determined in line with stress scenarios and are adjusted at regular intervals.

Development of pbb Group's Risk Position

The development of the liquidity position in 2013 exceeded expectations in the light of increasing normalisation on the capital markets.

The cumulative liquidity position (liquid assets as well as expected net cash flows) calculated as part of the liquidity risk measurement as of 31 December 2013 amounted to €8.0 billion for a 12-month horizon in the base scenario. There was an increase by €2.5 billion in comparison with the previous year. Because of a higher middle- and long-term unsecured funding and the first contribution of new funding source (deposit business) this increase was more than the expected change of liquidity. The increase in the liquidity position was also due to lower overcollateralisation requirements for mortgage cover pool assets.

The liquidity ratio in accordance with the Liquidity Ordinance amounted to 3.03 at Deutsche Pfandbriefbank AG as of 31 December 2013; it was thus higher than the statutory minimum of 1.0.

Funding

In 2013, capital markets were dominated by the low interest rate environment, expansionary monetary policy and uncertainty as to the central banks' future course of action.

The historically low interest rate environment led to stronger demand for unsecured bonds and securities from the periphery of Europe. Deutsche Pfandbriefbank successfully placed the first of two senior unsecured benchmark transactions on the market in January.

Worries about whether the sovereign debt crisis had been overcome resurfaced after Cyprus was bailed out, increasing market volatility. Pfandbriefe remained attractive for investors and the risk premiums for securities placed on the primary market improved again. For the first time since the crisis, pbb was once again able to issue a long-term public sector Pfandbrief with a term of 15 years.

The rise in long-term interest rates due to speculation about monetary policy tapering led to market uncertainty in the third quarter. However, the debate on the budget deficit and the associated temporary shutdown of selected parts of the administration in the USA forced the Federal Reserve to continue its expansionary monetary policy. In the eurozone, the mixed performance by countries and emerging deflationary tendencies in fact caused the ECB to expand the liquidity supply even further by lowering interest rates in November 2013. This liquidity situation made it easier for credit institutions to obtain funding and led to a significant decline in risk premiums for Pfandbriefe and unsecured bonds.

pbb Group can take advantage of both secured and unsecured issues for funding purposes. Pfandbriefe are the main funding instrument used. These are less affected by market volatility than many other sources of funding due to their high quality and acceptance on the international capital markets.

With a total of 14 new and tap issues, Deutsche Pfandbriefbank was one of the most active issuers using the benchmark format. In addition to the issuance of a public sector Pfandbrief and three mortgage Pfandbriefe, pbb placed two unsecured issues and Pfandbriefe denominated in sterling on the market. The long-term issue volume amounted to €7.7 billion, of which approximately €4.5 billion was funded by Pfandbriefe and €3.2 billion by unsecured securities. In addition, a large part of the funding was achieved through private placements. Alongside public transactions, these represent an important funding vehicle for the Bank and contribute to the granularity of funding thanks to their small-scale character.

Forecast Liquidity Requirement

Due to the balanced asset and liability structure there are no significant liquidity mismatches.

In addition to the forecast liquidity requirement for new business activities, the extent of the future liquidity requirement further depends on numerous external factors:
> Further development of the European financial crisis and possible effects on the real economy
> The future development of haircuts for securities for repo refinancing on the market and with the central banks
> Possible additional collateral demands as a result of changing market parameters (such as interest rates and foreign currency rates)
> The development in collateral demands for hedges
> Changed requirements of the rating agencies regarding the necessary overcollateralisation in the cover pools

Funding Risk

With regard to the funding risk, please refer to the presentation of the business risk in the section «Result of Risk-bearing Capacity Analysis».

Market Liquidity Risk

With regard to financial instruments which are measured at fair value, quantitative details for a better assessment of the market liquidity risk can be obtained from the presentation of the three levels of the fair value hierarchy in the notes. Generally there is no intention to sell LaR holdings for liquidity management purposes, as liquidity for these holdings can mainly be generated by way of including them in the cover pool, refinancing opportunities of the central bank or repo transactions.

Risks

The adjustments of the ECB's interest rate policy in the light of the European financial crisis and the resulting decline in overall interest rates entail the risk that investors underweight the bond market when allocating funds. This could lead to a general increase in funding spreads.

Opportunities

The cumulative liquidity position of €8.0 billion in the base scenario over a horizon of 12 months which is detailed in the section «Development of the Risk Position of the pbb Group» as of 31 December 2013 opens up the opportunity of being able to provide a flexible response particularly with regard to possible new business.

If there was an overall positive development for pbb Group in the external factors specified in the section «Forecast Liquidity Requirement», this would per se result in a lower future liquidity requirement.

Operational Risk

Definition

pbb Group defines operational risk as «the risk of loss resulting from inadequate or failed internal processes, people and systems or from external events». The definition includes legal risks, but excludes strategic and reputational risks, which are examined separately.

Strategy for Operational Risks

The overriding aims of pbb Group are the early recognition, recording, assessment as well as monitoring, prevention and limiting of operational risks as well as early and meaningful management reporting. pbb Group does not attempt to completely preclude the possibility of risk; instead, it aims to minimise potential losses. The approach is to ensure that there is sufficient information to make informed decisions about risk mitigation.

Organisation of Operational Risk Management

Within Risk Management & Control, the operational risk division is responsible for the coordination of consistent policy, tools and practices throughout the HRE Group for the management, measurement, monitoring and reporting of relevant operational risks. This also comprises pbb Group.

Risk Reports, Monitoring and Management of Operational Risks

Operational risks are monitored by means of a network of controls, procedures, reports and responsibilities. Within pbb Group, each individual business area and management level takes on responsibility for its own operational risks, and provides appropriate resources and processes for limiting such risks. The focus of the operational risk department is the proactive identification, management and mitigation of risks rather than on just risk monitoring, measurement and reaction to risk.

Consolidated information is used in order to determine the operational risk profile of pbb Group and any required measures in relation to mitigation of identified risks. Operational risk scenario analyses, which are conducted annually, are also used in this context.

Regular reports are prepared for the Chief Risk Officer (CRO) and the Group Risk Committee. The monthly Group risk report includes details concerning operational risk events and losses and key risk issues affecting pbb Group. In addition, a quarterly risk report regarding key risk indicators notifies the Management Board of potential risk sources. On an annual basis an annual operational risk report is produced which includes a summary of important events during the year and also the results of the operational risk self-assessment process. This report is circulated to the board of pbb and presented to the Group Risk Committee.

Risk Measurement

The economic capital for operational risk in the going-concern perspective amounted to €37 million as of 31 December 2013 (31 December 2012: €14 million). Details of the calculation are set out in the chapter «Result of Risk-bearing Capacity Analysis».

In line with the standard approach in accordance with Basel II, the regulatory capital backing for operational risks, which is calculated at the end of each year, was €74 million as of 31 December 2012 (31 December 2012: €82 million).

Operational Risks Profile of pbb

pbb suffered financial losses of €1,2 million in relation to operational risk during 2013 (2012: €3,3 million). The operational loss was distributed to the Real Estate Finance Segment with 94% and to the Public Sector Finance segment with 6%.

The Basel II event type «Execution, Delivery & Process Management» was the category with the highest number both of events (85%) and of related financial losses (94%) in 2013. The value in the «Execution, Delivery & Process Management» event type is normal for the industry given the number of transactions. At pbb, this was attributable both to the increase in new business and to the services provided to FMS Wertmanagement. The services provided to FMS Wertmanagement were discontinued as at 30 September 2013.

This event was also reflected in the operational risk self-assessment process, which is a bottom-up risk assessment performed by all of the Bank's segments.

pbb's operational risk profile has improved continually over the past few years, inter alia thanks to the successful implementation of various IT projects and the consolidation of its core systems.

In addition, the separation of pbb and DEPFA was promoted. To date, this ongoing change has not given rise to any additional issues with respect to operational risk.

Opportunities

The annual reports published in recent years note that pbb has an increased reliance on employees in key positions. This was attributed to the special situation at the time during the financial market crisis and the resulting uncertainty surrounding pbb's future. We expect this key person risk to decrease as the privatisation of pbb is getting closer.

Result of Risk-bearing Capacity Analysis

Going concern

Going concern in € million	**31.12.2013**	**31.12.2012**	△ in € million
Credit risk	237	226	11
Market risk	185	171	14
Operational risk	37	14	23
Business risk	–	–	–
Property risk	9	11	–2
Total before diversification effects	**468**	**422**	**46**
Total after diversification effects	**421**	**375**	**46**
Available financial resources (free capital)	1,946	1,660	286
Excess capital (+)/capital shortfall (-)	1,525	1,285	240

The going-concern perspective explicitly focuses on the protection of regulatory minimum capitalisation, and thus focuses on the continuation of business activities of pbb Group in periods of difficult economic downturns. In order to prove the risk-bearing capacity the first step is to calculate the economic capital at a confidence level of 95%. This includes the risk types which we define to be of a material nature, namely credit risk, market risk, operational risk, funding risk as part of the business risk and property risk.

Excluding the diversification effects between the individual risk types, the economic capital of pbb Group in the going-concern perspective amounted to € 468 million (31 December 2012: € 422 million). If these effects are taken into account, it was € 421 million (31 December 2012: € 375 million). The most significant risk type on the basis of the ICAAP (measured in terms of the economic capital) was the credit risk, which accounted for approximately 51% of the undiversified economic capital. The increase in economic capital after diversification effects is due to both a deterioration in the credit quality of countries and methodological enhancements (such as risk measurement for operational risk or the adjustment of the correlation parameters used to aggregate credit and market risk).

This is opposed by the so-called free capital as available financial resources, comprising core Tier 1 capital less the Tier 1 capital necessary for covering the regulatory minimum ratios and a buffer for risks which are minor and are not quantifiable or only partially quantifiable. In accordance with the principle of prudence, an additional charge in relation to the risk-weighted assets is taken into account in order to determine the Tier 1 capital necessary for covering the regulatory minimum ratios. The amount of free capital as of the reference date was € 1.9 billion (31 December 2012: € 1.7 billion).

Accordingly, the resulting excess capital as of 31 December 2013 amounted to € 1.5 billion for the given period of one year (31 December 2012: € 1.3 billion); it is further proof of the risk-bearing capacity of pbb Group in the leading going-concern perspective.

The distribution of the economic capital according to segments is as follows:

Economic capital by segments in € million	31.12.2013	31.12.2012	△ in € million
Real Estate Finance	137	127	10
Public Sector Finance	268	250	18
Value Portfolio	12	3	9
Consolidation & Adjustments	56	29	27
Total	**421**	**375**	**46**

Gone Concern (Instantaneous Liquidation Perspective)

In order to fully comply with the regulatory requirements with regard to banks' internal risk-bearing capacity concepts pbb has developed the existing gone-concern approach (liquidation perspective) and has implemented it as an additional, parallel steering approach. The purpose of the so-called instantaneous liquidation perspective is to guarantee protection of the senior lender in a theoretical liquidation scenario with a very high probability. pbb has selected a confidence level of 99.91% which is based on the average probability of default of companies which have been awarded good long-term credit ratings by external rating agencies, namely A– from Standard & Poor's, A–/A3 from Fitch Ratings and Moody's. However, this liquidation scenario does not assume an opportunistic winding up of portfolios as postulated by the German Pfandbrief Act, and instead assumes an immediate sale at stressed market values of assets recognised at fair value and securities in the investment book. According to this assumption the instantaneous liquidation perspective besides the already mentioned major risks takes account of credit spread risks arising from securities in the investment book for calculating the economic capital, and deducts simultaneously the hidden losses attributable to these securities for determining the available financial resources.

Gone Concern (instantaneous liquidation perspective) in € million	31.12.2013	31.12.2012	△ in € million
Credit risk	1,447	1,446	1
Market risk	1,083	1,143	−60
Operational risk	78	86	−8
Business risk	53	42	11
Property risk	20	20	–
Total before diversification effects	**2,681**	**2,737**	**−56**
Total after diversification effects	**2,436**	**2,383**	**53**
Available financial resources before hidden losses	4,285	3,953	332
Hidden losses	546	1,394	−848
Available financial resources	**3,739**	**2,559**	**1,180**
Excess capital (+) /capital shortfall (-)	1,303	176	1,127

In the instantaneous liquidation perspective, the economic capital without diversification effects amounted to € 2.7 billion as of 31 December 2013 (31 December 2012: € 2.7 billion); if these effects are taken into consideration, it amounted to € 2.4 billion (31 December 2012: € 2.4 billion). The main drivers in this respect are the credit risk (€1.4 billion) and the market risk (€1.1 billion). Most of the market risk is attributable to the sub-portfolio of budget finance in Public Sector Finance – which is non-strategic and earmarked for being streamlined – due to the fact that the volatility of credit spreads is still increased for certain areas of the European Economic Area. This effect can also be seen in the following table of economic capital by segments. The credit risk remained constant year-to-year.

The available financial resources in the instantaneous liquidation perspective initially amounted to € 4.3 billion (31 December 2012: € 4.0 billion); this figure was reduced to € 3.7 billion (31 December 2012: € 2.6 billion) after the net hidden losses attributable to the securities in the investment portfolio were deducted.

The distribution of the economic capital by segments in the instantaneous liquidation perspective is as follows:

Economic capital by segments in € million	**31.12.2013**	**31.12.2012**	△ in € million
Real Estate Finance	515	633	–118
Public Sector Finance	1,869	1,702	167
Value Portfolio	27	10	17
Consolidation & Adjustments	188	134	54
Total	**2,436**	**2,383**	**53**

Strategic Gone Concern (Strategic Liquidation Perspective)

In addition to the instantaneous liquidation perspective described above, pbb Group has also developed a strategic gone-concern perspective. In this perspective, the risk calculation is adjusted by the budget finance portfolio which has been earmarked for streamlining and the Value Portfolio in order to focus on management of the strategic core business of real estate finance and public investment finance. All risk types which have been defined as being significant, including the credit spread risk for securities in the investment book, are taken into consideration, aggregated to form an economic capital and are then limited. In the strategic gone-concern perspective, the economic capital amounted to € 1.2 billion (31 December 2012: € 1.2 billion) and the hidden losses of the strategic portfolio amounted to around € 0.4 billion (31 December 2012: € 0.7 billion).

Opportunities

The results of the risk-bearing capacity analysis in the instantaneous liquidation view are still very much affected by the relatively high volume of hidden losses of the securities in the investment book which has to be considered as a deduction from the available financial resources. This is due to a considerable extent to the credit spread of some Southern European countries, regions and municipalities which still had been widened as of the reference date as a result of the European sovereign debt crisis. The volatility of credit spreads of some European countries is also still higher compared with the period before the crisis, and puts a strain on the result of the risk-bearing capacity statement as a result of a correspondingly higher market risk. The downgrades observed in 2013 have resulted in an increased credit risk.

Although it is still clearly too soon to speak of a turnaround in the European sovereign debt crisis in 2014, we have observed a stabilisation of the European bond markets as a result of the crisis management of ECB. Overall, the ICAAP-relevant hidden losses of pbb for securities in the investment book have declined by approximately €848 million since the beginning of 2013. A continuation would result in a further expansion of the excess capital in the ICAAP liquidation approach of pbb Group in 2014.

If there is a comprehensive recovery of trust in the European public finances, systematic rating improvements of public sector issuers could lead to a significant reduction of risk and therefore as well to a further increase of the excess capital in the ICAAP.

Method Used for the Individual Risk Types

The economic capital for each risk type is determined using a quantitative approach and is aggregated to form an overall bank risk with due consideration being given to specific correlations. In line with the common market standard, the risk types are calculated for a period of one year and in relation to a defined confidence level (99.91% in the gone concern, 95% in the going concern). For the gone-concern confidence level, the Bank uses the average figure for long-term default rates of companies with very good external ratings (A– at Standard & Poor's and Fitch Ratings, A3 at Moody's).

The method of calculating the economic capital for the individual material risk types for 2013 is explained in the following.

Credit Risk For calculating the credit risk at the portfolio level, pbb Group uses a credit portfolio model which follows the approach of a so-called asset value model. The fundamental idea of this approach is that the repeated simulation of correlated rating migrations, borrower defaults as well as a calculation of resultant value changes via a corresponding revaluation of the portfolio mean that probability statements can be made with regard to potential losses from lending business. The loss distribution calculated in this way can then be used to calculate the economic credit risk capital as an unexpected loss. This defines the maximum unexpected loss calculated for a defined confidence level which will result within one year due to rating migrations and defaults in lending business. In addition to the loss distribution of the credit portfolio, a significant result is the risk-commensurate allocation of the credit risk capital to the individual borrower units using the so-called expected shortfall principle. This ensures fair causation-based allocation to the borrowers, and thus constitutes a major module in the risk-oriented management of the credit portfolio.

In addition adjustments of the parameterisation of the correlation within the credit portfolio model had been implemented in 2013. Target of these adjustments was the optimal alignment of the credit portfolio model to the business model of pbb Group with simultaneous consideration of the conservative regulatory requirements on the modelling of diversification effects.

Market Risk The purpose of calculating the economic capital for the market risk is to identify potential financial losses resulting from changes in the prices of items in the investment book and trading book. In this process, the potential non-systematic losses are derived from an analysis of historical time series of specific factors of influence (risk factors), e.g. interest rates, exchange rates and credit spreads over the previous seven years. The relatively long period of seven years ensures that economic phases which are not favourable for the Bank are also taken into account in the model. The annual loss distribution of the portfolio market value is then determined by means of a simulation procedure and using the linear sensitivities of the financial instruments; this can then be used to determine the economic capital in relation to a confidence level of 95% and 99.91%.

Operational Risk The calculation of economic capital for operational risk takes into account both the results of the calculation in accordance with the Standard Approach under Basel II and the results generated by a mathematical model used to calculate losses from operational risks, which uses internal data as inputs. This past-related approach is enhanced by the recognition of forward-looking budget figures for three years. For the purposes of the capital adequacy procedure, the regulatory capital requirement is scaled to the corresponding lower confidence level (from 99.9% to 95%). In the gone-concern approach it is scaled to the higher confidence level of 99.91%.

Business Risk In pbb Group, the business risk is generally defined as the risk of reductions in profit due to changes in the external business environment which affect the economic conditions of the Bank. Alongside non-quantifiable risks such as regulatory risk, reputational risk and strategic risk, these include risks arising from increased funding costs and higher funding requirements, as well as earnings risk. Economic capital for business risk is calculated using a scenario-based increase in financing costs due to higher funding requirements and a simultaneous increase in the unsecured funding rate. Earnings risk is taken into account by not including planned income from new business in the risk cover amount.

Property Risk pbb Group's real estate risk is calculated using a mathematical-statistical model that enables the Bank to make statements on the probability of potential declines in the value of properties in its portfolio. The inputs for the model are mainly based on time series of representative real estate indices for the portfolio.

Liquidity Risk Capitalising for liquidity risk in the narrower sense is not possible. Liquidity risks in the broader sense of higher funding costs for potential funding gaps are recognised in the economic capital for the business risk.

Stress Tests

Stress tests have become increasingly important in the recent past, both from a supervisory perspective and for internal bank management, not least as a result of the European sovereign debt crisis. All activities, developments and decisions relating to stress tests are bundled within the Stress Test Committee, which reports directly to the Risk Committee. As part of an integrated approach, the impact of macroeconomic stress scenarios on all material risks and on risk-taking potential under stressed market parameters was calculated for a multi-year time horizon in the period under review. These scenarios focus on the continuation and/or intensification of the current sovereign debt crisis.

Furthermore, stress tests relating to economic risk capital and risk cover funds are used to obtain a deeper understanding of the sensitivity of risk-bearing capacity to adverse changes in economic factors. In addition, inverse stress tests are conducted regularly. These describe specific constellations of parameters under which capital adequacy is still assured. Alongside institutionalised stress tests, ad hoc requests by the Management Board for information played an important role in the period under review.

Regulatory Indicators According to German Solvency Regulation

In accordance with the waiver rule set out in Section 2 a of the Kreditwesengesetz (KWG - German Banking Act), pbb is exempted from having to calculate equity and Tier 1 capital ratios at the level of the institution.

The waiver regulation set out in Section 2 a KWG states that a credit institution or financial services institution which has its registered offices within Germany and which is part of a regulated group of institutions or financial holding group does not have to comply with the following regulations if these regulations are complied with at the level of the ultimate parent company:

> Regulations regarding solvency (equity in relation to risk-weighted assets)
> Regulations regarding large loans (equity in relation to loans extended to individual borrower units)
> Regulations set out in Section 25 a (1) Clause 3 No. 1 KWG for establishing and assuring risk-bearing capacity, defining strategies, setting up processes for identifying, assessing, managing, monitoring and communicating risks.

The pbb Group voluntarily discloses these figures on a pro forma basis.

pbb Group's regulatory capital in accordance with the Solvabilitätsverordnung (SolvV – German Solvency Regulation) is as follows:

Own funds[1] in € million	**31.12.2013**	**31.12.2012**
Core capital (Tier I)	2,825	2,898
Supplementary capital (Tier II)	835	1,179
Equity capital	**3,660**	4,077
Tier III capital	–	–
Total	**3,660**	**4,077**

[1] Consolidated in accordance with section 10 a of the KWG; pro forma in accordance with the prepared annual financial statements and following the appropriation of net profit

The risk-weighted assets, the operational risks and the market risk positions are as follows:

Risk-weighted assets[1] in € billion	**31.12.2013**	**31.12.2012**
Risk-weighted assets	14.1	15.3

[1] Including weighted credit risk positions and capital charges for market risk positions and operational risk, using a scaling factor of 12.5; according to Basel II advanced IRB approach for authorised portfolios, otherwise Basel II standardised approach; pro forma in accordance with the prepared annual financial statements and following the appropriation of net profit

Operational risks in € million	**31.12.2013**	**31.12.2012**
Total	74	86

Market risk positions in € million	**31.12.2013**	**31.12.2012**
Currency risks	6	6
Interest rate risks	–	–
Total	**6**	**6**

The capital ratios were calculated on the basis of the definition of equity given in the SolvV and using risk-weighted assets in accordance with Basel II and are as follows:

Key capital ratios[1] in %	**31.12.2013**	**31.12.2012**
Tier 1 capital ratio[2]	20.1	18.9
Equity capital ratio[3]	26.1	26.7
Own funds ratio (overall indicator)[2]	26.0	26.6

[1] Pro forma in accordance with the prepared annual financial statements and following the appropriation of net profit
[2] Including weighted credit risk positions and capital charges for market risk positions and operational risk, using a scaling factor of 12.5
[3] Including weighted credit risk positions and capital charges for operational risk, using a scaling factor of 12.5

Internal Control System and Risk Management System Relevant for the Consolidated Financial Reporting Process

Concept

The internal control system and risk management system relevant for the consolidated financial reporting process comprise the principles, processes and measures used to ensure the effectiveness and cost-effectiveness of financial reporting, as well as to ensure compliance with statutory provisions. The goal of the internal control system and risk management system relevant for the consolidated financial reporting process is to identify and assess risks that could run counter to the objective of ensuring that the financial statements comply with the relevant rules, as well as to limit identified risks and to assess their effect on the financial statements and the corresponding presentation of these risks. The internal control system relevant for the consolidated financial reporting process is an integral part of the risk management system. It aims to implement controls so as to provide sufficient assurance that, despite the risks identified, the financial statements are prepared in accordance with the relevant rules. However, an internal control and risk management system relevant for the consolidated financial reporting process cannot provide an absolute guarantee that these goals will be met.

pbb Group's internal control system and risk management system relevant for the consolidated financial reporting process is reflected in its organisational structure and workflows. With respect to the organisational structure, it primarily comprises the Management Board, the Supervisory Board as the body that supervises the Management Board, the Audit Committee established by the Supervisory Board, the Finance division, which reports to the CFO/COO, and the Group Finance Committee (GFC).

As the Company's legal representative, pbb's Management Board is required to prepare consolidated financial statements and a Group management report. In connection with the requirement to establish a Group-wide internal control and risk management system, the full Management Board of pbb is also responsible for the form – i.e. the concept, implementation, maintenance and monitoring – of an appropriate and effective internal control and risk management system relevant for the consolidated financial reporting process. All strategies are resolved by the full Management Board on the basis of recommendations made by the CFO/COO or the GFC.

The Supervisory Board is tasked with advising and monitoring the Management Board. It also has audit and reporting-related obligations. pbb's Supervisory Board established an Audit Committee to support its activities in this area. In accordance with section 100 (5) of the Aktiengesetz (AktG – German Stock Corporation Act), at least one member of the Supervisory Board must have expertise in accounting or auditing.

Group Internal Audit supports the Management Board in its control function by performing independent audits.

In financial year 2013, the CFO/COO was responsible for Finance, Human Resources and Operations, among other functions. The Finance division comprises the Accounting, Financial Reporting, Regulatory Reporting, Procurement Services & Corporate Controlling and Tax departments. The Finance division prepares the consolidated financial statements in accordance with IFRSs and provides the capital market information relevant to accounting. pbb Group companies prepare their financial statements in accordance with the relevant local legal requirements. These financial statements are standardised around uniform Group accounting policies in accordance with IFRSs for the purposes of Group financial reporting. Each entity included in the consolidated financial statements reports its statement of financial position, income statement, and notes to the financial statements to a central department in Group Accounting via the consolidation software. Group Accounting translates the data in foreign currency positions into euros using the accounting software. The data are also reviewed for reasonableness, analysed and consolidated.

The GFC at HRE level issues recommendations to the Management Board. These include, among other things, establishing and monitoring accounting and reporting policies and workflows for all HRE units and segments, including all pbb Group units. The GFC is composed of the members of the Management Board and the managers of the Finance and Risk Management & Control divisions.

With respect to workflows, the internal control system and risk management system relevant for the consolidated financial reporting process is based on the objective of largely standardising the processes and software used. Core activities and processes are governed by policies and a code of conduct, according to which the principle of dual control must be applied in all material transactions. Data and IT systems are protected against unauthorised access. In addition, certain relevant information is only made available to those employees who need it for their work. Where necessary, results are agreed at Group level.

Implementation

pbb Group implemented the concept for the internal control system and risk management system relevant for the consolidated financial reporting process using various measures designed to identify, assess and limit risks. The governing bodies of HRE Holding and pbb largely comprise the same people, enabling uniform management of these companies. For example, the members of pbb's Management Board also serve as the Management Board of HRE Holding.

There is a clear separation of functions within the CFO's area of responsibility; for example, there are separate Accounting and Financial Reporting departments. The GFC and other committees, as well as divisional meetings serve as overarching links between the different tasks. In addition, executory, accounting and administrative activities such as payment transfers and payment entries are clearly separated or subject to the dual control principle. Furthermore, the units included in the consolidated financial statements report their data to a central Group department, ensuring that downstream processing uses a single, uniform method.

Systems-based and non-systems-based risk management measures and internal controls are used within the workflows. At the systems level, standard software is used as far as possible to post, reconcile, check and report data so as to avoid errors. The same applies to consolidation, which is performed using standard market software. The consolidation software uses a clearly defined process to support the reconciliation of intragroup transactions at a technical level, ensuring that these transactions are eliminated correctly and in full. Data from the entities included in the consolidated financial statements are reported using a uniform, standardised chart of accounts. Automated plausibility checks are performed on the data reported by subsidiaries for consolidation purposes, for example. The balances carried forward are checked by the system. To prevent data loss, the data in the consolidation software are backed up on a daily basis and the backup is stored on tape. As a general rule, pbb Group's software is protected against unauthorised access by a clearly defined administration concept and rights authorisation rules.

Alongside the systems-based measures, pbb Group has implemented manual and non-systems-based processes. For example, the correctness and completeness of the data reported are checked using a standardised process involving variance analyses based on target/actual comparisons, among other things. In addition, the consolidated statement of financial position and the consolidated income statement are calculated on a monthly basis. Projections and forecasts are also drawn up. Analysing figures on an ongoing, regular basis provides a better understanding of them. Mandatory Group-wide accounting guidelines are defined and communicated in a manual, among other ways. These guidelines cover the analysis and interpretation of new and existing IFRS standards and interpretations so as to ensure the application of uniform accounting policies across the Group.

Generally applicable measurement procedures are used. The procedures used and the underlying inputs are reviewed at regular intervals and modified as necessary.

In order to improve the quality of controls, various divisions are integrated in certain processes and are required to coordinate their activities. For example, the enterprise-wide new product process and the review of existing products (with a right of veto by the Finance division) are designed to ensure that products are recognised in the financial reporting in a uniform and systematic manner. Annual and interim financial report preparation is another example of enterprise-wide coordination. All of the areas involved must sign off on these reports before they are officially prepared by the Management Board (subcertification process), creating an additional level of control for the products to be disclosed. All of the divisions affected agree in advance on the content of material sections of the annual report in editorial meetings.

As part of the risk management system relevant for the consolidated financial reporting process, pbb Group takes measures to combat fraud and intentional violations that negatively impact the Group. Fraud against pbb Group includes theft, embezzlement, or breach of fiduciary duty, as well as intentional accounting errors in connection with the consolidated financial reporting process. pbb Group identifies and evaluates risks and takes measures to prevent such fraudulent activities and intentional violations. In addition, a newly developed systems-based concept is used to train employees in compliance regulations.

Maintenance

pbb Group reviews and improves its internal control system and risk management system relevant for the consolidated financial reporting process on an ongoing basis, including within the scope of Management Board and GFC meetings, to ensure that risks are identified, assessed and limited as accurately and as comprehensively as possible. Consequently, the internal control and risk management system relevant for the consolidated financial reporting process is also adapted to new circumstances such as changes to pbb Group's structure or business model, or new statutory requirements.

The risk of fraud and intentional violations is regularly analysed in order to take defensive measures. Factors taken into account include suspicious events and changes in pbb Group's situation and that of individual employees.

Any changes to processes and IT systems required as a result of legislative amendments are implemented as separate enterprise-wide projects with a clear allocation of functions. At the same time, the risk management system relevant for the consolidated financial reporting process is also adapted to the changes in the provisions.

pbb Group's IT landscape is continually enhanced. For example, the Group is reviewing its Group-wide general ledger structure. These and other measures will reduce the complexity of the consolidated financial reporting process.

Monitoring

Group Internal Audit is responsible for checking that transactions are conducted in a due and proper manner and identifying inefficiencies, irregularities or manipulation. It also reviews the effectiveness and appropriateness of risk management and the internal control system in a risk-oriented manner in line with the rules set out in the Mindestanforderungen an das Risikomanagement (MaRisk – Minimum Requirements for Risk Management), and identifies any weaknesses in risk identification, assessment and mitigation. This also includes reviewing the IT systems and the processes and controls in the CFO functions. Concrete action plans with specific deadlines are drawn up and their implementation monitored to remedy the identified shortcomings. Group Internal Audit is not integrated into the workflow, nor is it responsible for the results of the process to be audited. In order to be able to carry out its duties, Group Internal Audit has a full and unrestricted right to information on activities, processes and the IT systems.

As the body responsible for supervising and advising the Management Board, the Supervisory Board may inspect and examine the Company's books and assets in accordance with section 111 (2) of the AktG. In addition, the Management Board reports regularly to the Supervisory Board. The Supervisory Board also directly consults division managers. The Supervisory Board discusses the internal control and risk management system relevant for the consolidated financial reporting process and engages the auditors of the consolidated financial statements and the Group management report. The Supervisory Board approves the consolidated financial statements and the Group management report prepared by the Management Board and audited by the independent auditors.

The auditors of the financial statements attend the Supervisory Board meetings relating to the financial statements and all of the meetings of pbb Group's Audit Committee, and report on the material findings of their audit, including on any material weaknesses in the internal control and risk management system relevant for the consolidated financial reporting process. Where relevant, the auditors immediately report on any findings and issues that emerge during the audit and that are material for the duties of the Supervisory Board. The Supervisory Board discusses the areas of emphasis of the audit with the auditor in advance.

Report on Expected Developments

Macroeconomic Forecast

Global economic growth is likely to rise from 2.2% in 2013 to 3.0% in 2014. The 2014 forecasts for Europe are based on the assumption that uncertainty as to the future management of the eurozone crisis has declined significantly. Following the slight drop in economic output in 2013, growth of 1.1% is expected for 2014. However, the current upswing is not self-sustaining, as the public finances of many industrialised countries are still heavily in deficit. Growth is expected to reach 1.6% in Germany and should even be slightly higher in the United Kingdom, at 1.9%. France's gross domestic product is expected to grow by 1.1%, while Spain and Portugal are expected to see at least slight growth. The Nordic countries should grow stronger in 2014 compared to 2013, Central and Eastern Europe shall develop positively as well.

Since the trend in demand remains weak, inflation during the forecast period is likely to be even slower than last year in most regions. However, inflation risk could increase over the medium term, the longer the European Central Bank continues to supply economies with money at close-to-zero rates. A modest rise in long-term interest rates is therefore likely, while short-term rates will remain largely unchanged.

Source: Sachverständigenrat zur gesamtwirtschaftlichen Entwicklung

Sector-specific Environment

Overall Situation in the Banking Sector

The environment for banks will remain difficult in 2014, and policy makers and central banks will continue to have a major influence on the sector.

Earnings will continue to be weighed down by the low level of interest rates. Numerous new regulatory measures will impact business models and balance sheet structures, chief among them being the capital and liquidity requirements set out in the Basel III reform package and the introduction of a binding leverage ratio. These requirements will be implemented in the European Union through the new Capital Requirements Directive (CRD) and enter into force successively from 2014 onwards.

The planned handover of responsibility for the supervision of systemically relevant eurozone banks to the European Central Bank in autumn 2014 will involve substantial effect for the banks concerned due to the comprehensive upfront assessment of the bank's balance sheets that is required (risk assessment, balance sheet assessment and stress test).

Given the banks' key role in the financial crisis, the extensive new regulatory measures and the ongoing investigations and prosecutions relating to wide variety of issues, the general public is likely to continue to view banking sector developments with a critical eye in 2014. Generally, costs of regulation will burden profitability.

Real Estate Finance

European real estate markets are expected to see a continuation of the positive prior-year trend in 2014, with real estate investment volumes set to increase further. This would restore them to pre-financial and economic crisis levels.

Within Europe, investors are likely to be interested primarily in properties in Germany, France, the United Kingdom, Scandinavia and Eastern Europe. Spain may also see further growth.

Overall, investor focus is expected to continue to shift from prime properties in central locations to properties in more outlying areas. The office and retail property segments should continue to dominate the marketplace although demand for logistics properties is also expected to trend upwards.

Real estate finance providers should also benefit from the increasing transaction volume, while financing terms are expected to remain attractive. One anticipated result is that large-volume finance transactions and financing entailing some speculative elements will pick up. In addition, alternative lenders such as insurance companies, pension funds, or credit funds are expected to offer increasing amounts of finance.

Source: CBRE research

Public Sector Finance

Banks providing public investment finance will continue to apply stringent transparency requirements to public sector borrowers in the foreseeable future. In particular, lenders will probably again begin to very selectively assess countries that have been under the spotlight, such as Spain and Italy, for new business opportunities under certain conditions. In addition to clear disclosure of their financial situation and an analysis of the precise purpose of the requested investment finance, the borrowers' economic situation and outlook will be crucial factors in financing decisions.

This market environment will continue to see significant shifts in the competition. As a result, previously cautious banks will again start to increase their financing activity in some countries and, in specific cases, financing will be offered by other market participants, such as insurance companies and credit funds.

The situation on the German and French markets is likely to remain largely unchanged compared with 2013. The German market continues to be dominated by public sector banks and development banks, with margins at a low level. In France, fierce competition has led to shrinking margins. This trend is set to continue for the next year at least. However, France will again offer good opportunities for transactions with attractive risk-return profiles.

In the area of export financing, there also will be sufficient opportunities for new business in the future, partly due to the changed strategic orientation of previously very active banks.

Funding Markets

Future central bank monetary policy will have a major influence on the capital market. The historically low interest rate environment is expected to sustain the high investor demand for unsecured bonds. However, the ECB's comprehensive assessment could lead to market volatility.

It remains to be seen what effect the regulatory changes will have on the funding markets. The expected classification of Pfandbriefe as liquid or even as high quality, highly liquid securities for the purposes of the liquidity coverage ratio should lead to stable, or potentially rising, demand. A low volume of new issues and a continued high money supply would certainly positively impact the funding opportunities for Pfandbrief banks. However, the regulatory and legal changes could make it difficult for some issuers to place unsecured bonds.

Company Forecasts

The forecasts for pbb Group's future development represent estimates that were made on the basis of the information currently available. If the assumptions on which the forecasts are based do not materialise or if risks and opportunities do not occur to the extent calculated, the actual results may differ significantly from the results currently expected.

Future Developments in Assets, Financial Position and Earnings

pbb Group recorded pre-tax profit of € 165 million at the end of 2013. This was significantly higher than the earnings forecast of at least € 100 million made at the start of the year. The raised forecast for the year of at least € 150 million, which was issued on 8 October, was also met. Additionally, pbb Group has proven its continuing profitability, reporting positive results for the past three-and-a-half years.

pbb Group is also expecting to record a positive pre-tax profit in the 2014 forecast period: specifically, the Management Board is forecasting a figure of at least € 140 million for 2014. One-off factors are unlikely to have the same impact as in 2013, when the result was boosted in particular by the gain from the disposal of the shares in Little Britain Holdings (Jersey) Ltd., Jersey. The return on equity after taxes will be at least 3.7 % (2013: 4.9 %).

The key income statement items are expected to perform in 2014 as follows:

> A further increase in net interest income as against 2013 is planned. This positive trend depends on pbb Group reaching the targets for new business. In the areas of real estate finance (Real Estate Finance segment) and public investment finance (part of the Public Sector Finance segment), a significant increase is expected in the volume of new business as against 2013 (€ 8.2 billion). This includes prolongations with maturities of more than one year that will be implemented if this results in economic benefits to pbb Group. As new business will probably exceed redemptions, the real estate loans portfolio is likely to increase slightly. In the Public Sector Finance segment, the volume of public investment loans is expected to increase, but will be more than offset by the decline in budget financing in line with the Group's strategy.

> Net trading income will probably no longer be impacted by accounting-related changes to estimates such as the first-time use of overnight interest rate curves to measure derivatives, and hence will not be as clearly negative as in 2013.

> Net income from financial investments, which was boosted in 2013 by the gain from the disposal of the shares in Little Britain Holdings (Jersey) Ltd., Jersey, will no longer benefit from one-off factors.

> Additions to provisions for losses on loans and advances are expected to be higher, at normalised levels for the lending business, in 2014, after additions and reversals largely offset each other in 2013.

> General administrative expenses will decrease as a result of the discontinuation of services provided to FMS Wertmanagement. However, this improvement will not completely offset the loss of income due to fixed costs and dissynergies. General administrative expenses will also be impacted in 2014 by additional costs for projects, e.g. to implement regulatory and accounting-specific requirements. Starting in the fourth quarter, IT expenses will probably decrease, due to a contract adjustment.

The cost-income ratio – a financial key performance indicator for efficiency – will improve slightly year-on-year (2013: 64.7%). The lower operating revenues will be more than offset by decreased general administrative expenses.

Profits will be retained until privatisation under the burden sharing required by the European Commission in order to redeem the silent participation made by the Financial Market Stabilisation Fund (Finanzmarktstabilisierungsfonds-FMS).

As in 2013, consolidated profit will be higher in the Real Estate Finance segment. Slightly positive pre-tax profit is expected in the Public Investment Finance and Value Portfolio (including budget financing) segments that will be reported as from 2014.

An important additional condition for pbb Group to meet its earnings and profitability targets is ensuring its risk-bearing capacity. With respect to the going concern principle, it is probable that the risk-bearing capacity available after compliance with regulatory minimum capital ratios will exceed the required economic risk capital. From a gone concern perspective, pbb Group believes that the capital available to cover risks will exceed the required economic risk capital as long as spreads in the European focus countries do not widen significantly and hence increase hidden liabilities.

The core capital ratios will probably decrease slightly in 2014 due to higher risk assets expected in the portfolio and in our new business, as well as to the implementation of the CRR/CRD IV (Basel III). However, it is expected to be both significantly above the regulatory limits and considerably higher than pbb Group's target CET1 capital ratio (the core capital ratio under Basel III) of 11%. This will be somewhat lower than the core capital ratio as a result of the more restrictive CET definition. During the implementation of Basel III, IFRSs will replace HGB as the relevant accounting standards for regulatory purposes. Core capital will increase particularly as a result of the change in the eligibility of the silent participation. However, this effect will be reduced by restrictions on the eligibility of certain capital instruments. As a result of these effects, the capital ratios will decline compared with the balance sheet date, but will continue to be at a comfortable level.

Total assets as at 31 December 2013 amounted to €73.9 billion. The increase in assets in Real Estate Finance and Public Investment Finance should largely offset the decline in budget financing in line with the Group's strategy in 2014. Consequently, the volume of liabilities is also expected to remain largely constant.

Opportunities pbb Group has reported positive pre-tax profits for the last 14 quarters. This illustrates the positive trend at pbb Group, which offers the following opportunities on development in assets, financial position and earnings for the future:

> The successful restructuring measures implemented in recent years have strengthened ppb Group's market position, as can be seen from the year-on-year rise in new business volumes recorded in 2013. This successful reorientation has made it possible for pbb Group to continue its healthy development and increase the profitability of its core business areas of real estate finance and public investment finance, with the aim of achieving growth.

> The discontinuation of the operating services provided to FMS Wertmanagement in September 2013 has created another opportunity to further increase the focus on the relevant customer markets in the areas of real estate finance and public investment finance. This should have a positive impact on new business volumes and new business margins, and hence also on development in assets and earnings.

> There is strong demand for financing on the markets which are relevant for pbb Group. In view of this, pbb Group considers that the market climate for real estate finance and public investment finance will remain attractive over the long term. This should have a positive impact on new business volumes and new business margins, and hence also on development in assets and earnings.

- Even in recent years, which have been dominated by market uncertainty, Pfandbriefe have remained a sound investment with a tried-and-tested market infrastructure; this was also reflected by the strong demand from investors in 2013. pbb Group has extensive experience in the Pfandbrief market and is able to build on its existing customer relationships. As a result, it was able to successfully place several mortgage and public sector Pfandbriefe on the market last year. pbb Group therefore utilises on a capital market instrument that is still in demand – something that has a positive effect on its development in financial position.
- pbb Group also placed unsecured issues in 2013, a clear reflection of investors' confidence. This important means of raising funds has a positive impact on pbb Group's liquidity and development in financial position.
- pbb Group takes out overnight deposits and term deposits with terms of up to ten years via pbb direkt. pbb direkt's deposit volumes have increased continuously in recent months, allowing pbb Group to access a new source of funding, diversify its funding base and react flexibly to market opportunities. This has a positive impact on pbb Group's liquidity and development in financial position.
- Further progress was made on separating pbb Group and DEPFA, which both belong to HRE, in 2013. This separation will increase the chances of successfully privatising pbb Group.
- pbb Group's strong focus on costs represents a further opportunity. The reduced general administrative expenses in financial year 2013 reflect the successes already achieved. pbb Group's target model was implemented effectively. The status of the various processes will continue to be assessed on an ongoing basis in future to ensure appropriate measures for improvement are identified. pbb Group will use these measures to significantly reduce its cost base and become leaner and more efficient, so as to increase its profitability.
- pbb Group has also made significant progress on harmonising its IT systems, which has generated additional efficiency gains.
- The process optimisation and the creation of specialist teams allow customer needs to be met more rapidly and customer satisfaction increased. This has a positive impact on new business volumes and new business margins, and hence also on devepolment in assets and earnings.
- pbb Group is an attractive employer. This encourages the loyalty of productive and highly qualified employees and executives who can help pbb Group achieve its ambitious targets.

Risks However, the possibility of future negative effects on pbb Group's development in assets, financial position and earnings cannot be ruled out. The scope of such potential negative effects will be influenced in particular by whether the following risks materialise or not, and if so, to what extent:

- Several European countries were only able to obtain funding with the support of international aid programmes in financial year 2013. If the debt crisis worsens in certain countries and it becomes necessary for creditors to take a haircut on other countries' bonds, or if public sector debtors become insolvent, pbb Group could also suffer substantial impairment losses on receivables and securities. These impairment losses could further increase if interconnectedness or market turbulence causes a crisis in some countries to spread to debtors that are currently considered to be solvent.
- Write-downs were only required for a small number of individual exposures in 2012 and 2013 thanks, among other things, to pbb Group's effective portfolio management. However, it cannot be ruled out that receivables may have to be significantly written down in future. The need to recognise write-downs primarily depends on the economic situation of the financed properties, although it could also be the result of a general crisis in individual markets, such as the real estate markets of various countries.
- The funding markets improved in the year under review. Nevertheless, the funding markets remain susceptible to disruption. For example, the debt crisis in some European countries could result in a major loss of confidence and sharply reduced sales on the issuing markets or the interbank market. Interest rate movements could also affect market liquidity. If the funding markets were to be disrupted by such events, pbb Group's liquidity situation could be negatively impacted, despite the existence of an appropriate cushion. A further consequence might be a conscious reduction in the volume of new business.

> In 2014, the European Central Bank will conduct a comprehensive assessment before the Single Supervisory Mechanism (SSM) starts. The comprehensive assessment is consisting of a risk assessment and a balance sheet assessment; it concludes with a stress test. HRE and therefore pbb Group have been designated to participate in this bank assessment, as one of 128 banks in the eurozone. Depending on the results, the European Central Bank could require HRE to increase the level of own funds held, which could in turn affect pbb Group's capital requirements. In addition, market uncertainty could increase before the results are published, which might make it more difficult to obtain funding. The comprehensive assessment could therefore impact the devepolment in assets, financial position and earnings of pbb Group.

> Enhanced national and international supervisory requirements might affect the structure of assets and liabilities, and hence also the development in earnings. For instance, profitability could be reduced by the new, more stringent, liquidity requirements announced by the Basel Committee on Banking Supervision (Basel III), or by more stringent capital requirements. In addition, existing regulatory and economic parameters could be impacted, resulting for example in a change in the capital backing.

> As part of its approval decision in the state aid proceedings, the European Commission specified that pbb must be privatised as soon as possible and by no later than 31 December 2015. If privatisation has not taken place by 31 December 2015, a divestiture trustee will sell pbb without a minimum price being specified, provided that the Commission has approved the purchaser and the final binding purchase agreement. The sale or alternative shareholder concepts agreed with the European Commission could have a positive or negative impact on the development in assets, financial position and earnings of pbb Group.

> The methods used by the market to value financial instruments are constantly evolving. For example, the market conventions for valuing derivatives have changed, as demonstrated in 2013 by the use of overnight interest rate curves to value derivatives. Similar changes could have a negative impact on pbb Group's development in earnings in 2014.

> Rating agencies continue to adapt their methodologies and models in order to assess, amongst other factors, the changing macro-enconomic environment and the potential impact of the European sovereign debt crisis. These include the new European legislative initiatives to centralise supervision of large banks and to support bank resolution and bail-in of senior unsecured creditors. These measures alongside the specific rating drivers for pbb and its Pfandbriefe could lead to rating changes. Ratings could also be impacted by a change in ownership structure due to the Bank's planned privatisation. Downgrades to Bank and/or Pfandbrief-Ratings could have a negative impact, particularly on the Bank's funding conditions, on triggers and termination rights within derivatives and other contracts and on access to suitable hedge counterparties and hence on its financial position and profitability.

> The risk-bearing capacity concept is enhanced on a continuous basis. These enhancements and new regulatory requirements could have an impact on the risk-bearing capacity assessment using both the going concern approach and the gone concern approach. Under the gone concern approach, changes in the fair value of assets and liabilities also influence risk-bearing capacity. If hidden liabilities increase due to changes in fair value, the cover capital could fall below the economic capital requirement.

> pbb Group's image has been negatively impacted in recent years by its membership of the HRE Group. Although it has already successfully re-entered the markets, negative consequences for the achievement of pbb Group's objectives cannot be ruled out.

> Due to the nature and the international character of its business as well as the high number of relevant laws and regulations, pbb Group is involved in litigation, arbitration and regulatory proceedings in some countries. Legal disputes which are currently pending (especially relating to participation certificates issued, described under note Provisions) or could become pending in future could have a material adverse effect on pbb Group's results and equity base.

- pbb Group is exposed to operational risks, resulting, for example, from the technology risks associated with the large number of accounting systems. Although pbb Group has already successfully completed a number of projects to optimise processes and IT infrastructure, it is exposed to operational risks that could result in significant losses.
- A further operational risk results from reliance on employees who hold risk-taking positions. Employees in key positions could leave. This could impact the development in assets, financial position and earnings.
- Additional bank levies are planned or under discussion in most EU countries. Examples include the introduction of a European restructuring fund or a financial transaction tax. Such taxes could have a negative impact on pbb Group's results and render certain transactions unprofitable.

Summary

pbb Group's positive development in recent years is resulting in numerous opportunities to increase profitability in future. However, this assessment is based on the assumption that risks resulting e.g. from factors beyond pbb's control, such as the sovereign debt crisis, do not materialise. Overall, giving due consideration to the opportunities and risks, pbb Group is expecting a pre-tax profit of at least € 140 million for 2014.

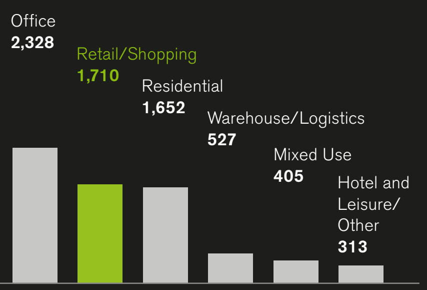
Höfe am Brühl Leipzig

€ 57 million

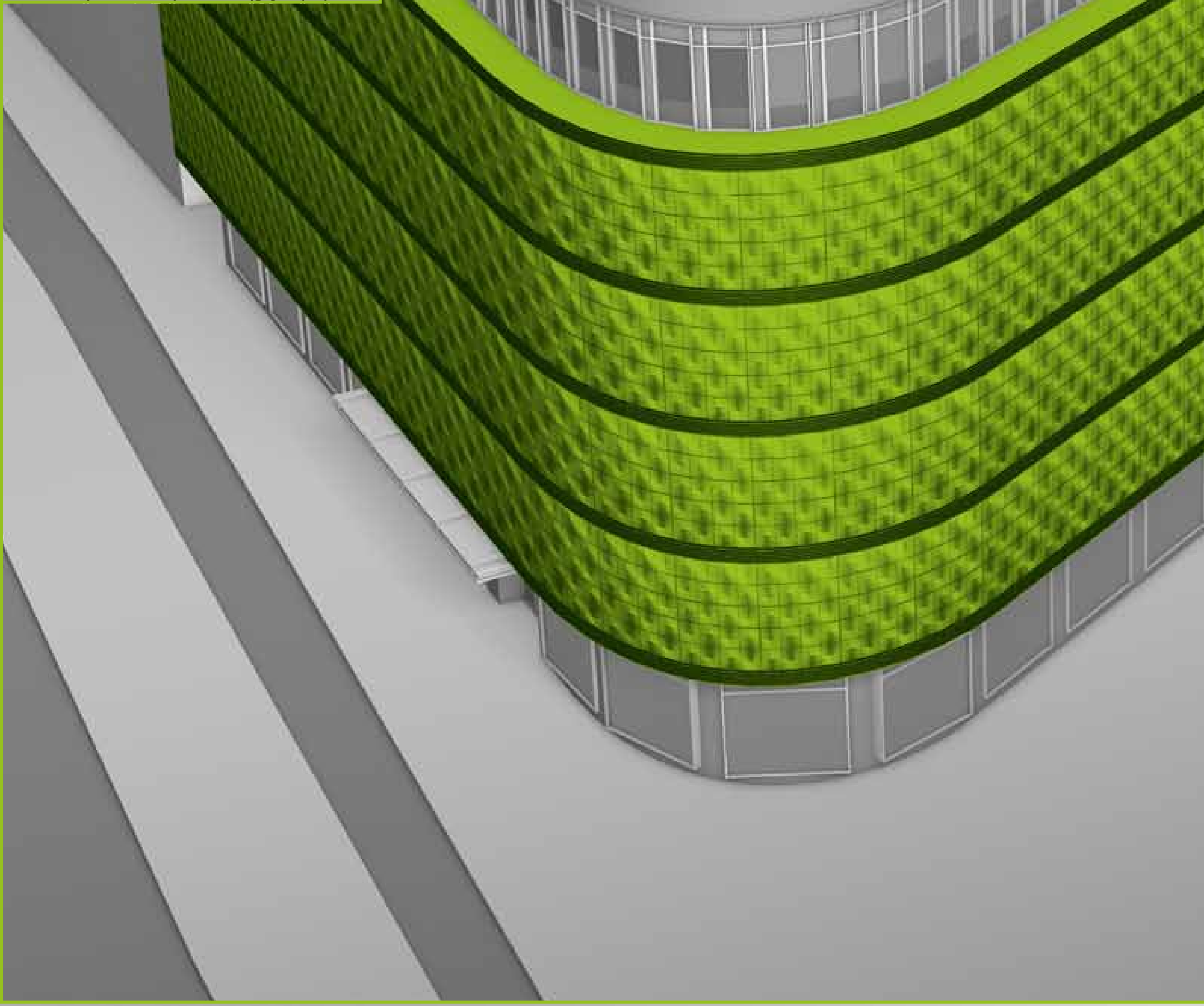
Syndicated investment finance
Germany
June 2013

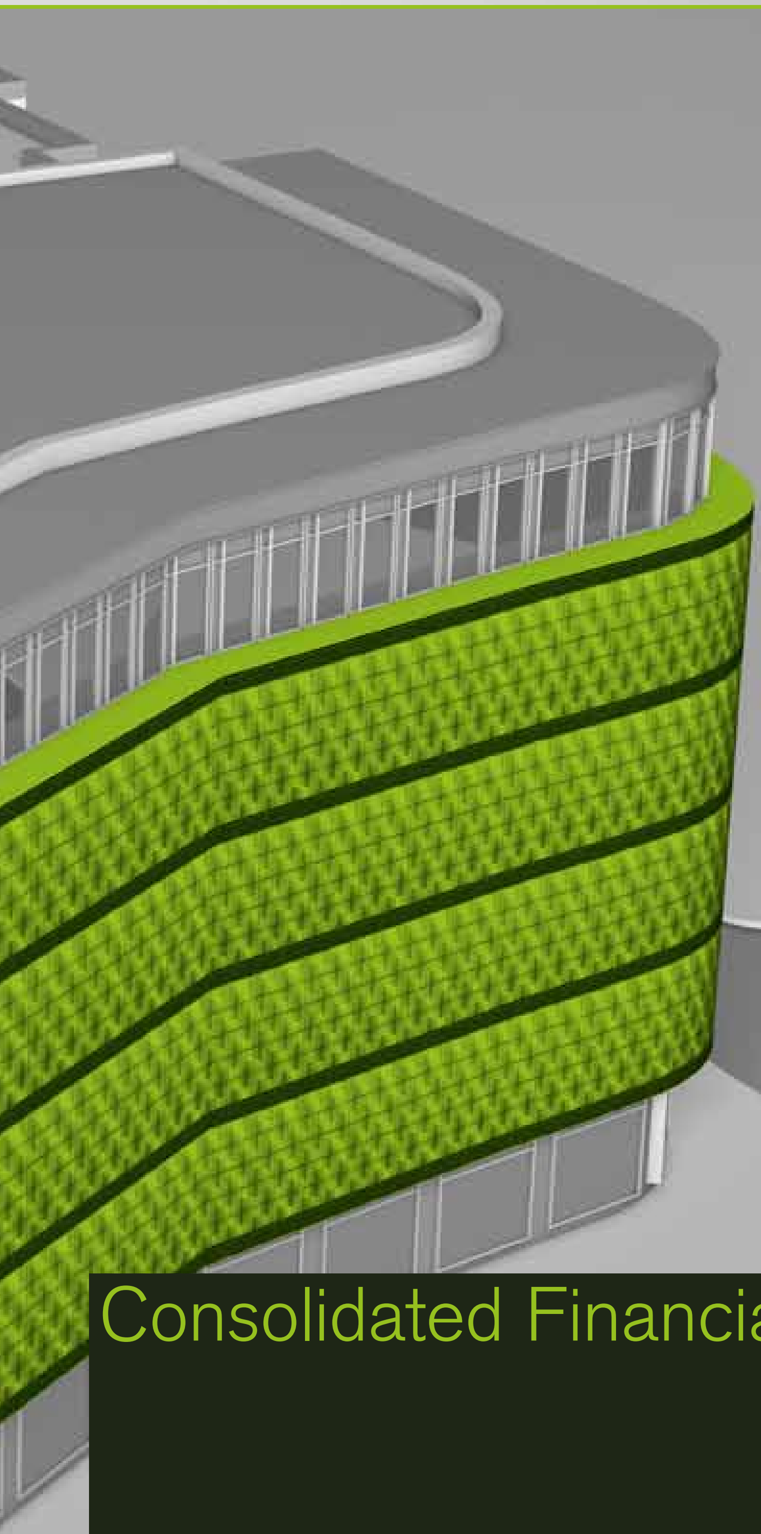
Loans in Germany constitute roughly half of pbb's entire real estate finance portfolio. The importance of the Bank's home market is also underscored by its share of new business in 2013, with over 50 percent attributable to German financing deals. Retail properties are among the key property types that pbb finances, both nationally and internationally. Höfe am Brühl is a shopping centre in central Leipzig with 133 shops, plus restaurants and apartments. pbb partnered with Deutschen Hypo, the arranger, and Helaba to provide the €170 million financing volume in equal parts.

Real Estate Finance: new business by property type
Commitments in € million



Germany
Leipzig





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Consolidated Financial Statements
Consolidated Income Statement

Income/expenses in € million	Notes	**2013**	**2012**	Δ in € million
Operating revenues		482	467	15
Net interest income and similar income	30	319	296	23
Interest income and similar income		2,448	2,879	−431
Interest expenses and similar expenses		−2,129	−2,583	454
Net commission income	31	9	23	−14
Commission income		15	27	−12
Commission expenses		−6	−4	−2
Net trading income	32	−51	10	−61
Net income from financial investments	33	96	13	83
Net income from hedge relationships	34	9	−6	15
Balance of other operating income/expenses	35	100	131	−31
Provision for losses on loans and advances	36	−8	4	−12
General administrative expenses	37	−312	−341	29
Balance of other income/expenses	38	3	−6	9
Pre-tax profit/loss		**165**	**124**	**41**
Taxes on income	39	−5	−55	50
Net income/loss		**160**	**69**	**91**
attributable to: Equity holders (consolidated profit/loss attributable to the parent company)		160	69	91

Consolidated Statement of Comprehensive Income

Consolidated statement of comprehensive income			2013			2012
in € million	Before tax	Tax	Net of tax	Before tax	Tax	Net of tax
Net income/loss	**165**	**–5**	**160**	**124**	**–55**	**69**
Items that will not be reclassified to income statement	7	–2	5	–56	14	–42
Additional paid-in capital	–	–	–	–	–	–
Retained earnings	–	–	–	–6	–	–6
Profits/losses from pension commitments[1]	7	–2	5	–50	14	–36
Items that may be reclassified to income statement	45	–13	32	240	–66	174
Foreign currency reserve	–1	–	–1	5	–	5
AfS reserve	196	–56	140	260	–71	189
Cash flow hedge reserve	–150	43	–107	–25	5	–20
Total other comprehensive income of the period	**52**	**–15**	**37**	**184**	**–52**	**132**
Total comprehensive income of the period	**217**	**–20**	**197**	**308**	**–107**	**201**
attributable to: Equity holders (consolidated profit/loss attributable to the parent company)	217	–20	197	308	–107	201

Disclosure of components of consolidated comprehensive income		
in € million	2013	2012
Net income/loss	**160**	**69**
Additional paid-in capital	–	–
Unrealised gains/losses	–	–
Retained earnings	–	–6
Unrealised gains/losses	–	–6
Profits/losses from pension commitments[1]	5	–36
Unrealised gains/losses	5	–36
Foreign currency reserve	–1	5
Unrealised gains/losses	–1	5
AfS reserve	140	189
Unrealised gains/losses	137	186
Reclassification adjustments for gains/losses included in profit or loss	3	3
Cash flow hedge reserve	–107	–20
Unrealised gains/losses	–175	16
Reclassification adjustments for gains/losses included in profit or loss	68	–36
Total other comprehensive income of the period	37	132
Total unrealised gains/losses	–34	165
Total reclassification adjustments for gains/losses included in profit or loss	71	–33
Total comprehensive income of the period	**197**	**201**

[1] Adjusted due to retrospective IAS 19 (revised) first time adoption. Details are disclosed in Note «Principles»

Consolidated Statement of Financial Position

Assets in € million	Notes	31.12.2013	31.12.2012[1]	Δ in € million	1.1.2012[1]
Cash reserve	7, 41	3,532	1,937	1,595	323
Trading assets	8, 42	1,642	3,325	–1,683	9,818
Loans and advances to other banks	9, 43	5,798	7,995	–2,197	7,632
Loans and advances to customers	9, 44	36,242	49,590	–13,348	55,236
Allowances for losses on loans and advances	10, 45	–148	–325	177	–477
Financial investments	11, 46	20,892	25,572	–4,680	28,677
Property, plant and equipment	12, 47	1	2	–1	3
Intangible assets	13, 48	31	39	–8	35
Other assets	14, 49	4,769	7,242	–2,473	6,065
Income tax assets	23, 50	1,165	1,704	–539	1,478
Current tax assets		44	53	–9	55
Deferred tax assets		1,121	1,651	–530	1,423
Total assets		**73,924**	**97,081**	**–23,157**	**108,790**

Equity and liabilities in € million	Notes	31.12.2013	31.12.2012[1]	Δ in € million	1.1.2012[1]
Liabilities to other banks	15, 54	3,522	7,797	–4,275	8,223
Liabilities to customers	15, 55	10,848	11,895	–1,047	12,363
Liabilities evidenced by certificates	15, 56	47,060	52,550	–5,490	55,038
Trading liabilities	16, 57	1,453	3,192	–1,739	9,903
Provisions	17, 58	209	235	–26	184
Other liabilities	18, 59	4,722	14,438	–9,716	16,123
Income tax liabilities	23, 60	1,190	1,698	–508	1,373
Current tax liabilities		64	64	–	82
Deferred tax liabilities		1,126	1,634	–508	1,291
Subordinated capital	19, 61	1,440	1,993	–553	2,501
Liabilities		**70,444**	**93,798**	**–23,354**	**105,708**
Equity attributable to equity holders		**3,480**	**3,283**	**197**	**3,082**
Subscribed capital	62	380	380	–	380
Silent participation	20, 62	999	999	–	999
Additional paid-in capital	62	5,036	5,036	–	5,036
Retained earnings	62	–3,097	–3,166	69	–3,277
Profits/losses from pension commitments		–41	–46	5	–10
Foreign currency reserve	22	–30	–29	–1	–34
Revaluation reserve	6	73	40	33	–129
AfS reserve		–220	–360	140	–549
Cash flow hedge reserve		293	400	–107	420
Consolidated profit/loss 1.1.–31.12.		160	69	91	117
Equity		**3,480**	**3,283**	**197**	**3,082**
Total equity and liabilities		**73,924**	**97,081**	**–23,157**	**108,790**

[1] Adjusted due to retrospective IAS 19 (revised) first time adoption. Details are disclosed in Note «Principles»

Consolidated Statement of Changes in Equity

Consolidated statement of changes in equity	Equity attributable to equity holders									
							Revaluation reserve			
in € million	Subscribed capital	Silent participation	Additional paid-in capital	Retained earnings	Profits/losses from pension commitments[1]	Foreign currency reserve	AfS reserve	Cash flow hedge reserve	Consolidated profit/loss	Equity
Equity at 1.1.2012	**380**	**999**	**5,036**	**−3,277**	**−10**	**−34**	**−549**	**420**	**117**	**3,082**
Capital increase	–	–	–	–	–	–	–	–	–	–
Transaction costs of capital measures	–	–	–	–	–	–	–	–	–	–
Treasury shares	–	–	–	–	–	–	–	–	–	–
Distribution	–	–	–	–	–	–	–	–	–	–
Total comprehensive income for the year	–	–	–	−6	−36	5	189	−20	69	201
Transfer to retained earnings	–	–	–	117	–	–	–	–	−117	–
Changes in the group of consolidated companies	–	–	–	–	–	–	–	–	–	–
Equity at 31.12.2012	**380**	**999**	**5,036**	**−3,166**	**−46**	**−29**	**−360**	**400**	**69**	**3,283**
Equity at 1.1.2013	**380**	**999**	**5,036**	**−3,166**	**−46**	**−29**	**−360**	**400**	**69**	**3,283**
Capital increase	–	–	–	–	–	–	–	–	–	–
Transaction costs of capital measures	–	–	–	–	–	–	–	–	–	–
Treasury shares	–	–	–	–	–	–	–	–	–	–
Distribution	–	–	–	–	–	–	–	–	–	–
Total comprehensive income for the year	–	–	–	–	5	−1	140	−107	160	197
Transfer to retained earnings	–	–	–	69	–	–	–	–	−69	–
Changes in the group of consolidated companies	–	–	–	–	–	–	–	–	–	–
Equity at 31.12.2013	**380**	**999**	**5,036**	**−3,097**	**−41**	**−30**	**−220**	**293**	**160**	**3,480**

[1] Adjusted due to retrospective IAS 19 (revised) first time adoption. Details are disclosed in Note «Principles»

Consolidated Statement of Cash Flows

Consolidated statement of cash flows[1] in € million	2013	2012
Net income/loss	**160**	**69**
Write-downs, provisions for losses on, and write-ups of, loans and advances and additions to provisions in lending business	13	4
Write-downs and depreciation less write-ups on non-current assets	15	19
Change in other non-cash positions	185	163
Result from the sale of non-current assets	–97	–18
Other adjustments	–320	–241
Subtotal	**–44**	**–4**
Change in assets and liabilities from operating activities after correction for non-cash components		
Increase in assets/decrease in liabilities (–)		
Decrease in assets/increase in liabilities (+)		
Trading portfolio	–57	–235
Loans and advances to other banks	2,127	–546
Loans and advances to customers	4,892	5,837
Other assets from operating activities	119	–108
Liabilities to other banks	–3,992	–493
Liabilities to customers	–927	–545
Liabilities evidenced by certificates	–3,646	–3,433
Other liabilities from operating activities	–561	–2,276
Interest income received	2,226	2,493
Dividend income received	–	1
Interest expense paid	–1,987	–2,267
Taxes on income paid	11	–17
Cash flow from operating activities	**–1,839**	**–1,593**
Proceeds from the sale of non-current assets	4,843	4,290
Payments for the acquisition of non-current assets	–944	–533
Proceeds from the sale of investments	81	–
Payments for the acquisition of investments	–	–
Cash flow from investing activities	**3,980**	**3,757**
Payments of subordinated capital	–546	–550
Cash flow from financing activities	**–546**	**–550**
Cash and cash equivalents at the end of the previous period	1,937	323
+/– Cash flow from operating activities	–1,839	–1,593
+/– Cash flow from investing activities	3,980	3,757
+/– Cash flow from financing activities	–546	–550
+/– Effects of exchange rate changes and non-cash valuation changes	–	–
Cash and cash equivalents at the end of the period	**3,532**	**1,937**

[1] Explanations in Note «Notes to the Items in the Consolidated Statement of Cash Flows»

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1 General Information

The Group is headed by pbb which is registered in the commercial register of the Amtsgericht (local court) Munich (HRB 41054) and is a 100% subsidiary of Hypo Real Estate Holding AG (HRE Holding). HRE Holding is a 100% subsidiary of Finanzmarktstabilisierungsfonds-FMS. pbb Group combines the strategic assets and new business of Hypo Real Estate Group (HRE). New business is generated in public investment finance and real estate finance.

Accounting Policies

2 Principles

pbb has prepared its Group financial statements for the period ended 31 December 2013 in line with EC ordinance No. 1606/2002 of the European Parliament and Council of 19 July 2002 in accordance with International Financial Reporting Standards (IFRS). These financial statements are based on the IFRS rules, which have been adopted in European Law by the European commission as part of the endorsement process; it is also based on the regulations of commercial law which are applicable in accordance with section 315a (1) HGB (German Commercial Code).

The IFRS are standards and interpretations adopted by the International Accounting Standards Board (IASB). These are the International Financial Reporting Standards (IFRS), the International Accounting Standards (IAS) and the interpretations of the IFRS Interpretations Committee (formerly IFRIC) or the former Standing Interpretations Committee (SIC).

If they are not inconsistent with the IFRS, the German Accounting Standards (Deutsche Rechnungslegungs Standards – DRS) published by the Deutsche Rechnungslegungs Standards Committee (DRSC) have been taken into account.

The Management Board of pbb prepared these consolidated financial statements on 18 March 2014 under the going-concern assumption.

Initially Adopted Standards, Interpretations and Amendments Applied for the First Time The following standards, interpretations and amendments, sorted by their date of endorsement by the European Union, were applied for the first time in financial year 2013:
> Amendments to IAS 1 Presentation of Items of Other Comprehensive Income
> Amendments to IAS 12 Income Taxes – Deferred Tax: Recovery of Underlying Assets
> Amendments to IFRS 1 – Severe Hyperinflation and Removal of Fixed Dates for First-time Adopters
> Amendments to IFRS 1 – Government Loans
> Amendments to IFRS 7 Financial Instruments: Disclosure – Offsetting Financial Assets and Financial Liabilities
> IAS 19 (revised 2011) Employee Benefits
> IFRIC Interpretation 20: Stripping Costs in the Production Phase of a Surface Mine
> IFRS 13 Fair Value Measurement
> Improvements to IFRS (2011)

Under the amendments to IAS 1, items of other comprehensive income are required to be grouped and presented based on whether they could be recycled to the consolidated income statement. The presentation requirements were taken into account in these consolidated financial statements by adding new headings to the consolidated statement of comprehensive income.

The amendments to IAS 12 supersede interpretation SIC-21 and govern the manner in which it should be presumed that investment properties, property, plant and equipment and intangible assets measured at fair value will be recovered when measuring deferred taxes. They had no impact on these consolidated financial statements, as pbb Group measures such assets at amortised cost.

Amendments to IFRS 1 – Severe Hyperinflation and Removal of Fixed Dates for First-time Adopters and Amendments to IFRS 1 – Government Loans relate only to first-time adopters of IFRSs and therefore have no impact on pbb Group.

The amendments to IFRS 7 extend the disclosures required about financial assets and financial liabilities that have been set off. In addition to a qualitative description of rights of set-off, they also require extensive quantitative disclosures, such as the gross amount before offsetting, the net amount after offsetting and the fair value of financial instruments received or pledged as collateral. The extended disclosure requirements were taken into account in these consolidated financial instruments in the note Offsetting of Financial Instruments.

IAS 19 (revised 2011) removes the option to use the corridor approach to recognise actuarial gains and losses. Instead, these effects must be recognised in equity (other comprehensive income). Past service cost must be recognised in the period in which the underlying plan amendment occurs rather than allocated over the vesting period of the benefits, as was the case previously. Under IAS 19 (revised 2011), the interest rate determined for discounting pension obligations is now also used for expected returns on plan assets. In addition, IAS 19 (revised 2011) changes the accounting for bonus payments for partial retirement agreements. IAS 19.173 requires the changes under IAS 19 (revised 2011) to be applied retrospectively. Due to the change in the presentation of actuarial gains/losses, equity declined by €46 million as at 31 December 2012 (prior-year reporting date) (31 December 2011: €10 million). Actuarial gains/losses arising from defined benefit obligations are presented in a separate line item in equity. At the same time, provisions for pensions and similar obligations increased by €71 million (31 December 2011: €21 million). Deferred tax assets for these items increased by €18 million as at 31 December 2012 (31 December 2011: €4 million) as wells as other assets by €7 million (31 December 2011: €7 million). As the effects of the change in the interest rate determined for expected returns on plan assets and the change in the recognition of past service cost and bonus payments for partial retirement agreements are insignificant for pbb Group, the prior-year consolidated income statement was unaffected. Due to the change in actuarial gains and losses arising from defined benefit obligations, prior-year total comprehensive income, which also includes changes in equity, declined by €36 million.

IFRIC 20 governs the treatment of stripping costs incurred in surface mining. Due to pbb Group's business model, IFRIC 20 has no impact on these consolidated financial statements.

IFRS 13 combines the rules on fair value measurement for all assets and liabilities. Significant new requirements in IFRS 13 relate, for example, to the definition of fair value as the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction in the principal market (or most advantageous market) at the measurement date under current market conditions (i.e. an exit price). pbb Group ensures that items are measured at exit prices by using secondary market spreads or referring to them for validation. This primarily had an impact of €–0.1 billion on the fair values of pbb Group's financial assets and liabilities. IFRS 13 also extends the disclosure requirements, particularly for the fair value hierarchy. The extended disclosures are presented in these consolidated financial statements in the Note «Fair Values of Financial Instruments».

Improvements to IFRSs (2011) contain minor changes to or clarifications of IFRS 1, IAS 1, IAS 16, IAS 32 and IAS 34. It had no significant impact on these consolidated financial statements.

Standards, Interpretations and Amendments Endorsed but Not Yet Effective The following standards, interpretations and amendments, sorted by their date of endorsement by the European Union, were endorsed prior to 31 December 2013, but are not yet effective and were not applied early:

- IFRS 10 Consolidated Financial Statements and Amendments to IAS 27 Separate Financial Statements
- IFRS 11 Joint Arrangements and Amendments to IAS 28 Investments in Associates and Joint Ventures
- IFRS 12 Disclosure of Interests in Other Entities
- Amendments to IFRS 10 Consolidated Financial Statements, IFRS 11 Joint Arrangements and IFRS 12 Disclosure of Interests in Other Entities: Transition Guidance
- Amendments to IFRS 10 Consolidated Financial Statements, IFRS 12 Disclosure of Interests in Other Entities and IAS 27 Separate Financial Statements: Investment Entities
- Amendments to IAS 32: Offsetting Financial Assets and Financial Liabilities
- Amendments to IAS 36: Recoverable Amount Disclosures for Non Financial Assets
- Amendments to IAS 39: Novation of Derivatives and Continuation of Hedge Accounting

IFRS 10 replaces the guidance on control and consolidation previously contained in IAS 27 and SIC-12. IFRS 10 introduces the concept of control as the basis for consolidation. Under this model, parent-subsidiary relationships can arise not only from voting power, but from other contractual arrangements as well. IAS 27 was renamed Separate Financial Statements and now deals only with separate financial statements; SIC-12 was withdrawn. The new standards were initially effective for financial years beginning on or after 1 January 2013. However, they were endorsed by the European Union with an effective date of 1 January 2014. Initial application of IFRS 10 is expected to result in only two changes in the consolidated group structure of pbb Group. The previously consolidated House of Europe Funding I Ltd., Grand Cayman, will cease to be consolidated, as a result of which the total assets of pbb Group will decline by €0.2 billion. Ceasing to consolidate the entity will have no impact on pbb Group's income statement. In addition, DEPFA Finance N.V., Amsterdam, will be consolidated for the first time. This will increase pbb Group's equity by €5 million and its total assets by €0.9 billion. Consolidating the entity for the first time is not expected to have a significant impact on pbb Group's income statement.

IFRS 11 supersedes IAS 31 and removes the option to proportionately consolidate joint ventures. In future, joint ventures will be accounted for using the equity method in accordance with IAS 28. The new standards were initially effective for financial years beginning on or after 1 January 2013. However, they were endorsed by the European Union with an effective date of 1 January 2014. The impact on future consolidated financial statements will depend on whether or not pbb Group has any joint ventures or investments required to be included using the equity method in future. This is not currently the case.

IFRS 12 combines the disclosure requirements for interests in subsidiaries, joint ventures, associates and unconsolidated structured entities in a single standard. The new standard was initially effective for financial years beginning on or after 1 January 2013. However, it was endorsed by the European Union with an effective date of 1 January 2014. pbb Group expects the application of IFRS 12 to result in extended disclosures about interests in other entities.

Transition Guidance (Amendments to IFRS 10, IFRS 11 and IFRS 12) clarifies that decisions about whether or not investments are required to be consolidated in accordance with IFRS 10 should be made at the beginning of the period in which the standard is applied for the first time. In pbb Group, the decision will therefore be made on 1 January 2014. pbb Group has changed its accounting processes to ensure that the decision about whether to consolidate is made on 1 January 2014.

Investment Entities (Amendments to IFRS 10, IFRS 12 and IAS 27) exempts specifically defined investment entities from the requirement to consolidate subsidiaries that they control. The investments in question must instead be measured at fair value through profit or loss. IFRS 12 also contains specific disclosure requirements for investment entities. As pbb Group is not an investment entity within the meaning of the IFRS definition, this will have no impact on pbb Group.

The amendments to IAS 32 clarify the requirements for offsetting financial instruments. They also explain the meaning of «currently has a legally enforceable right of set-off» and clarify which gross settlement systems may be considered equivalent to net settlement within the meaning of the standard. The amendments to IAS 32 must be applied for the first time for financial years beginning on or after 1 January 2014. The clarification of IAS 32 is not expected to have a significant impact on pbb Group. The amendments to IFRS 7 Financial Instruments accompanying the amendments to IAS 32 and the resulting extended disclosures were presented in these financial statements in the note Offsetting of Financial Instruments.

The amendments to IAS 36 correct a disclosure requirement introduced into IAS 36 by IFRS 13 regarding the recoverable amount of cash-generating units to which a significant amount of goodwill or intangible assets with indefinite useful lives has been allocated. They also introduce new disclosures when an impairment loss is recognised or reversed for an asset or a cash-generating unit and recoverable amount was based on fair value less costs of disposal. The amendments must be applied retrospectively, but only for reporting periods in which IFRS 13 has already been applied. They are not expected to have any impact on pbb Group unless it holds such intangible assets in future.

Lawmakers have made far-reaching legal changes designed to improve transparency and regulatory oversight of over-the-counter derivatives. For example, entities are required to novate derivatives to central counterparties subject to certain conditions. The amendments to IAS 39 take account of these changes, as the previous IAS 39 requires hedge accounting to cease if the original derivative no longer exists. For hedge accounting purposes, the derivative entered into with the central counterparty would have to be redesignated as a hedging instrument, which may result in more ineffectiveness compared with the previous hedging relationship. The IASB has therefore added a provision to the previous IAS 39 providing relief from the requirement to cease hedge accounting if the novation of a hedging instrument with a central counterparty meets certain criteria. In particular, the relief requires that novation be required by laws or regulations. The amendments to IAS 39 must be applied for financial years beginning on or after 1 January 2014. Early application of the requirements is permitted. pbb Group will make use of the relief in order to maximise the effectiveness of its hedging relationships.

Standards, Interpretations and Amendments Issued but Not Yet Endorsed In addition, the following standards, interpretations and amendments, sorted by their date of publication, were issued, but had not yet been endorsed by the European Union and not applied early by pbb Group at the reporting date:

- IFRS 9 – Financial Instruments
- IFRS 9 – Hedge Accounting and Amendments to IFRS 9, IFRS 7 and IAS 39
- Amendments to IFRS 9 and IFRS 7 – Mandatory Effective Date and Transition Disclosures
- Amendments to IAS 19 (revised 2011) Employee Benefits: Defined Benefit Plans – Employee Contributions
- IFRIC Interpretation 21 Levies
- Improvements to IFRSs 2012
- Improvements to IFRSs 2013

The IASB is replacing IAS 39 with IFRS 9 through a project in several phases. In 2009 and 2010, the IASB published new requirements for the first phase of the project, Classification and Measurement, which are likely to be amended again. For the Impairment Methodology and Hedge Accounting phases of the project, on the other hand, no sections of the standard have yet been adopted. The Classification and Measurement phase is expected to provide the following measurement categories for the classification of financial instruments:
> at fair value through profit or loss
> at fair value through other comprehensive income
> at amortised cost

The classification of financial debt instruments on the assets side depends on the entity's business model for managing financial assets and the characteristics of the contractual cash flows of the financial asset. Equity instruments and assets at FVTPL, on the other hand, are generally required to be measured at fair value. On the liabilities side, non-derivative liabilities that are not held for trading or that the entity does not elect to measure at fair value must be measured at amortised cost. Changes in the value of liabilities at FVTPL that are attributable to changes in the entity's own credit risk are required to be recognised directly in equity. The effective date of IFRS 9 is currently expected to be 1 January 2018. Initial application of the new standard is expected to have an extensive impact on pbb's consolidated financial statements. It is likely that some assets and liabilities previously measured at amortised cost will have to be measured at fair value in future and vice versa. However, the overall impact on pbb Group will not become clear until all sections of IFRS 9 have been published.

Amendments to IFRS 10, IFRS 11 and IFRS 12: Transition Guidance clarify the retrospective application of the concerned standards and have to be initially adopted along with IFRS 10, IFRS 11 and IFRS 12 for financial years beginning on or after 1 January 2014.

In a second phase of the project, the IASB published IFRS 9 – Hedge Accounting and Amendments to IFRS 9, IFRS 7 and IAS 39. The aim of the hedge accounting model under IFRS 9 is to more closely align accounting with the risk management system. The types of hedging relationship still permitted are:
> Cash flow hedge accounting
> Fair value hedge accounting
> Hedge of a net investment in a foreign operation

The list of qualifying hedged items and hedges has in each case been extended. In particular, groups of hedged items may now be designated if, individually, the hedged items qualify for designation, as may net positions and nil net positions. As a rule, any financial instrument measured at fair value is suitable as a hedging instrument. The exception to this rule are liabilities for which the fair value option has been used and equity instruments designated at fair value through other comprehensive income. IFRS 9 dispenses with the range of 80% to 125% required by IAS 39 when measuring effectiveness, as a result of which effectiveness no longer has to be tested retrospectively. Effectiveness still has to be tested prospectively and any ineffectiveness recognised. A hedging relationship may only be discontinued if the requirements defined for this are met; this means that hedging relationships must be continued if the risk management objective remains unchanged. Extended disclosures have to be made about the risk management strategy, the effects of risk management on future cash flows and the effects of hedge accounting on the financial statements. In addition, recognition in other comprehensive income of own credit risk for financial liabilities that the entity has elected to measure at fair value is now possible in isolation, i.e. without applying the other requirements under IFRS 9. This section of IFRS 9 must be initially applied in accordance with the requirements on the initial application of IFRS 9 as a whole. The requirements will have an impact on pbb Group's hedge accounting. However, it will not be possible to assess the overall impact until all sections of IFRS 9 have been published.

Mandatory Effective Date and Transition Disclosures (Amendments to IFRS 9 and IFRS 7) provides relief from restating prior-year amounts when applying IFRS 9 for the first time. This relief was initially only available when early applying IFRS 9 before 1 January 2012 and involves making additional disclosures in accordance with IFRS 7 at the date of transition. The effective date of these amendments is the same as specified in IFRS 9.

The amendments to IAS 19 (revised 2011) clarify the requirements regarding the attribution of employee contributions or contributions from third parties to periods of service when the contributions are linked to service. They also provide relief when contributions are independent of the number of years of service. Subject to endorsement by the European Union, the amendments are effective for financial years beginning on or after 1 July 2014. They are not expected to have a significant impact on pbb Group.

IFRIC 21 Levies is an interpretation of IAS 37 Provisions, Contingent Liabilities and Contingent Assets. IFRIC 21 clarifies when a present obligation exists and a provision or liability has to be recognised for levies imposed by governments. In particular, levies resulting from IAS 12 Income Taxes are not within the scope of IFRIC 21. IFRIC 21 requires a liability to be recognised for levies when the event triggering the obligation to pay the levy occurs. This triggering event that gives rise to the obligation results, in turn, from the wording of the underlying standard. Its wording therefore determines the accounting treatment. Subject to endorsement by the European Union, the interpretation is effective for financial years beginning on or after 1 January 2014. For pbb Group, IFRIC 21 is not at present expected to have a significant impact on the levies currently payable.

Through the Annual Improvements Project, minor amendments are made to individual standards in order to clarify issues or standardise the wording. Improvements to IFRSs 2012 related to IFRS 2, IFRS 3, IFRS 8, IFRS 13, IAS 16, IAS 24 and IAS 38, and Improvements to IFRSs 2013 to IFRS 1, IFRS 3, IFRS 13 and IAS 40. Subject to endorsement by the European Union, both sets of improvements are effective for financial years beginning on or after 1 July 2014. They are not expected to have a significant impact on pbb Group.

Statement of Compliance for the Public Corporate Governance Code of the Federation The Management Board of the Company, that is wholly owned indirectly by the Federal Republic of Germany, has resolved to use the Public Corporate Governance Code of the federal government, which is based on the «comply or explain» principle, subject to identical resolution by the Supervisory Board. The Management Board and the Supervisory Board published a statement of compliance for the public corporate governance code of the federation on pbb'a website (www.pfandbriefbank.com) after the respective resolution is adopted by the Supervisory Board.

Group Management Report The Group management report meets the requirements of section 315 (1) and (2) HGB (German Civil Code) and DRS 20, which was already initially adopted in the reporting year 2012 on a voluntarily basis. It comprises fundamental information about the Group, a report on the economic position, a report on post-balance-sheet date events, and a report on expected developments as well as a risk and opportunity report. The risk and opportunity report contains information which, under IFRS 7, is required to be disclosed. Events after the balance sheet date are described in the report on post-balance-sheet date events.

3 Consistency

pbb Group applies accounting policies consistently in accordance with the framework of IFRS as well as IAS 1 and IAS 8.

In financial year 2013, pbb Group changed the presentation logic for expenditure items. These are now shown with minus signs. Prior-year figures are presented in the same way.

As of 31 December 2013 pbb Group applied the equal accounting and measurement principles as in the consolidated financial statements as of 31 December 2012.

4 Uniform Consolidated Accounting

The separate financial statements of the consolidated domestic and foreign companies are incorporated in the consolidated financial statements of pbb Group using uniform accounting and measurement principles.

5 Consolidation

Number of subsidiaries/ entities[1]	Fully consolidated subsidiaries		Not fully consolidated subsidiaries[1]		Associated companies and other investments		
	Total	Thereof special-purpose entities	Total	Thereof special-purpose entities	Associated companies	Other investments	**Total**
1.1.2012	**12**	**4**	**7**	**2**	**4**	**6**	**29**
Additions	1	1	–	–	–	–	1
Disposals	–2	–	–1	–1	–1	–2	–6
Mergers	–1	–	–1	–	–	–	–2
31.12.2012	**10**	**5**	**5**	**1**	**3**	**4**	**22**
1.1.2013	**10**	**5**	**5**	**1**	**3**	**4**	**22**
Additions	1	1	–	–	–	–	1
Disposals	–1	–1	–	–	–	–	–1
Mergers	–	–	–1	–	–	–	–1
31.12.2013	**10**	**5**	**4**	**1**	**3**	**4**	**21**

[1] pbb, subsidiaries (including special-purpose entities), associated companies and other investments
[2] Not fully consolidated due to immateriality respectively not to be consolidated according to SIC-12

These consolidated financial statements set out a list of shareholdings in the chapter «Holdings». In this list, the subsidiaries are structured on the basis of whether or not they are consolidated. Other shareholdings are also listed. All fully consolidated companies have prepared their individual financial statements for the period ended 31 December 2013.

The effects of the contractual relations between the Group companies and the subsidiaries which are not consolidated are set out in the consolidated financial statements. The pooled results of the subsidiaries, which have not been consolidated in view of their minor significance, are less than € 1 million (2012: € 2 million). Net losses are almost completely included in the Group financial statement by depreciation on investments, provisions and profits transferred. The pooled total assets of the non-consolidated subsidiaries account as in the previous year for less than 0.1% of the Group's total assets. The shares in the non-consolidated companies are shown as AfS financial investments.

pbb holds 100% of the interest in DEPFA Finance N.V., Amsterdam. As the majority of risks and rewards is held Group-externally pbb has not to consolidate the special-purpose entity according to IAS 27 in conjunction with SIC 12.

In 2013 it came to the following changes in consolidation:

All shares of Little Britain Holdings (Jersey) Ltd., Jersey, were sold on 20 September 2013. The selling price less costs and the repayment of a liability owed by the company to pbb was €79 million. The deconsolidation resulted in a gain of €92 million, which was recognised in pbb's consolidated financial statements under net income from financial investments. The €1 million loss generated by the company between 1 January and the date of sale, 20 September 2013, is included in pbb's consolidated financial statements. The total assets in accordance with the accounting policies applicable to pbb's consolidated financial statements amounted to €97 million. The assets side of the company's statement of financial position primarily comprised salvage acquisitions in the amount of €91 million, which were reported under other assets. The equity and liabilities side mainly consisted of a liability to pbb in the amount of €108 million and equity in the amount of €–13 million.

FUNDUS Gesellschaft für Grundbesitz und Beteiligungen GmbH, Munich, previously an unconsolidated subsidiary, was merged with pbb effective 28 August 2013.

The company RPPSE Espacio Oviedo S.L.U., Madrid, was initially consolidated on 26 Novermber 2013. On this day pbb firmly committed to take over the participation in the company and gained control over the company. The company has a property with a book value of €27 million on the asset side according to the accounting policies of the Group and a funding from pbb about €61 million on the liability side. The initial consolidation resulted in an asset change. pbb Group recognises the property with a book value of €27 million as a salvage acquisition under the item other assets instead of the loan impaired to this amount. There have been no material effects on the income statement. The shares were purchased for €1 on 25 February 2014 by IMMO Invest Real Estate GmbH, Munich, a subsidiary of pbb.

Consolidation Principles At the acquisition date the costs of a business combination are allocated by recognising the acquiree's identifiable assets, liabilities and contingent liabilities that satisfy the recognition criteria according to IFRS 3.10 at their fair values at that date. Any difference between the cost of the business combination and the acquirer's interest in the net fair value of the identifiable assets, liabilities and contingent liabilities so recognised are accounted as goodwill or as an excess of acquirer's interest in the net fair value of acquiree's identifiable assets, liabilities and contingent liabilities in accordance with IFRS 3.32-36. If the interest in net fair value of the identifiable assets, liabilities and contingent liabilities exceeds the costs of business combination the acquirer shall reassess the identifiable assets, liabilities and contingent liabilities and the measurement of the cost of the combination, and recognise immediately in profit or loss any excess remaining after reassessment.

Business relations within the group of consolidated companies are netted with respect to each other. Intercompany results attributable to internal transactions are eliminated.

There are no material interests in associated companies or joint ventures. The holdings are accounted as AfS financial instruments.

6 Financial Instruments

According to IAS 32, a financial instrument is any contract that gives rise to a financial asset of one entity and a financial liability or equity instrument of another entity.

Recognition and Derecognition pbb Group recognises a financial asset or a financial liability in its statement of financial position if a Group company becomes party to the contractual provisions of the financial instrument.

The purchases or sales of financial instruments are recognised on the trading date. Premiums and discounts are recognised in accordance with the accrual concept in the position net interest income and similar income. In accordance with the primary derecognition concept of IAS 39, a financial asset has to be derecognised when all risks and rewards have substantially been transferred. If the main risks and rewards of ownership of the transferred financial asset are neither transferred nor retained, and if control over the transferred asset is retained, the Company has to recognise the asset to the extent of its continuing involvement. There are no transactions within pbb Group which result in partial derecognition due to a continuing involvement.

In case of pension agreements and synthetic securitisations the assets transferred do not qualify for derecognition because derecognition criteria of IAS 39 are not fulfilled.

Collaterals with the same counterparty and same conditions (e.g. ISDA frame contract) are netted according to IAS 32.34 and thus disclosed as a net amount.

Categories According to IAS 39 When a financial asset or financial liability is recognised initially, it is measured at its fair value.

For subsequent measurement purposes IAS 39 requires that all financial instruments have to be classified according to this standard, to be disclosed in the statement of financial position and to be measured according to its categorisation:

Held-for-Trading A financial asset or a financial liability is held for trading if it is:
> acquired or incurred principally for the purpose of selling or repurchasing it in the near term
> part of a portfolio of identified financial instruments that are managed together and for which there is evidence of a recent actual pattern of short-term profit-taking
> a derivative (except for a derivative that is a designated and effective hedging instrument)

Held-for-trading financial instruments are measured at fair value. Changes in fair value are recognised in profit or loss. Held-for-trading financial instruments are disclosed as trading assets and trading liabilities. Interest and dividend income as well as the refinancing costs for the held-for-trading instruments are recognised in net trading income.

If there is a difference between transaction price and market value at the trading date and the difference results from unobservable data that have a significant impact on the measurement of a financial instrument, the difference (so-called day one profit) is not recognised immediately in profit or loss but is recognised over the life of the transaction. The remaining difference is recognised directly in profit or loss when the inputs become observable, when the transaction matures or is closed out. In the financial years 2013 and 2012 there were no material day one profits.

Designated at Fair Value through Profit or Loss (dFVTPL) If certain conditions are satisfied, financial assets or liabilities can be classified as a financial asset respectively a financial liability at fair value through profit or loss when they are initially recognised. A designation can be made if the use of the measurement category means that a recognition and measurement inconsistency is either avoided or considerably reduced, and management and performance measurement of a portfolio of financial instruments are based on the fair values or if the instrument contains a separable embedded derivative. dFVTPL financial instruments are measured at fair value. Changes in fair value are recognised in profit or loss.

As of 31 December 2013, pbb Group had no financial assets and no financial liabilities in the category dFVTPL. As of 31 December 2012, one fixed-income security was held in the category dFVTPL. An inconsistency in terms of measurement was avoided by this designation. This security was recognised under financial investments. Interest income from the securities was recognised in net interest income and similar income. The changes in value to be recognised in profit or loss were recognised in net income from hedge relationships in the same way as the changes in value of the corresponding derivatives.

Held-to-Maturity (HtM) Held-to-maturity investments are non-derivative financial assets with fixed or determinable payments and fixed maturity that an entity has the positive intention and ability to hold to maturity. HtM financial investments are measured at amortised cost. In financial years 2013 and 2012, no financial assets were classified as HtM at pbb Group.

Loans and Receivables (LaR) Loans and receivables are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market. Loans and receivables include bonded notes.

Loans and receivables are recognised in the positions loans and advances to banks, loans and advances to customers and financial investments, and are measured at amortised cost. Interest income from loans and receivables is recognised in net interest income and similar income. Market price related net gains and net losses attributable to prepayment penalties and disposal of loans and advances to customers and of loans and advances to banks are disclosed in net interest income and similar income. Such net gains and net losses from financial investments are recognised in net income from financial investments. Impairments due to credit standing factors and which affecting profit or loss are recognised in provisions for losses on loans and advances respectively, in the case of financial investments, in net income from financial investments.

Available-for-Sale (AfS) Available-for-sale assets are those non-derivative financial assets that are classified as available for sale and which are not classified as loans and receivables, held-to-maturity investments or financial assets at fair value through profit or loss. pbb Group only classifies securities as AfS but not loans and advances.

AfS financial assets are measured at fair value. Changes in fair value are recognised in a separate item of equity (AfS reserve) not affecting profit or loss until the asset is sold, withdrawn or otherwise disposed of or if an impairment is established for the financial asset in accordance with IAS 39.58 et seq., so that the cumulative loss previously recognised in equity is now recognised in profit or loss. If the objective evidence for the impairment of an AfS debt instrument drops out, the impairment has to be reversed through profit or loss. On the other hand, impairments of an AfS equity instrument which have been recognised in profit or loss are not permitted to be reversed through profit or loss.

AfS financial assets are disclosed as financial investments. Interest income from AfS assets is recognised in net interest income and similar income. Net gains and net losses generated by the disposal of AfS financial instruments as well as by changes in value as a result of impairment or reversals to be recognised in profit or loss are recognised in net income from financial investments.

Financial Liabilities at Amortised Cost Financial liabilities at amortised cost are those non-derivative financial liabilities that are not classified at fair value through profit or loss.

Financial liabilities at amortised cost are measured at amortised cost. Financial liabilities at amortised cost that are not securitised are recognised in liabilities to other banks and liabilities to customers. If these financial liabilities are securitised and not subordinated, they are recognised in liabilities evidenced by certificates. Subordinated liabilities are recognised in subordinated capital. Interest expenses from financial liabilities at amortised cost are recognised in net interest income and similar income. In addition, the position net interest income and similar income includes net gains and net losses attributable to repurchases or withdrawals before maturity as well as impairments and impairment reversals of financial liabilities at amortised cost.

Derivatives Derivatives are measured at fair value. Changes in fair value are recognised in profit or loss if the derivatives are not part of cash flow hedge accounting. The measurement gains and losses from stand-alone derivatives are recognised in net trading income and from hedging derivatives in net income from hedge relationships. In the statement of financial position, stand-alone derivatives are disclosed as trading assets and trading liabilities. Hedging derivatives are disclosed as other assets and other liabilities.

Outside the held-for-trading and dFVTPL category, embedded derivative financial instruments within a structured product and which are required to be separated are separated from the host contract and recognised as stand-alone derivative financial instruments. Thereafter, the host contract is measured in accordance with its classification. The change in value arising from the separated derivatives that are measured at fair value is recognised in profit or loss.

Classes IFRS 7 and IFRS 13 required disclosures according to classes of financial instruments. pbb Group mainly defined the IAS 39 measurement categories, irrevocable loan commitments, financial guarantees, hedging derivatives and cash reserve as classes.

Measurement Methods Financial instruments at fair value are measured on the basis of stock market prices or other market prices, if existent. If a price is not available from an active market, observable market prices from comparable financial instruments are used. If prices from comparable financial instruments are not available, valuation models are used that base on observable market parameters. If these parameters are not observable at the markets, the measurement of the financial assets is based on models with non-market-observable parameters. The used measurement models are market standard models. A description of these models and the products is given in the Note «Fair Values of Financial Instruments».

Impairment According to IAS 39.58 a financial asset must be tested for impairment. At each balance sheet date pbb Group assesses on a case-by-case basis whether there is objective evidence for impairment. The criteria used to determine if there is such objective evidence included:
> significant financial difficulties of the borrower
> overdue contractual payments of either principal or interest or other breaches of contract
> increased probability that the borrower will enter bankruptcy or other financial reorganisation
> renegotiations due to economic problems
> a decline in the fair value of a financial asset below its (amortised) cost

Receivables at risk of default are restructured by pbb Group when the borrower's financial position has detoriated but going concern for the loan exposure can still be assumed. The Group then partly grants special conditions by agreeing to terms and conditions that are more favourable for the borrower than the Group has provided initially. The Group implements a forbearance policy, respectively restructuring agreements in order to maximise collection opportunities and minimise the risk of default.

Under the Group's forbearance policy respectively restructuring agreement, loan forbearance or loan extension is granted on a selective basis in a situation where the debtor is currently in default on its debt, or where there is a high risk of default, there is evidence that the debtor made all reasonable effort to pay under the original contractual terms and it is expected to be able to meet the revised terms. The revised terms usually include extending maturity, changing timing of interest payments and amendments to the terms of loan covenants. The credit risk associated with restructured loans is managed by the Group's Credit Risk Management units. The methods used to measure and manage risk are presented in the section of the risk and opportunity report entitled «Credit Risk». Further information is provided in the note restructured loans and advances.

Two types of allowances are in place: individual allowances and portfolio-based allowances. Allowances for loans and advances are recognised in a separate account (allowances for losses on loans and advances) instead of directly reducing the carrying amount of the assets. The expense is recognised in provisions for losses on loans and advances through profit or loss. Individual allowances on AfS financial investments as well as individual allowances and portfolio-based allowances on LaR financial assets are directly deducted from the carrying amount of the assets. The expense is recognised in net income from financial investments through profit or loss. Where subsequent measurement of financial assets is based on fair value through profit or loss, impairment is implied in the fair value.

pbb Group impairs loans and advances as well as financial investments whose terms have been renegotiated if there is objective evidence for impairment.

To measure the impairment loss, the following factors are especially considered:
> pbb Group's aggregate exposure to the customer
> the amount and timing of expected interest and redemption payments
> the realisable value of collateral and likelihood of successful repossession
> the likely deduction of any costs involved in recovering amounts outstanding
> the market price of the asset if available

For the purpose of calculating portfolio-based allowances, financial assets carried at amortised cost for which no impairment has been identified on an individual basis are grouped in portfolios according to their credit risk. This allowance covers losses which have been incurred but have not yet been identified on loans subject to individual assessment. The parameters used to determine portfolio-based allowances are checked regularly and adjusted if necessary. The portfolio-based allowances are determined after taking into account:
> historical loss experience in portfolios of similar credit risk characteristics
> a judgement whether current economic conditions and credit conditions improved or deteriorated compared to the past
> the estimated period between impairment occurring and the impairment being identified
> state of the current economic cycle

Hedge Accounting Hedging relationships between financial instruments are classified as a fair value hedge, a cash flow hedge or hedge of a net investment in a foreign operation in accordance with IAS 39. Hedging instruments are mainly interest rate derivatives, for example interest rate swaps and options. Mainly interest rate risks are hedged.

Fair Value Hedge Under IAS 39, with a fair value hedge, a recognised asset, a recognised liability, off-balance-sheet fixed obligation or a precisely designated part of such an asset, liability or obligation, is hedged against the risk of a change in fair value which is attributable to a specific risk and possibly has an effect on profit or loss for the period.

If the hedge of the fair value in the course of the reporting period meets the criteria of IAS 39.88, the hedge is accounted as follows:

> The profit or loss arising when the hedging instrument is remeasured at fair value (for a derivative hedging instrument) or the currency component of its carrying amount measured in accordance with IAS 21 (for non-derivative hedging instruments) is recognised in profit or loss for the period and
> The carrying amount of a hedged item is adjusted by the profit or loss arising from the hedged item and attributable to the hedged risks, and is recognised in profit or loss for the period. This is applicable if the hedged item is otherwise measured at cost. The profit or loss attributable to the hedged risk is recognised in profit or loss for the period if the hedged item is an available-for-sale (AfS) financial asset. The amortisation of the hedge adjustment is started on the date of the revoking of the hedge relationship.

pbb Group uses fair value hedge accounting for presenting micro-hedge relationships. Fair value hedge accounting is not used for a portfolio of interest risks. Ineffective portions within the range permitted under IAS 39 are recognised in net income from hedge relationships. For measuring effectiveness the regression analysis is used. The dollar offset method is applied for quantifying the ineffectiveness. If the hedge relationship is terminated for reasons other than the derecognition of the hedged item, the difference between the carrying amount of the hedged item at that point and the value at which it would have been carried, had the hedge never existed (the unamortised fair value adjustment), is amortised through profit or loss over the remaining term of the original hedge. If the hedged item is derecognised, e.g. due to disposal or repayment, the unamortised fair value adjustment is recognised immediately in profit or loss.

Cash Flow Hedge According to IAS 39, a cash flow hedge is a hedge of the exposure to variability in cash flows that is attributable to a particular risk associated with the recognised asset or liability (for instance some or all future interest payments on variable-interest debt) or a highly probable forecast transaction that could affect profit or loss. For instance, future variable interest payments on variable interest receivables and liabilities are swapped for fixed payments primarily by means of interest rate swaps.

Under cash flow hedge accounting, hedging instruments are measured at fair value. The measurement result has to be broken down into an effective and an ineffective portion of the hedge relationship.

The effective portion of the hedging instrument is recognised in a separate item of equity without any impact on profit or loss (cash flow hedge reserve). The inefficient portion of the hedging instrument is recognised in profit or loss in the net income from hedge relationships.

A hedging relationship is deemed to be effective if, at the beginning and throughout the entire duration of the transactions, variability in cash flows of the hedged item are compensated almost completely (range of 80% to 125%) by variability in cash flows of the hedging instruments. For the purpose of establishing whether a specific portion of the hedging instrument is effective, the future variable interest payments on the receivables and liabilities to be hedged are compared quarterly with the variable interest payments from the interest derivatives in detailed maturity bands. The dollar offset method is used to assess efficiency.

In those periods in which the cash flows of the hedged item have an impact on profit or loss for the period, the cash flow hedge reserve is released through profit or loss. If a cash flow hedge for a forecast transaction is deemed to be no longer effective, or if the hedge relationship is revoked, the cumulative gains or losses on the hedging derivative initially recognised in equity remain in equity until the committed or forecast transaction occurs. At this point, the gains or losses have to be recognised in profit or loss. pbb Group uses a macro approach for cash flow hedge accounting.

Hedge of a Net Investment in a Foreign Operation A net investment hedge is a hedge of the foreign currency exposure on a net investment in a foreign operation. Hedges of net investments in foreign operations are accounted for similarly to cash flow hedges. pbb Group did not hedge a net investment in a foreign operation in the financial years 2013 and 2012.

7 Cash Reserve

Cash reserve contains balances with central banks which are measured at cost.

8 Trading Assets

Trading assets comprise positive market values of stand-alone derivatives of the bank book. Trading assets are measured at fair value. Unrealised and realised gains and losses attributable to trading assets are recognised in net trading income in profit or loss.

9 Loans and Advances

Loans and advances to other banks and loans and advances to customers are measured in accordance with IAS 39 at amortised cost if they are not categorised dFVTPL or AfS or a hedged item of a fair value hedge. As of 31 December 2013, and as of 31 December 2012, pbb Group did not have loans and advances which are classified as AfS or dFVTPL.

Additions to allowances for losses on loans and advances are disclosed as a separate item provisions for losses in profit or loss. Value changes from hedge relationships are recognised under net income from hedge relationships. All other income and expenses from loans and advances, including net gains and net losses, are recognised in net interest income and similar income.

10 Allowances for Losses on Loans and Advances and Provisions for Contingent Liabilities and Other Commitments (Risk Provisions)

Allowances for losses on loans and advances are recognised if there is objective evidence that it will not be possible for the entire amount which is due in accordance with the original contractual conditions to be recovered. Allowances for loans and advances are measured mainly on the basis of expectations with regard to loan defaults, the structure and quality of the loan portfolio as well as macroeconomic parameters on an individual and portfolio basis.

Individual Allowances For all recognisable default risks, the extent of the allowance for losses on loans and advances is calculated as the difference between the carrying amount of the asset and the present value of the expected future cash flows. The latter is calculated on the basis of the initial effective interest rate. Market interest rate changes do not have any effect in this respect. The increase in the present value of an adjusted receivable (so-called unwinding) which occurs over a period of time is recognised as an interest income.

Portfolio-based Allowances Under IAS 39.64, loans which were not individually impaired are pooled in risk-inherent portfolios. Portfolio-based allowances are recognised for these portfolios; these allowances are measured in respect of current events and information with regard to significant changes with detrimental consequences which have occurred in the technology, market, economic or legal environment, as well as historical default rates.

Allowances for losses on loans and advances are broken down into allowances relating to loans and advances and provisions for contingent liabilities and other commitments like irrevocable loan commitments. An allowance relating to loans and advances is disclosed as a negative item on the assets side of the statement of financial position, whereas a provision for contingent liabilities and other commitments is disclosed on the liabilities side of the statement of financial position. In profit or loss, all effects are disclosed as provisions for losses on loans and advances apart from time-related increases in the present value of impaired receivables which are disclosed in net interest income and similar income.

11 Financial Investments

dFVTPL, LaR and AfS securities are recognised and disclosed as financial investments. dFVTPL and AfS financial assets are measured at fair value. Changes in the fair value are through profit or loss in case of dFVTPL financial assets in economical hedge relationships and are recognised in net income from hedge relationships and disclosed in the net income from hedge relationships. Changes in fair value of AfS financial assets are disclosed as a separate item of equity (AfS reserve) not affecting profit or loss until the asset is sold, withdrawn, disposed of, or if an impairment is established for the financial asset in accordance with IAS 39.58 et seq. Therefore, the cumulative profit or loss previously recognised in equity is now affecting profit or loss. Individual allowances on AfS financial assets are directly deducted from the carrying amount of the assets. Portfolio-based allowances on AfS financial assets shall not be created for AfS financial assets. AfS financial assets which are hedged effectively against market price risks are part of the hedge accounting. LaR financial investments are measured at amortised cost. Individual allowances and portfolio-based allowances on LaR financial investments are directly deducted from the carrying amount of the assets. In the financial years 2013 and 2012, pbb Group did not have any HtM financial assets.

12 Property, Plant and Equipment

Property, plant and equipment are generally measured at cost of purchase or cost of production. The carrying amounts of tangible assets (except land) are depreciated on a straight-line basis in accordance with the expected useful lives of the assets. In addition, property, plant and equipment are tested at least annually for impairment. If the value of property, plant and equipment has impaired, an impairment loss is recognised in profit or loss. If the reasons for the impairment no longer exist, an amount not exceeding amortised cost is reversed through profit or loss. In the case of fittings in rented buildings, the contract duration taking account of extension options is used as the basis of this contract duration if it is shorter than the useful life.

Useful lives

in years	
Fixture in rental buildings	5–15
IT equipment (broad sense)	3–5
Other plant and operating equipment	3–25

Subsequent cost of purchase or costs of conversion are capitalised if an additional economic benefit flows to the Company. Maintenance expenses of property, plant and equipment are recognised in profit or loss of the financial year in which they arose.

13 Intangible Assets

Purchased and internally generated software are the main items recognised as intangible assets. Goodwill, brand names and customer relations are not activated.

Software is an intangible asset with a finite useful life. Purchased software is measured at amortised cost. pbb Group capitalises internally generated software if it is probable that future economic benefits will flow to the Group and the expenses can be measured reliably. Expenses eligible for capitalisation include external directly attributable costs of materials and services as well as personnel expenses for employees directly associated with an internally generated software project. Software is amortised on a straight-line basis over expected useful lives of three to five years. In addition, intangible assets with a finite useful life have to be tested for impairment annually or whenever there is an indication that the intangible asset may be impaired.

14 Other Assets

Other assets mainly comprise positive fair values from derivative financial instruments (hedging derivatives) and salvage acquisitions. Salvage acquisitions are measured as inventories according to IAS 2 at the lower of cost of purchase and net realisable value.

15 Liabilities

Liabilities other than hedged items of an effective fair value hedge and which are not classified as dFVTPL are measured at amortised cost. Premiums and discounts are recognised on a pro rata basis. Interest-free liabilities are recognised with their present value. pbb Group has not designated any liabilities into the category dFVTPL. Changes in value resulting from hedge relationships are disclosed under net income from hedge relationships. All income and expenses from liabilities including net gains and net losses resulting from redemption of liabilities are recognised in net interest income and similar income.

16 Trading Liabilities

Trading liabilities include negative market values of trading derivatives and of stand-alone derivatives of the bank book. Trading liabilities are measured at fair value. Unrealised and realised profits and losses attributable to trading liabilities are recognised in net trading income through profit or loss.

17 Provisions

Under IAS 37.36 et seq., the best estimate is used for measuring provisions for contingent liabilities and contingent losses attributable to pending transactions. Long-term provisions are generally discounted with an interest rate that reflects the current assessments of the time value of money and the risks specific to the liability.

Provisions for defined benefit plan provisions are calculated on the basis of actuarial reports in accordance with IAS 19. They are measured using the projected unit credit method. The amount of the provision equals the so-called net defined benefit liability which is the difference between the present value of the defined benefit obligation and the fair value of plan assets. pbb closed plan assets in the form of a qualifying insurance policy to hedge parts of the risk from the defined benefit obligations. The reinsurance is pledged to the plan beneficiaries.

The determination of the net defined benefit liability is based on demographic and financial actuarial assumptions. A demographic assumption is for example the mortality for which pbb uses guidance tables. In financial actuarial assumptions the discount rate has the greatest effect on the amount of defined benefit liability. The rate used for the measurement is determined by reference to market yields at the end of the reporting period on high-quality corporate bonds.

Net interest on the defined benefit liability is determined by multiplying the defined benefit liability by the discount rate. The determination is done at the start of the annual reporting period taking account of any changes in the net defined benefit liability during the period as a result of contribution and benefit payments. Net interest on defined benefit liability are shown together with all other effects on income statement from the defined benefit obligations and the plan assets in the position pension expenses and related employee benefit costs in general administrative expenses.

Remeasurements of the net defined benefit liability result from actuarial gains and losses and the return on plan assets excluding amounts included in net interest on the net defined benefit liability. Remeasurements of the net defined benefit liability are shown in equity in the position profit/losses from pension obligations. Changes of remeasurements of the net defined benefit liability within a period are shown as a component of the consolidated statement of comprehensive income. Actuarial gains and losses result from increases or decreases in the present value of the defined benefit obligation due to changes of actuarial assumptions and experience adjustments. Changes of the discount rate usually have the biggest effect on the actuarial gains and losses.

18 Other Liabilities

Besides negative fair values from derivative financial instruments (hedging derivatives and derivatives hedging dFVTPL financial instruments), accruals are one of the items recognised in other liabilities. Accruals arose from liabilities for products or services which have been received or supplied and have not yet been paid for, invoiced by the supplier or formally agreed. This also includes short-term liabilities to employees, for instance flexitime credits and vacation entitlements. The accruals are measured at the amount likely to be utilised.

If the obligations listed at this note cannot be quantified more precisely on the balance sheet date and if the criteria specified in IAS 37 for recognising provisions are satisfied, these items have to be disclosed as provisions.

19 Subordinated Capital

In the event of insolvency or liquidation subordinated capital may only be repaid after all non-subordinated creditors have been satisfied. Subordinated capital of pbb Group encompasses subordinated liabilities, participating certificates outstanding and hybrid capital instruments. For some instruments of subordinated capital the holders participate in any net loss or consolidated loss. In addition, the interest entitlement can be ceased or reduced under specific conditions. For other instruments the interest ceases only in case of a net loss which can be caught up depending on the structuring.

Pursuant to IAS 32 the subordinated capital instruments issued by companies of pbb Group were classified as financial liabilities or equity instruments in accordance with the substance of the contractual arrangement and the definitions of a financial liability and an equity instrument. Financial liabilities are measured at amortised cost. The amortised costs are the amount at which the financial liability is measured at initial recognition minus principal payments, plus or minus the cumulative amortisation using the effective interest rate method of any difference between that initial amount and the maturity amount and minus any expected reduction of interest and/or principal payments.

20 Silent Participation

Finanzmarktstabilisierungsfonds-FMS provided pbb with a silent participation of € 1.0 billion deducted by transaction costs in 2009. The silent participation has an indefinite life. The silent shareholder participates in a cumulative loss to the extent of its silent deposit expressed as a percentage of the total carrying amount of all liability capital shares of the Bank which participate in a cumulative loss. The extent to which the silent shareholder participates in the cumulative loss is limited to its silent deposit. The cumulative loss attributable to the year 2008 is not taken into consideration for calculating the participation in the loss. The silent participation is classified as an equity instrument on initial recognition in accordance with the substance of the contractual arrangement and the definitions in IAS 32. The silent participation is measured initially at cost, with such cost being equivalent to the fair value of the consideration received.

21 Share-based Compensation

As of 31 December 2013 and as of 31 December 2012 no company of pbb Group has provided a commitment for share-based compensation.

22 Currency Translation

Currency translation is carried out in accordance with the regulations of IAS 21. On the balance sheet date, monetary items in a foreign currency are translated into the functional currency. The reporting currency is the euro. Non-monetary items which were stated in a foreign currency using historical cost of purchase are measured using the exchange rate applicable at date of purchase.

Income and expenses attributable to currency translation of the affiliated companies' single financial statements into the functional currency are generally recognised in profit or loss in balance of other operating income/expenses.

In this consolidated financial statement, balance sheet items of the subsidiaries, if they do not prepare financial statements in euros, are translated using the closing rates at the balance sheet date. For translating the expenses and income of these subsidiaries, the average rates are used. Differences resulting from the translation of the financial statements of the subsidiaries do not affect profit or loss and are disclosed in the statement of changes in equity. The group of consolidated companies does not include any companies from hyperinflationary countries.

23 Taxes on Income

Taxes on income are recognised and measured in accordance with IAS 12. Apart from the exceptions defined in the standard, deferred taxes are calculated for all temporary differences for the IFRS values and the tax base as well as for the differences resulting from uniform Group measurement principles and differences from the consolidation (balance sheet method). Deferred tax assets arising from non-utilised losses carried forward, interest assets carried forward and tax credits are recognised if required from IAS 12.34 et seq.

Deferred taxes are measured using the national tax rates which are expected at the time when the differences are balanced, as the concept of deferred taxes is based on the presentation of future tax assets or tax liabilities (liability method). Changes of tax rates have been taken into account. The pay-out of the corporate income tax claim which was capitalised on 31 December 2006 has begun since 1 January 2008 over a period of ten years independently of a dividend payment. The interest-free claim had to be shown with the present value. An unchanged rate of 3.7% p.a. has been used for discounting purposes.

24 Non-current Assets Held for Sale

In accordance with IFRS 5, non-current assets held for sale or disposal group have to be measured on the balance sheet date at the lower of carrying amount and fair value less costs to sell. The assets have to be disclosed separately in the statement of financial position. As at 31 December 2013 and at 31 December 2012 pbb Group did not own non-current assets held for sale.

25 Accounting Estimates and Assumptions

When the financial statements are being prepared, pbb Group makes future-related assumptions as well as estimations, resulting in a considerable risk of a major change to the disclosed assets and liabilities becoming necessary during the next financial year. The assumptions and parameters underlying the estimates to be made are based on the exercise of appropriate judgement.

Going Concern The consolidated financial statements of pbb are based on the assumption of going concern. The conditions of going concern are described in the report on expected developments.

Allowances The portfolio of pbb Group is reviewed at least annually in order to identify any impairment losses on loans and advances. It is necessary to assess whether the estimated future cash flows of a loan portfolio are lower than the actual contractual ones. For this purpose, it is necessary to make judgements as to whether there is any observable data indicating that there is a measurable decrease in the estimated future cash flows. This evidence may include observable data indicating that there has been an adverse change in the payment status of borrowers, or national or economic conditions that correlate with defaults on assets in the portfolio. The methods and assumptions concerning the assessments of the extent and timing of the payment streams are reviewed regularly to reduce any differences between estimated and actual defaults. In addition, the determination of portfolio-based provisions is based on a loss identification period as well as the expected loss based on statistical data.

Fair Values of Original and Derivative Financial Instruments The fair value of financial instruments that are not listed on active markets is measured using valuation models. In the cases in which valuation models are used, a check is performed regularly to assess whether the valuation models provide a comparable standard for current market prices. For practical considerations, the valuation models can only take account of quantifiable factors (e.g. cash flows and discount rates) that also require estimates. Changes in assumptions relating to these factors might have an impact on the fair values of the financial instruments. In accordance with IAS 8.34, accounting estimates must be revised if changes occur in the circumstances on which the estimate was based or as a result of new information or experience gained. In the reporting period, pbb Group revised the credit value adjustment (CVA) estimates used to measure derivatives. As a result, market-based parameters are used to calculate credit risk for pbb Group and for counterparties that do not have specific credit default swaps (CDS). The accounting estimate changes led to income of €3 million, which was recognised in net trading income. In addition, overnight yield curves (including tenor basis effects) were used to measure derivatives for the first time as of 31 December 2013 due to changes in market conventions. This resulted in a transition effect of €–33 million, which was recognised in the income statement under net trading income, and an effect of €–4 million that was recognised in equity (other comprehensive income) under the cash flow hedge reserve.

Embedded Derivatives According to IAS 39.11, an embedded derivative has to be separated from the host contract and has to be measured separately if, in addition to other criteria, the economic characteristics and risks of the embedded derivative are not closely related to the economic characteristics and risks of the host contract. The economic risks of the host contracts and embedded derivatives are assessed on the basis of measuring methods to evaluate the existence of an obligation to separate.

Hedge Accounting Relations between hedged items and hedging instruments can be presented in hedge accounting. A relation only qualifies for hedge accounting when certain conditions specified under IAS 39.88 are satisfied. One of these conditions is that the hedge has to be very efficient with regard to achieving compensation for the risks resulting from changes in the fair value or the cash flow in relation to the hedged risk.

The determination of the effectiveness of the risk hedge depends on risk measuring methods, the parameters which are used and assumptions relating to the probability of occurrence. These methods and parameters are continuously developed in line with the risk management objectives and strategies.

Intangible Assets and Property, Plant and Equipment pbb Group's accounting for intangible assets and property, plant and equipment is subject to estimating uncertainty, particularly in the determination of the useful life of assets and the associated amount of depreciation/amortisation recognised per period.

Provisions Estimates are used in the measurement of provisions at pbb Group. Estimating uncertainty arises in particular during assessment of the amount of the future cash outflows, the time horizon and the discount rate.

Taxes on Income pbb Group is subject to a wide range of national tax regulations with regard to the calculation of taxes on income. In order to measure the tax expenses, it is necessary to make estimates that are calculated with the knowledge existing as of the balance sheet date and closely related to the tax return prepared in the following financial year. In some countries, the current tax charges attributable to the current financial year can only be definitely finalised after the corresponding tax audit has been completed. The variances with regard to the estimated tax burden may have a positive or negative influence on the tax burden in future financial years.

With regard to the capitalisation of losses carried forward and other tax credits, the extent as well as the availability of such tax benefits are subject to estimation. Major losses carried forward are subject to national German tax law, and their availability also depends on the restrictions set out in section 10 d EStG, 8 c KStG as well as section 10 a GewStG. Deferred tax assets arising from losses carried forward are recognised as far as it is likely that taxable income will be available to offset the non-utilised tax losses carried forward.

Segment Reporting

26 Notes to Segment Reporting by Operating Segment

pbb Group operates in the three operating segments Real Estate Finance, Public Sector Finance and Value Portfolio, which are used as the basis for managing the Group.

The presentation of the segments of pbb Group is based on internal reporting which is prepared in accordance with IFRS. Income and expenses are allocated to the segments in line with the principle of causation. The external net interest income of the Group is calculatively allocated to the segments.

Real Estate Finance (REF) The REF operating segment comprises all real estate financing arrangements of the Group. New business focuses on financing existing properties with a conservative refinancing strategy. The customers are professional investors. Adequate batch sizes and loan-to-values commensurate for the level of risk involved are essential for independent operations. Strategic partnerships are agreed with other institutions with the aim of permitting higher loan-to-values and larger volumes for customers by means of syndications and syndicated financing arrangements.

Public Sector Finance (PSF) The PSF operating segment comprises the financing arrangements for the public sector which are eligible as cover funds in accordance with German law. pbb Group will generate new business in public investment finance. No new business will be realised by pbb Group in public sector finance as pure budget financing. Concentrating on public investment finance is the aim. The target group for these activities are profitable customer segments with a commensurate risk level: regions, cities and municipalities as well as state-guaranteed public corporations and guaranteed public-private partnerships.

Value Portfolio (VP) The VP operating segment mainly presents income and expenses from services of pbb Group to ongoing operation of FMS Wertmanagement as well as for IT services to its sister company DEPFA. Furthermore, the segment comprises non-strategic portfolios, e.g. selected structured products.

Consolidation & Adjustments is used for reconciling the sum of operating segments results with the consolidated result. The column includes equity which is not allocated to the operating segments.

27 Income Statement by Operating Segment

Income/expenses in € million		REF	PSF	VP	Consolidation & Adjustments	**pbb Group**
Operating revenues	2013	334	28	102	18	482
	2012	264	47	147	9	467
Net interest income and similar income	2013	240	62	–	17	319
	2012	227	58	1	10	296
Net commission income	2013	10	–	–	–1	9
	2012	25	–1	–1	–	23
Net trading income	2013	–21	–30	–	–	–51
	2012	2	8	–	–	10
Net income from financial investments	2013	96	–	–	–	96
	2012	16	–2	–1	–	13
Net income from hedge relationships	2013	4	5	–	–	9
	2012	–3	–3	–	–	–6
Balance of other operating income/expenses	2013	5	–9	102	2	100
	2012	–3	–13	148	–1	131
Provisions for losses on loans and advances	2013	–1	–7	–	–	–8
	2012	5	–4	3	–	4
General administrative expenses	2013	–147	–54	–111	–	–312
	2012	–139	–53	–148	–1	–341
Balance of other income/expenses	2013	2	1	–	–	3
	2012	–3	–1	–2	–	–6
Pre-tax profit	2013	**188**	**–32**	**–9**	**18**	**165**
	2012	**127**	**–11**	**–**	**8**	**124**

Cost-income ratio[1] in %		REF	PSF	VP	**pbb Group**
Cost-income ratio (based on operating revenues)	2013	44.0	>100.0	>100.0	64.7
	2012	52.7	>100.0	>100.0	73.0

[1] The cost-income ratio is the ratio of general administrative expenses and operating revenues

28 Balance-sheet-related Measures by Operating Segment

The Management Board controls balance-sheet-related measures by operating segments based on equity, risk-weighted assets and on financing volumes. Financing volumes are the notional amounts of the drawn parts of granted loans and parts of the securities portfolio.

Balance-sheet-related measures by operating segment

in € billion		REF	PSF	VP	Consolidation & Adjustments	**pbb Group**
Equity[1]	31.12.2013	0.8	1.6	–	1.0	3.4
	31.12.2012	1.0	1.4	–	0.8	3.2
Risk-weighted assets[2]	31.12.2013	8.1	5.4	0.1	0.5	14.1
	31.12.2012	9.6	5.0	0.2	0.5	15.3
Financing volumes	31.12.2013	20.4	30.0	0.8	–	51.2
	31.12.2012	22.1	35.4	0.9	–	58.4

[1] Excluding revaluation reserve

[2] Including risk-weighted credit risk positions as well as the capital requirements for market risk positions and operational risks scaled with the factor 12.5; according to Basel II advanced IRB approach for authorised portfolios, otherwise Basel II standardised approach; pro forma as per prepared annual financial statements and after result distribution

29 Breakdown of Operating Revenues

Operating Revenues by Products Operating revenues from other products mainly contained a balance of other operating income/expenses for the on 30 September 2013 mostly discontinuated servicing for the ongoing operation of FMS Wertmanagement and for IT services to the sister company DEPFA totalling €96 million (2012: €146 million).

Operating revenues by products

in € million		Commercial real estate financing	Public sector financing	Other products	**pbb Group**
Operating revenues	2013	334	28	120	**482**
	2012	264	47	156	**467**

Operating Revenues by Regions pbb Group differentiates between the regions Germany, Rest of Europe and America/Asia. Allocation of values to regions is based on the location of the registered offices of the Group companies or their branches.

Operating revenues by regions

in € million		Germany	Rest of Europe	America/Asia	**pbb Group**
Operating revenues	2013	326	53	103	**482**
	2012	473	17	−23	**467**

Operating Revenues by Customers A balance of other operating income/expenses of €60 million (2012: €106 million) recognised in the Value Portfolio segment resulted from services for the ongoing operation of FMS Wertmanagement. The service provided for the FMS Wertmanagement discontinuated to a large extend as mandated by the European Commission an 30 September 2013. Because this position accounted for more than 10% of all operating revenues of pbb Group, FMS Wertmanagement was a major client in accordance with IFRS 8.34. The balance of other operating income/expenses compensated for the expenses additional profit margin of the pbb Group incurred in connection with servicing.

Notes to the Consolidated Income Statement

30 Net Interest Income and Similar Income

Net interest income and similar income by categories of income/expenses in € million	2013	2012
Interest income and similar income	**2,448**	**2,879**
Lending and money-market business	1,302	1,557
Fixed-income securities and government-inscribed debt	785	869
Investments	–	2
Current result from swap transactions (balance of interest income and interest expenses)	361	451
Interest expenses and similar expenses	**−2,129**	**−2,583**
Liabilities to other banks and customers	−487	−604
Liabilities evidenced by certificates	−1,570	−1,884
Subordinated capital	−72	−95
Total	**319**	**296**

Total interest income for financial assets that are measured at amortised cost, amount to € 2.1 billion (2012: € 2.4 billion). Total interest expenses for financial liabilities that are not measured at fair value through profit or loss amount to €−2.1 billion (2012: €−2.6 billion).

31 Net Commission Income

Net commission income in € million	2013	2012
Securities and custodial services	−1	−2
Lending operations and other service operations	10	25
Total	**9**	**23**

Net commission income is attributable exclusively to financial assets and financial liabilities which are not designated at fair value through profit or loss.

32 Net Trading Income

Net trading income in € million	2013	2012
From interest rate instruments and related derivatives	−51	8
From credit risk instruments and related derivatives	–	2
Total	**−51**	**10**

33 Net Income From Financial Investments

Net income from financial investments in € million	2013	2012
Income from financial investments	101	22
Expenses from financial investments	–5	–9
Total	**96**	**13**

Net income from financial investments consists of income from the sale of securities of the measurement categories AfS and LaR together with changes in the value of such instruments that are to be recognised in profit or loss. HtM investments were not held in 2013 and 2012. Based on measurement categories, net income from financial investments is broken down as follows:

Net income from financial investments by IAS 39 categories in € million	2013	2012
AfS financial investments	4	14
LaR financial investments	–2	–1
Total	**2**	**13**

Net income from financial investments not accounting for IAS 39 amounted to €94 million. Attributable to the disposal of Little Britain Holdings (Jersey) Ltd. was a result of €92 million.

34 Net Income from Hedge Relationships

Net income from hedge relationships in € million	2013	2012
Result from fair value hedge accounting	8	–6
Result from hedged items	–344	–450
Result from hedging instruments	352	444
Result from dFVTPL investments and related derivatives	–	2
Result from dFVTPL investments	–1	–
Result from derivatives related to dFVTPL investments	1	2
Ineffectiveness from cash flow hedge accounting affecting income	1	–2
Total	**9**	**–6**

35 Balance of Other Operating Income/Expenses

Balance of other operating income/expenses in € million	2013	2012
Other operating income	245	277
Other operating expenses	–145	–146
Balance of other operating income/expenses	**100**	**131**

The balance of other operating income/expenses from services for the ongoing operation of FMS Wertmanagement amounted to €60 million (2012: €106 million). The services provided to FMS Wertmanagement were largely discontinued on 30 September 2013 as mandated by the European Commission, which meant that the volume of necessary services has declined accordingly. General administrative expenses declined simultaneously. Income from IT services to fellow subsidiary DEPFA amounted to €36 million (2012: €40 million). In the financial year 2013, the bank levy resulted in expenses of €–11 million (2012: €–24 million). An income of €11 million (2012: €7 million) was attributable to rental income generated from taken over real estate. Net income resulting from foreign currency translation amounted to less than €1 million (2012: net income of €3 million).

36 Provisions for Losses on Loans and Advances

Provisions for losses on loans and advances in € million	2013	2012
Provisions for losses on loans and advances	–17	–1
Additions	–66	–66
Reversals	49	65
Provisions for contingent liabilities and other commitments	1	4
Additions	–	–4
Reversals	1	8
Recoveries from written-off loans and advances	8	1
Total	**–8**	**4**

The development of individual allowances on loans and advances as well as portfolio-based allowances is disclosed in the note «Allowances for Losses on Loans and Advances».

37 General Administrative Expenses

General administrative expenses in € million	2013	2012
Personnel expenses	–121	–131
Wages and salaries	–94	–104
Social security costs	–18	–19
Pension expenses and related employee benefit costs	–9	–8
Non-personnel expenses	–191	–210
Other general administrative expenses	–177	–197
Consulting expenses	–40	–57
IT expenses	–91	–102
Office and operating expenses	–14	–14
Other administrative expenses	–32	–24
Depreciation/amortisation	–14	–13
On software and other intangible assets excluding goodwill	–13	–12
On property, plant and equipment	–1	–1
Total	**–312**	**–341**

Cost-income ratio in %	2013	2012
Cost-income ratio	64.7	73.0

38 Balance of Other Income/Expenses

Balance of other income/expenses in € million	2013	2012
Other income	11	5
thereof: Reversals of restructuring provisions	11	5
Other expenses	–8	–11
thereof: Additions to restructuring provisions	–4	–11
Other taxes	–4	–
Balance of other income/expenses	**3**	**–6**

39 Taxes on Income

Breakdown in € million	**2013**	**2012**
Current taxes	2	8
Deferred taxes	−7	−63
thereof: Deferred taxes on capitalised losses carried forward	80	−7
Total	**−5**	**−55**

Current taxes contain tax income for prior years of €6 million (2012: €20 million).

The following overview shows the development of the deferred taxes recognised in the financial statements.

Development of deferred taxes in € million	**2013**	**2012**[1]
Deferred taxes recognised in the statement of financial position	−5	17
Difference to prior year	−22	−115
thereof: Recognised in income statement	−7	−63
Recognised in profits/losses from pension commitments	−2	14
Recognised in AfS reserve	−56	−71
Recognised in cash flow hedge reserve	43	5

[1] Adjusted due to retrospective IAS 19 (revised) first time adoption. Details are disclosed in Note «Principles»

Reconciliation in € million	**2013**	**2012**
Net income/loss before taxes	165	124
Applicable (legal) tax rate in %	15.83	15.83
Expected (computed) tax expense	−26	−20
Tax effects		
arising from foreign income	−1	–
arising from tax rate differences	10	−26
arising from tax-free income	–	1
arising from deductible and non-deductible items	−10	−15
arising from valuation adjustments and non-application of deferred taxes	23	−7
arising from prior years	−1	12
Reported taxes on income	**−5**	**−55**
Group tax ratio in %	**3.03**	**44.35**

The tax rate applicable for the financial year, including solidarity surcharge, is 15.83% and is comprised of the 15.0% German corporate tax rate currently valid together with the payable solidarity surcharge of 5.5%.

The effects attributable to foreign income comprise tax rate differences arising from foreign fiscal jurisdictions. These arose as foreign income has been taxed with different tax rates.

The effects from tax rate differences include the trade tax burden (current and deferred in accordance with IFRS) which exists in Germany additionally to German corporation tax and solidarity surcharge.

The item effects arising from tax-free income comprises effects from tax-free income from participating interests and dividends both domestically and internationally. Regulations for the determination of taxable income were applied as valid for the particular jurisdiction.

The effects attributable to tax additions and deductions relate primarily to non-deductible expenses, which do not have to be taken into account as deferred taxes as a result of permanent differences, but which have reduced or increased the basis of taxation.

The item effects arising from valuation adjustments and non-application of deferred taxes comprises major effects from not recognised deferred tax assets at periodical losses. pbb Group recognised no impairments on deferred tax assets which have been recorded last year on the basis of existing losses carried forward.

The item effects from previous years includes both current taxes for years which have been incurred as a result of tax audits or a reassessment of the tax liability, as well as deferred taxes for prior years.

The Group tax ratio is the quotient of the stated income taxes (current and deferred taxes) and net income/loss before taxes.

The deferred tax liabilities or deferred tax assets relate to the following items:

Deferred tax liabilities/assets in € million	**2013**	**2012**[1]
Loans and advances to other banks/customers (including loan loss allowances)	22	27
Financial investments	11	13
Trading assets	384	536
Other assets/liabilities	696	1,041
Others	13	17
Deferred tax liabilities	**1,126**	**1,634**
Loans and advances to other banks/customers (including loan loss allowances)	9	9
Financial investments	88	144
Provisions	38	69
Other assets/liabilities	483	820
Trading liabilities	284	472
Liabilities evidenced by certificates	5	3
Losses carried forward	214	134
Deferred tax assets	**1,121**	**1,651**

[1] Adjusted due to retrospective IAS 19 (revised) first time adoption. Details are disclosed in Note «Principles»

For the domestic companies, the deferred taxes are calculated using the uniform rate of corporation tax of 15.0% plus the 5.5% solidarity surcharge payable on this and the locally applicable collection rate for municipal trade tax (the current basic rate is 3.5%). For pbb the tax rate for the valuation of deferred taxes is 27.80% (2012: 28.00%).

On the reporting date, there are unused losses carried forward totalling €3,781 million (2012: €3,649 million) at corporate tax level and €3,844 million (2012: €3,747 million) at trade tax level. Deferred tax assets have been stated as €738 million (2012: €447 million) at corporate tax level and €810 million (2012: €519 million) at trade tax level, because the criteria for recognition in accordance with IAS12.34 et seq. were satisfied. The loss carried forward can be utilised for an unlimited period of time. Additionally temporary differences of €1 million (2012: €3 million) were not recognised with deferred tax assets.

From the origination and reversal of temporary differences a deferred tax expense arose of €–86 million (2012: €–56 million).

No deferred tax income resulted from tax rate changes (2012: €1 million).

As in the previous year the current tax expense was not reduced by the use of previously unrecognised tax losses. Deferred tax income of € 39 million resulted from capitalisation not yet recognised losses carried forward.

On differences associated with investments in subsidiaries, deferred tax liabilities in the amount of €140 million (2012: €173 million) has not been stated because it is the ability and the intention to invest profits permanently in these subsidiaries.

40 Net Gains/Net Losses

The income statement contains the following net gains/net losses recognised in profit or loss according to IFRS 7.20(a):

Net gains/net losses in € million	2013	2012
Loans and receivables	16	10
Available for sale	4	14
Held for trading	–51	10
Designated at fair value through profit or loss	–1	–
Financial liabilities at amortised cost	–	6

Notes to the Consolidated Statement of Financial Position (Assets)

41 Cash Reserve

Cash reserve in € million	31.12.2013	31.12.2012
Balance with central banks	3,532	1,937
Total	**3,532**	**1,937**

Cash in hand as of 31 December 2013 amounts to less than € 1 million as was the case in the previous year.

42 Trading Assets

Trading assets in € million	31.12.2013	31.12.2012
Positive fair values of derivative financial instruments	1,642	3,325
Total	**1,642**	**3,325**

43 Loans and Advances to Other Banks

Loans and advances to other banks by type of business in € million	31.12.2013	31.12.2012
Loans and advances	3,744	5,092
Public sector loans	1,978	2,231
Real estate loans	51	52
Other loans and advances	1,715	2,809
Investments	2,054	2,903
Total	**5,798**	**7,995**

Loans and advances to other banks by maturities in € million	31.12.2013	31.12.2012
Repayable on demand	1,648	2,736
With agreed maturities	4,150	5,259
up to 3 months	2,138	3,016
3 months to 1 year	381	222
1 year to 5 years	646	891
5 years and over	985	1,130
Total	**5,798**	**7,995**

44 Loans and Advances to Customers

Loans and advances to customers by type of business in € million	31.12.2013	31.12.2012
Loans and advances	36,042	49,090
Public sector loans	15,464	19,139
Real estate loans	20,557	29,919
Other loans and advances	21	32
Investments	200	500
Total	**36,242**	**49,590**

Loans and advances to customers by maturities in € million	31.12.2013	31.12.2012
With agreed maturities	36,242	49,590
up to 3 months	2,087	4,008
3 months to 1 year	2,937	4,973
1 year to 5 years	15,122	21,595
5 years and over	16,096	19,014
Total	**36,242**	**49,590**

45 Allowances for Losses on Loans and Advances

Breakdown in € million	31.12.2013	31.12.2012
Specific allowances for losses on loans and advances to other banks	–	–
Specific allowances for losses on loans and advances to customers	–97	–283
Portfolio-based allowances	–51	–42
Total	**–148**	**–325**

Development in € million	Specific allowances	Portfolio-based allowances	Total
Balance at 1.1.2012	**–413**	**–64**	**–477**
Changes affecting income	–15	22	7
Gross additions	–48	–18	–66
Reversals	25	40	65
Increase of the present value due to passage of time (unwinding)	8	–	8
Changes not affecting income	145	–	145
Use of existing loan-loss allowances	145	–	145
Balance at 31.12.2012	**–283**	**–42**	**–325**
Balance at 1.1.2013	**–283**	**–42**	**–325**
Changes affecting income	1	–9	–8
Gross additions	–50	–16	–66
Reversals	42	7	49
Increase of the present value due to passage of time (unwinding)	9	–	9
Changes not affecting income	185	–	185
Use of existing loan-loss allowances	185	–	185
Balance at 31.12.2013	**–97**	**–51**	**–148**

The allowances for losses on loans and advances were exclusively created for the measurement category loans and receivables.

46 Financial Investments

Breakdown in € million	31.12.2013	31.12.2012
AfS financial investments	4,284	3,920
Shares in non-consolidated subsidiaries	–	1
Debt securities and other fixed-income securities	4,282	3,917
Equity securities and other variable-yield securities	2	2
dFVTPL financial investments	–	83
Debt securities and other fixed-income securities	–	83
LaR financial investments	16,608	21,569
Debt securities and other fixed-income securities	16,608	21,569
Total	**20,892**	**25,572**

The carrying amounts of the LaR financial investments were reduced by portfolio-based allowances amounting to €–14 million (2012: €–12 million).

pbb Group cannot determine reliably a fair value for some shares in companies for which there is no market value available and which are not fully consolidated or are not accounted for using the equity method due to considerations of materiality or due to a missing control respectively a missing significant influence. These companies in the legal form of limited or private are not traded in an active market and therefore are measured at cost. The carrying amount of these financial investments amounted to €0 million as of 31 December 2013 (2012: €1 million). In financial year 2013, financial investments, for which it is not possible for the fair value to be reliably established, were derecognised for €1 million (2012: €1 million). As in the previous year no profit was recognised.

Financial investments by maturities in € million	31.12.2013	31.12.2012
Unspecified terms	2	3
With agreed maturities	20,890	25,569
Up to 3 months	767	3,131
From 3 months to 1 year	1,567	1,507
From 1 year to 5 years	7,671	8,121
From 5 years and over	10,885	12,810
Total	**20,892**	**25,572**

pbb Group has made use of the IASB amendments to IAS 39 and IFRS 7, published on 13 October 2008, and reclassified financial assets. pbb Group identified assets, eligible under the amendments, for which at the reclassification date it had a clear change of intent to hold for the foreseeable future rather than to exit or trade in the short term and which had met the definition of loans and receivables according to IAS 39 (amongst others not quoted in an active market). The reclassified portfolios are disclosed under financial investments.

pbb Group reclassified retrospectively as of 1 July 2008 financial investments out of the category available-for-sale of €30.2 billion.

At the date of reclassification the effective interest rate for the AfS assets was between 0.25% and 34.4%.

Since the date of reclassification, financial assets with a (reclassified) carrying amount of around € 10.3 billion (2012: € 9.5 billion) became due.

In the financial year 2013 no reclassified securities (2012: € 0.1 billion) were sold. Therefore no net profit or loss was realised (2012: net profit of € 6 million).

The reclassification of AfS assets did not cause a disclosure change of current interest income. Interest income is still shown under net interest income and similar income.

The following tables summarise the carrying amounts and fair values as of 31 December 2013 and 31 December 2012 as well as fair value gains and losses that would have been recognised in 2013 and 2012 if the financial assets had not been reclassified.

Reclassifications in 2008 **Effects in 2013**	into: Financial investments loans and receivables (LaR)			Effect in reporting period if no assets had been reclassified (1.1.–31.12.2013)	
			31.12.2013		
	Date	Carrying amount in € billion	Fair value in € billion	Income statement in € million	AfS reserve (after taxes) in € million
from: Financial investments available for sale (AfS)	1.7.2008	9.5	9.4	–	226

Reclassifications in 2008 **Effects in 2012**	into: Financial investments loans and receivables (LaR)			Effect in reporting period if no assets had been reclassified (1.1.–31.12.2012)	
			31.12.2012		
	Date	Carrying amount in € billion	Fair value in € billion	Income statement in € million	AfS reserve (after taxes) in € million
from: Financial investments available for sale (AfS)	1.7.2008	10.9	10.5	5	187

47 Property, Plant and Equipment

Breakdown in € million	31.12.2013	31.12.2012
Plant and operating equipment	1	2
Total	**1**	**2**

Development of property, plant and equipment in € million	2013	2012
Plant and operating equipment		
Acquisition/production costs		
Balance at 1.1.	**18**	**19**
Disposals	−3	−1
Balance at 31.12.	**15**	**18**
Depreciation and write-ups		
Balance at 1.1.	**−16**	**−16**
Depreciation	−1	−1
Disposals	3	1
Balance at 31.12.	**−14**	**−16**
Carrying amounts		
Balance at 31.12.	**1**	**2**

48 Intangible Assets

Breakdown in € million	31.12.2013	31.12.2012
Purchased software	2	4
Internally developed software	27	34
Other intangible assets	2	1
Total	**31**	**39**

Development of intangible assets				2013	2012
in € million	Software acquired	Internally generated software	Other intangible assets	Total	Total
Acquisition/production costs					
Balance at 1.1.	**76**	**51**	**1**	**128**	**118**
Additions	1	4	2	7	18
Disposals	–	−4	−1	−5	−8
Balance at 31.12.	**77**	**51**	**2**	**130**	**128**
Amortisation and write-ups					
Balance at 1.1.	**−72**	**−17**	**–**	**−89**	**−83**
Impairment losses	−3	−10	–	−13	−12
Disposals	–	3	–	3	6
Balance at 31.12.	**−75**	**−24**	**–**	**−99**	**−89**
Carrying amounts					
Balance at 31.12.	**2**	**27**	**2**	**31**	**39**

49 Other Assets

Other assets in € million	31.12.2013	31.12.2012[1]
Positive fair values from derivative financial instruments	4,601	6,821
Hedging derivatives	4,601	6,821
Fair value hedge	4,115	5,819
Cash flow hedge	486	1,002
Salvage acquisitions	97	176
Other assets	59	238
Capitalised excess cover of qualified insurance for pension provisions	12	7
Total	**4,769**	**7,242**

[1] Adjusted due to retrospective IAS 19 (revised) first time adoption. Details are disclosed in Note «Principles»

The decrease in salvage acquisitions was mainly due to the deconsolidation of Little Britain Holdings (Jersey) Ltd. (€−84 million). The carrying amount of salvage acquisitions also declined as a result of currency effects. The initial consolidation of RPPSE Espacio Oviedo S.L.U., Madrid, led to an increase of €27 million in the salvage acquisition portfolio.

50 Income Tax Assets

Income tax assets in € million	**31.12.2013**	**31.12.2012**[1]
Current tax assets	44	53
Deferred tax assets	1,121	1,651
Total	**1,165**	**1,704**

[1] Adjusted due to retrospective IAS 19 (revised) first time adoption. Details are disclosed in Note «Principles».

The income tax assets item contains both reimbursement claims from actual taxes as well as a considerable element of deferred tax claims. These are attributable to capitalised temporary tax claims in connection with tax losses carried forward as well as other temporary tax claims. A considerable proportion of deferred tax assets were credited pursuant to IAS 12.61 of AfS and cash flow hedge reserve, because the underlying assets were also posted under these items. The actual tax claims also include the capitalised claim for payment of the corporate income tax credit.

51 Subordinated Assets

The balance sheet items do not contain subordinated assets.

52 Repurchase Agreements

As a pledgor of genuine repurchase agreements, pbb Group has pledged assets with a book value of € 1.3 billion (2012: € 0.5 billion). The securities are still recognised as assets. The considerations which have been received amount to € 1.3 billion (2012: € 0.4 billion) and are recognised mainly as liabilities to other banks. Assets in repurchase agreements are the only transferable assets the acquirer can sell or repledge in the absence of default according to IAS 39.37 (a).

53 Securitisation

As of 31 December 2013 pbb Group has the synthetic securitisation Estate UK-3 with a transaction period of 15 years (maturity 2022) and a total volume of lending of € 384 million (2012: € 449 million) in the portfolio. The issuer of the transaction with commercial mortgage loans is pbb. The credit linked notes were completely sold to the investors. Therefore, no risks remained at pbb Group. Overall a reduction of expected loss according to Basel II of € 138 million (2012: € 120 million) was achieved.

Notes to the Consolidated Statement of Financial Position (Equity and Liabilities)

54 Liabilities to Other Banks

Liabilities to other banks by maturities in € million	31.12.2013	31.12.2012
Repayable on demand	1,269	2,058
With agreed maturities	2,253	5,739
Up to 3 months	1,015	378
3 months to 1 year	285	311
1 year to 5 years	478	4,572
5 years and over	475	478
Total	**3,522**	**7,797**

55 Liabilities to Customers

Liabilities to customers by maturities in € million	31.12.2013	31.12.2012
Repayable on demand	676	962
With agreed maturities	10,172	10,933
Up to 3 months	894	736
3 months to 1 year	1,821	1,340
1 year to 5 years	5,360	5,910
5 years and over	2,097	2,947
Total	**10,848**	**11,895**

56 Liabilities Evidenced by Certificates

Liabilities evidenced by certificates by type of business in € million	31.12.2013	31.12.2012
Debt securities issued	25,836	28,761
Mortgage bonds	8,719	7,681
Public sector bonds	12,103	17,160
Other debt securities	4,901	3,414
Money market securities	113	506
Registered notes issued	21,224	23,789
Mortgage bonds	5,907	6,783
Public sector bonds	13,719	15,711
Other debt securities	1,598	1,295
Total	**47,060**	**52,550**

Liabilities evidenced by certificates by maturities in € million	31.12.2013	31.12.2012
With agreed maturities		
Up to 3 months	2,883	6,202
3 months to 1 year	3,239	4,125
1 year to 5 years	19,886	17,874
5 years and over	21,052	24,349
Total	**47,060**	**52,550**

57 Trading Liabilities

Trading liabilities in € million	31.12.2013	31.12.2012
Negative fair values from derivative financial instruments	1,453	3,192
Total	**1,453**	**3,192**

58 Provisions

Breakdown in € million	31.12.2013	31.12.2012[1]
Provisions for pensions and similar obligations	65	71
Restructuring provisions	48	71
Provisions for contingent liabilities and other commitments	13	17
Other provisions	83	76
thereof: Long-term liabilities to employees	2	3
Total	**209**	**235**

[1] Adjusted due to retrospective IAS 19 (revised) first time adoption. Details are disclosed in Note «Principles»

There are defined contribution and defined benefit plans for the employees of pbb Group. In the defined contribution plans pbb makes payments for commitments by industry-wide organisations, for instance in Germany the BVV. In almost all non-German entities a defined percentage of fixed salary is paid into externally managed pension funds for employees as part of defined contribution pension schemes. Expenses in respect of defined contribution plans amounted to €–5 million (2012: €–5 million). In the year 2014 the expense may be lower due to the reduced number of employees. Expenses in respect of contribution-based plans for persons with key function in the Group amounted to less than €–1 million (2012: €–1 million). The employer's contribution to the statutory pension insurance amounted to €–7 million in the year 2013 (2012: €–8 million).

In case of defined benefit plans the employees receive a direct commitment from their respective company. The pension plan especially contains retirement pensions, invalidity pensions and surviving dependant's pensions. The receipt of retirement pensions respectively invalidity pensions starts after a vesting period is fulfilled, earliest after reaching a minimum age in the case of part or full incapacity for work, latest when going into retirement, usually after completion of the 65th year of life. In the case of active employees there are predominantly modern modular pension plans. For the other eligible persons there are also final salary-based defined benefit plans. The annual pension module depends amongst others from the paid gross annual salary and the member's length of service. The surviving dependant's pension usually amounts to 60% pension or contribution of the spouse. The pension plan is administered by pbb itself with the aid of an external service provider for the administration.

Pension provisions are recognised for obligations arising from direct commitments. The defined benefit plans have been principally closed for new entrants since 1 April 2004. There have been no plan amendments, curtailments and settlements in the years 2013 and 2012.

The risk of insolvency is covered within the framework of legal requirements by Pensionssicherungs-verein a.G. in relation to the total amount of pension obligations.

The following actuarial assumptions were used to measure the defined benefit pension obligations:

Actuarial assumptions in %	**31.12.2013/ 1.1.2014**	**31.12.2012/ 1.1.2013**
Discount rate	3.50	3.25
Rate of increase in pension obligations	2.00	2.00
Rate of increase in future compensation and vested rights	2.50	2.50

The rate of increase over career amounts for members of the Management Board 0.0% (2012: 0.0%), for directors and non-pay-scale staff 1.5% (2012: 1.5%) and for pay-scale staff 0.5% (2012: 0.5%). The guidance tables 2005G from Klaus Heubeck were used as the biometric basis.

The pension benefit obligations of pbb do not contain any unusual or entity-specific risks. pbb is faced by the common demographic risks, for example from longevity or invalidity of the entitled employees, and common financial risks like for example a change of the discount rate. pbb took out reinsurance to protect itself against parts of these risks. The reinsurance is a qualifying insurance policy in accordance with IAS 19 and thus is a plan asset. The fair value of plan assets is a component of the net defined benefit liability which is deducted from the present value of the defined benefit obligation. The reinsurance does not consist of any unusual or plan-specific risks.

Principally, the pension payments of the reinsured pension obligations are funded by the income from the plan assets. If the income does not cover the pension payments pbb has to pay the pensions out of its own funds. For the non-reinsured pension obligations the payments are also made out of own funds.

Amounts recognised in financial statements (net defined benefit liability) in € million	**2013**	**2012[1]**
Present value of defined benefit obligation	247	261
Fair value of plan assets	–182	–190
Total	**65**	**71**

[1] Adjusted due to retrospective IAS 19 (revised) first time adoption. Details are disclosed in Note «Principles».

Development of net defined benefit liability in € million	**2013**	**2012[1]**
Balance at 1.1.	**71**	**23**
Transfer of staff	–	–
Pension expenses	4	3
Remeasurements	–7	50
Reclassifications in reimbursements	2	–
Direct payments to beneficiaries	–5	–5
Balance at 31.12.	**65**	**71**

[1] Adjusted due to retrospective IAS 19 (revised) first time adoption. Details are disclosed in Note «Principles»

Development of defined benefit obligation in € million	**2013**	**2012[1]**
Balance at 1.1.	**261**	**215**
Transfer of staff	–4	–
Current service costs	2	1
Interest expenses	8	10
Remeasurements	–7	49
Actuarial gains/losses from demographic assumptions	–	–
Actuarial gains/losses from financial assumptions	–8	47
Actuarial gains/losses from experience assumptions	1	2
Settlements	–	–
Payments to beneficiaries	–13	–14
Balance at 31.12.	**247**	**261**

[1] Adjusted due to retrospective IAS 19 (revised) first time adoption. Details are disclosed in Note «Principles»

Plan assets consist exclusively of reinsurance pledged to plan beneficiaries. The plan assets accordingly do not contain any own financial instruments or any own used property, plant and equipment. For 2014 there are no contributions to plan assets expected. pbb does not use special asset-liability matching strategies to manage the pledged reinsurance.

Development of fair value of plan assets in € million	2013	2012[1]
Balance at 1.1.	**190**	**192**
Transfer to staff	–4	–
Interest income	6	8
Remeasurements	–	–1
Payments to beneficiaries	–8	–9
Reclassifications in/from reimbursements	–2	–
Balance at 31.12.	**182**	**190**

[1] Adjusted due to retrospective IAS 19 (revised) first time adoption. Details are disclosed in Note «Principles»

Development of pension expenses in € million	2013	2012
Service costs	2	1
Current service costs	2	1
Past service costs	–	–
Curtailments	–	–
Gains/losses on settlements	–	–
Net interest expenses	2	2
Interest expenses on defined benefit obligation	8	10
Interest income on plan assets	–6	–8
Total	**4**	**3**

For the year 2014 pbb expects pension expenses of a similar amount as in 2013. Pension expenses are part of general administrative expenses. As the pension plan has been principally closed further contributions in 2014 are not expected.

Remeasurements of the net defined benefit liability result from actuarial gains and losses and the return on plan assets excluding amounts included in net interest on the net defined benefit liability.

Remeasurement recognised in other comprehensive income (equity) in € million	2013	2012[1]
Actuarial gains/losses from demographic assumptions	–	–
Actuarial gains/losses from financial assumptions	8	–47
Actuarial gains/losses from experience assumptions	–1	–2
Remeasurements from plan assets	–	–1
Total	**7**	**–50**

[1] Adjusted due to retrospective IAS 19 (revised) first time adoption. Details are disclosed in Note «Principles»

Delevopment of reimbursement in € million	2013	2012
Balance at 1.1.	**7**	**7**
Additions	2	–
Balance at 31.12.	**9**	**7**

As at 31 December 2013, the quantitative sensitivity analysis – which uses the same measurement methods as the obligation recognised in the statement of financial position – for the material actuarial assumptions is as follows:

Actuarial assumptions	Discount rate		Rate of increase in pension obligations		Rate of increase in future compensation and vested rights	
Change of sensitivity level in percentage points	0.5 increase	0.5 decrease	0.5 increase	0.5 decrease	0.5 increase	0.5 decrease
Gross obligation	231	264	259	235	247	246

The assumption of mortality only has an immaterial effect because the risk of longevity is mainly covered by the plan assets.

The weighted average duration of the defined benefit obligations amounted to 14 years at 31 December 2013 (2012: 14 years).

Development of provisions (without provisions for pension and similar obligations) in € million	Restructuring provisions	Provisions for contingent liabilities and other commitments	Other provisions
Balance at 1.1.2012	**68**	**20**	**73**
Additions	11	11	47
Reversals	–5	–8	–15
Increase of the present value due to passage of time (unwinding)	4	–	1
Amounts used	–7	–5	–31
Reclassifications	–	–1	1
Balance at 31.12.2012	**71**	**17**	**76**
Balance at 1.1.2013	**71**	**17**	**76**
Additions	4	–	74
Reversals	–11	–4	–18
Increase of the present value due to passage of time (unwinding)	1	–	–
Amounts used	–17	–	–49
Reclassifications	–	–	–
Balance at 31.12.2013	**48**	**13**	**83**

On 19 December 2008 the Management Board and Supervisory Board of pbb Group decided upon the strategic realignment and restructuring of the Group. A restructuring provision amounting to € 120 million was created for obligations relating to the strategic realignment and restructuring in the fourth quarter 2008. In the financial year 2013 €–17 million (2012: €–7 million) were used of this provision. The restructuring provision will probably be completely utilised by the year 2024.

The provisions for contingent liabilities and other commitments mainly comprise provisions for guarantee risks, letters of credit, irrevocable loan commitments and litigation risks in the lending business.

The other provisions comprise primarily provisions for legal risks, other taxes, long-term liabilities with regard to employees and provisions in connection with the transfer of positions to FMS Wertmanagement.

Legal risk (litigation risk) pbb Group is bound, in all jurisdictions in which it conducts its business, to comply with a large number of statutory and supervisory requirements and regulations such as certain rules of conduct to avoid conflicts of interest, to combat money laundering, to prevent terrorist financing, to prevent criminal offences to the detriment of the financial sector, to regulate foreign trade and to safeguard bank, business and data secrecy. Given the nature and international scope of its business activities and the large number of relevant requirements and regulations, pbb Group is involved in litigation, arbitration and regulatory proceedings in several countries. These also include criminal and administrative proceedings as well as the assertion of claims in an amount not specified by the party asserting the claim. pbb Group recognises provisions for the uncertain liabilities arising from these proceedings if the potential outflow of resources is sufficiently likely and the amount of the liability can be estimated. The probability of the outflow of resources, which often cannot be estimated with certainty, is highly dependent on the outcome of the proceedings. The assessment of this probability and the quantification of the uncertain liability are largely based on estimates. The actual liability can vary considerably from this estimate. In accounting for the individual cases, pbb Group analyses developments in both individual cases and comparable cases, drawing on its own expertise or appraisals and opinions by external consultants, and in particular by legal advisors, depending on the significance and complexity of the case concerned. The provisions recognised for the proceedings are not reported separately as pbb Group believes that the outcome of the proceedings would be seriously compromised by their disclosure.

pbb received contractually agreed compensation of €6 million for a former French financing arrangement, which has since been repaid in full. The customer has brought an action before the Paris commercial court for repayment of the fee, which it believes to be unreasonable.

In award proceedings relating to the merger of three predecessor mortgage banks to form pbb in 2001, the new appraisal ordered by the court has resulted in an additional payment averaging €1.00 per share.

The profit participation certificates issued by the predecessor institutions participated in significant losses due to the net losses for the period incurred since 2008, and to pbb's net accumulated losses since this time. These reduced the amounts repaid and, as a result, no interest was paid. Individual plaintiffs therefore initiated legal proceedings, contesting in particular various individual clauses relating to loss participation and replenishment following loss participation. The key questions in this connection are which capital components must be used to calculate loss participation and whether replenishment is required if pbb records a net gain for the period or a net retained profit. The contested profit participation certificates had an aggregate principal amount of €260 million (of which proceedings involving a principal amount of €12.5 million were pending). The plaintiffs' repayment claims may increase up to the full amount or in part as a result of these actions.

Otherwise, no proceedings for which the Management Board believes the probability of an outflow of resources to be not unlikely, or which are of material significance to pbb Group for other reasons, exist with an amount in dispute in excess of €5 million.

59 Other Liabilities

Other liabilities in € million	31.12.2013	31.12.2012
Negative fair values from derivative financial instruments	4,441	6,230
Hedging derivatives	4,441	6,227
Fair value hedge	3,969	5,515
Cash flow hedge	472	712
Derivatives hedging dFVTPL financial instruments	–	3
Other liabilities	281	8,208
Total	**4,722**	**14,438**

The transfer of loans to FMS Wertmanagement in August 2013 was recognised in the statement of financial position and reduced the other liabilities position by €7.5 billion. Other liabilities include amongst others liabilities from the offsetting of results and also accruals pursuant to IAS 37. Accruals in particular include accounts payable in respect of invoices still outstanding, short-term liabilities to employees and other accruals in respect of commission, interest, operating expenses, etc.

60 Income Tax Liabilities

Income tax liabilities in € million	31.12.2013	31.12.2012
Current tax liabilities	64	64
Deferred tax liabilities	1,126	1,634
Total	**1,190**	**1,698**

Income tax liabilities include both provisions and liabilities from current taxes as well as deferred tax liabilities. A significant proportion of deferred tax liabilities were netted against cash flow hedge reserve.

61 Subordinated Capital

Breakdown in € million	31.12.2013	31.12.2012
Subordinated liabilities	1,119	1,689
Hybrid capital instruments	321	304
Total	**1,440**	**1,993**

With all subordinated liabilities, there can be no early repayment obligation on the part of the issuer. In the event of bankruptcy or liquidation, such liabilities may only be repaid after all non-subordinated creditors have been satisfied.

Subordinated capital by maturities in € million	**31.12.2013**	**31.12.2012**
With agreed maturities		
Up to 3 months	41	89
3 months to 1 year	10	502
1 year to 5 years	874	430
5 years and over	515	972
Total	**1,440**	**1,993**

The unwinding of some instruments of subordinated capital led to an expense of €–18 million (2012: €–17 million).

Participating Certificates Outstanding Issued participatory capital comprises the following issues with a carrying amount of €0 million (2012: €0 million):

Participating certificates outstanding in € million	Year of issue	Type	Nominal amount in € million	Interest rate in %	Maturity
pbb	1989	Registrated participation certificate	10	8.000	2014

The interest claim is reduced to the extent that a payout would result in an annual balance sheet loss for the year. Holders of participating certificates outstanding principally participate in any net loss or balance sheet loss for the year through a reduction in their repayment entitlements. During the term of the profit participation certificates, after the holders participate in net accumulated losses, the reduced profit participation capital must be replenished up to the principal amount before any additions are made to reserves and before any dividend is paid on the share capital. As at 31 December 2013, the holders of the profit participation certificates did not have any claim to payment due to (past) loss participations in accordance with the terms and conditions of the profit participation certificates.

Hybrid Capital Instruments Hybrid capital instruments in particular include issues in the form of preferred securities placed by specifically established special-purpose entities. These instruments differ from conventional supplementary capital in that they are subject to more stringent conditions in terms of maturity. In addition, hybrid capital instruments are not repaid until after supplementary capital (subordinated liabilities and participating certificates outstanding) in the event of bankruptcy. In contrast to traditional components of core capital, the claim to a share of profit, which depends on the existence of profit, takes the form of a fixed or variable interest payment in the case of hybrid capital instruments. Moreover, hybrid capital can be issued both with unlimited maturity and repayable in the long term.

62 Equity

Subscribed capital equals the maximum liability of the shareholder for the liabilities of the corporation to its creditors. Additional paid-in capital includes premiums from the issue of shares and the contribution of Finanzmarktstabilisierungsfonds-FMS to reserves. Retained earnings were generally created only from net income of the current financial year or previous periods. This includes legal reserves to be created from net income and other retained earnings.

The subscribed capital as of 31 December 2013 and during the entire financial year 2013 amounts to €380,376,059.67 which is divided into 134,475,308 ordinary bearer shares in the form of no-par-value shares representing a theoretical interest in the share capital of €2.83 per no-par-value share. HRE Holding holds 100% of the share capital of pbb. Finanzmarktstabilisierungsfonds-FMS is the only shareholder of HRE Holding. At 31 December 2013 and 31 December 2012 there was neither authorised capital nor conditional capital.

In the year 2009 Finanzmarktstabilisierungsfonds-FMS provided pbb with a silent participation of €1.0 billion. The silent participation participates in the cumulative loss calculated in accordance with the regulations of commercial law to the same extent that the silent participation is related to the total carrying amount of all liable capital shares which participate in the cumulative loss. The total loss of the silent partner in relation to the cumulative loss under commercial law is limited to its silent contribution. The cumulative loss which is attributable to the year 2008 is not used for calculating the loss participation. At the end of the year 2013, the silent contribution was reduced by €37 million to €92 million (2012: by €53 million to €129 million) in the commercial law financial statements of pbb. pbb has a replenishment obligation.

63 Trust Business

The following tables show the volume of fiduciary business not shown in the consolidated balance sheet.

Trust assets in € million	**31.12.2013**	**31.12.2012**
Loans and advances to customers	3	3
Total	**3**	**3**

Trust liabilities in € million	**31.12.2013**	**31.12.2012**
Liabilities to customers	3	3
Total	**3**	**3**

Notes to the Consolidated Statement of Cash Flows

64 Notes to the Items in the Consolidated Statement of Cash Flows

The consolidated statement of cash flows shows the cash flows of the financial year broken down into cash flows attributable to operating activities, investing activities and financing activities. Cash and cash equivalents correspond to the balance sheet item cash reserve, and include cash in hand and credit balances at central banks.

Operating activities are defined broadly, and correspond to operating result. Cash flow from operating activities includes payments (inflows and outflows) attributable to loans and advances to other banks and customers as well as securities attributable to trading assets and other assets. Inflows and outflows attributable to liabilities to other banks and customers, liabilities evidenced by certificates and other liabilities are also included under operating activities. The interest and dividend payments resulting from operating activities are shown under cash flow from operating activities.

Cash flow from investing activities comprises payments for investment and security holdings as well as for property, plant and equipment.

Cash flow from financing activities comprises inflows from capital increases, payments into reserves and silent participations as well as inflows and outflows for subordinated capital.

All shares of Little Britain Holdings (Jersey) Ltd., Jersey, were sold in financial year 2013. The selling price less costs and the repayment of a liability owed by the company to pbb was € 81 million and was recognised under cash flow from investing activities.

Notes to the Financial Instruments

65 Derivative Transactions

In order to minimise (reduce) both the economic and the regulatory credit risk, bilateral netting agreements have been concluded. By means of such netting agreements, the positive and negative fair values of the derivatives contracts included under the master agreement can be offset against one another, and the future regulatory risk add-ons for these products can be reduced. Through this netting process, the credit risk is limited to a single net claim on the party to the contract.

For both regulatory reports and the internal measurement and monitoring of the credit commitments, such risk-reducing techniques are utilised only if they are considered to be enforceable under the respective legal system in the event that the business associate becomes insolvent. Legal advice is taken in order to check enforceability.

Similar to the master agreements, pbb Group concludes collateral agreements with its business associates to collateralise the net claim or liability remaining after netting (obtained or pledged collateral). Usually, this collateral management reduces credit risk by means of prompt measurement and adjustment exposure to customers.

Volume of derivatives at 31 December 2013	Notional amount				Fair value	
	Remaining maturities					
in € million	Less than 1 year	1 to 5 years	More than 5 years	**Total**	positive	negative
Interest-based transactions						
OTC products	13,027	41,587	41,893	96,507	6,176	5,830
Interest rate swaps	11,931	38,223	41,871	92,025	6,165	5,815
Interest rate options	1,096	3,364	22	4,482	11	15
Call options	543	1,634	16	2,193	11	–
Put options	553	1,730	6	2,289	–	15
Total	**13,027**	**41,587**	**41,893**	**96,507**	**6,176**	**5,830**
Foreign-currency-based transactions						
OTC products	3,971	835	336	5,142	67	64
Spot and forward currency transactions	3,818	37	–	3,855	17	38
Interest rate/currency swaps	153	798	336	1,287	50	26
Total	**3,971**	**835**	**336**	**5,142**	**67**	**64**
Total	**16,998**	**42,422**	**42,229**	**101,649**	**6,243**	**5,894**

Use made of derivative transactions at 31 December 2013		Fair value	
in € million	Notional amount	positive	negative
Interest-based transactions			
Fair value hedge accounting	56,749	4,115	3,969
Cash flow hedge accounting	6,332	443	455
Derivatives hedging dFVTPL financial instruments	–	–	–
Stand-alone derivatives	33,426	1,618	1,406
Total	**96,507**	**6,176**	**5,830**
Foreign-currency-based transactions			
Cash flow hedge accounting	452	43	17
Stand-alone derivatives	4,690	24	47
Total	**5,142**	**67**	**64**
Total	**101,649**	**6,243**	**5,894**

Volume of derivatives at 31 December 2012	Notional amount				Fair value	
	Remaining maturities					
in € million	Less than 1 year	1 to 5 years	More than 5 years	**Total**	positive	negative
Interest-based transactions						
OTC products	20,452	51,772	48,664	120,888	10,026	9,325
Interest rate swaps	18,691	48,893	48,648	116,232	10,012	9,308
Interest rate options	1,761	2,879	23	4,663	14	17
Call options	872	1,392	6	2,270	14	–
Put options	889	1,487	17	2,393	–	17
Total	**20,452**	**51,772**	**48,671**	**120,895**	**10,026**	**9,325**
Foreign-currency-based transactions						
OTC products	4,968	479	607	6,054	120	97
Spot and forward currency transactions	4,838	38	–	4,876	23	24
Interest rate/currency swaps	130	441	607	1,178	97	73
Total	**4,968**	**479**	**607**	**6,054**	**120**	**97**
Total	**25,420**	**52,251**	**49,278**	**126,949**	**10,146**	**9,422**

Use made of derivative transactions at 31 December 2012 in € million	Notional amount	Fair value positive	 negative
Interest-based transactions			
Fair value hedge accounting	61,019	5,819	5,515
Cash flow hedge accounting	11,017	919	654
Derivatives hedging dFVTPL financial instruments	80	–	3
Stand-alone derivatives	48,779	3,288	3,153
Total	**120,895**	**10,026**	**9,325**
Foreign-currency-based transactions			
Cash flow hedge accounting	667	83	58
Stand-alone derivatives	5,387	37	39
Total	**6,054**	**120**	**97**
Total	**126,949**	**10,146**	**9,422**

Counterparties	**31.12.2013**		**31.12.2012**	
	Fair value		Fair value	
in € million	positive	negative	positive	negative
OECD banks	5,474	5,788	8,121	8,800
OECD financial institutions	205	42	1,090	572
Other companies and private individuals	564	64	935	50
Total	**6,243**	**5,894**	**10,146**	**9,422**

66 Cash Flow Hedge Accounting

The cash flows of the hedged items shown in cash flow hedge accounting are expected to occur in the following periods:

Cash flow hedge: periods of hedged items when cash flows are expected to occur in € million	31.12.2013	31.12.2012
Up to 1 month	–1	–
1 month to 3 months	–3	–
3 months to 1 year	–3	2
1 year to 2 years	–10	–3
2 years to 5 years	–15	13
5 years and over	–74	312
Total	**–106**	**324**

It is expected that the cash flows will affect the income statement in the period of occurrence.

The development of the cash flow hedge reserve is shown in the consolidated statement of changes in equity.

67 Undiscounted Cash Flows of Financial Liabilities

Contractual undiscounted cash flows of the financial liabilities according to IFRS 7.39 in € billion	31.12.2013	31.12.2012
Up to 3 months	3	8
From derivative financial instruments	1	1
From non-derivative financial instruments	2	7
3 months to 1 year	7	9
From derivative financial instruments	–	1
From non-derivative financial instruments	7	8
1 year to 5 years	33	38
From derivative financial instruments	2	4
From non-derivative financial instruments	31	34
5 years and over	35	46
From derivative financial instruments	2	4
From non-derivative financial instruments	33	42

In conformity with the requirements, the contractual undiscounted cash flow maturities are presented in accordance with the worst-case scenario, meaning that if there are options or terminations rights involved the most unfavourable case from a liquidity perspective is assumed. This presentation does not reflect the economic management which is based on expected cash flows. The liquidity risk strategy and management of pbb Group is described in the risk and opportunity report.

68 Assets Assigned or Pledged as Collateral

The following assets and received collaterals were assigned or pledged as collateral:

Liabilities in € million	31.12.2013	31.12.2012
Liabilities to other banks	1,479	4,474
Total	**1,479**	**4,474**

The following assets were pledged as collateral for the above liabilities:

Assets pledged in € million	31.12.2013	31.12.2012
Loans and advances to customers	200	232
Financial investments	1,294	5,775
Total	**1,494**	**6,007**

The assets pledged mainly resulted from repurchase agreements. The transactions were carried out at the normal standard terms for repurchase transactions and concluded on an arm's-length basis.

69 Collaterals Permitted to Resell or Repledge

As of 31 December 2013 and as of 31 December 2012 there were no collaterals that may be resold or repledged in the absence of default.

70 Transfer of Financial Assets

Transferred financial assets shall be derecognised if the derecognition criteria of IAS 39 were met. The derecognition concept of IAS 39 requires to derecognise financial assets, if risks and rewards were almost completely transferred.

However, the transferring party could retain a continuing involvement in derecognised assets. Normal representations and warranties in connection with the transfer, e.g. relating to fraud, good faith and fair dealings, do not represent a continuing involvement. pbb Group has no continuing involvement in transferred and derecognised financial assets.

71 Fair Values of Financial Instruments

The fair value of financial instruments, in the opinion of pbb Group, is the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction in the principal (or most advantageous) market at the measurement date under current market conditions (i. e. an exit price). The fair values were determined as of the balance sheet date based on the market information available and on valuation methods described here.

All financial assets and liabilities that are measured at fair value are grouped into the three fair value hierarchies by pbb Group. Reclassifications within the fair value hierarchy are made at the end of the reporting period. The three-level hierarchy is based on the degree to which the input for the fair value measurement is observable:

- Level1 – quoted priced (unadjusted) in active markets for identical financial assets or financial liabilities.
- Level 2 – inputs that are observable either directly or indirectly, other than quoted prices included within Level 1.
- Level 3 – valuation techniques that include inputs that are not based on observable market data (unobservable inputs).

Fair values of financial instruments and fair value hierarchy

					31.12.2013
in € million	Carrying amounts	Fair value	Level 1	Level 2	Level 3
Financial assets	**72,559**	**73,581**	**16,836**	**25,900**	**30,845**
at fair value through profit or loss	5,757	5,757	–	5,678	79
at fair value not affecting profit or loss	4,770	4,770	4,284	482	4
in balance sheet not measured at fair value	62,032	63,054	12,552	19,740	30,762
Cash reserve	3,532	3,532	3,532	–	–
Trading assets (HfT)	1,642	1,642	–	1,642	–
Loans and advances to other banks	5,798	5,702	1,728	1,222	2,752
Category LaR	5,798	5,702	1,728	1,222	2,752
Loans and advances to customers[1]	36,094	37,758	2	14,090	23,666
Category LaR	36,094	37,758	2	14,090	23,666
Real Estate Finance	20,501	21,350	–	–	21,350
Public Sector Finance	15,423	16,238	2	14,090	2,146
Other	221	221	–	–	221
Portfolio-based allowances	−51	−51	–	–	−51
Financial investments	20,892	20,346	11,574	4,428	4,344
Category AfS	4,284	4,284	4,284	–	–
Category LaR	16,608	16,062	7,290	4,428	4,344
Other assets	4,601	4,601	–	4,518	83
Fair value hedge derivatives	4,115	4,115	–	4,036	79
Cash flow hedge derivatives	486	486	–	482	4
Financial liabilities	**68,954**	**70,698**	**20,762**	**8,341**	**41,595**
thereof: at fair value through profit or loss	5,422	5,422	–	5,410	12
thereof: at fair value not affecting profit or loss	472	472	–	472	–
in balance sheet not measured at fair value	63,060	64,804	20,762	2,459	41,583
Liabilities to other banks	3,522	3,551	1,330	906	1,315
Liabilities to customers	10,848	11,277	1,329	–	9,948
Liabilities evidenced by certificates	47,060	48,456	18,059	1,553	28,844
Covered	40,810	42,169	15,798	1,499	24,872
Uncovered	6,250	6,287	2,261	54	3,972
Trading liabilities (HfT)	1,453	1,453	–	1,451	2
Other liabilities	4,631	4,631	44	4,431	156
Fair value hedge derivatives	3,969	3,969	–	3,959	10
Cash flow hedge derivatives	472	472	–	472	–
Other financial liabilities	190	190	44	–	146
Subordinated capital	1,440	1,330	–	–	1,330
Other items	**2,594**	**2,675**	**–**	**–**	**2,675**
Contingent liabilities	25	25	–	–	25
Irrevocable loan commitments	2,569	2,650	–	–	2,650

[1] Reduced by allowances for losses on loans and advances

Fair values of financial instruments and fair value hierarchy

in € million	Carrying amounts	Fair value	Level 1	Level 2	Level 3
					31.12.2012
Financial assets	**94,915**	**94,221**	**[1]**	**[1]**	**[1]**
at fair value through profit or loss	9,227	9,227	83	9,065	79
at fair value not affecting profit or loss	4,922	4,922	3,920	998	4
in balance sheet not measured at fair value	80,766	80,072	[1]	[1]	[1]
Cash reserve	1,937	1,937	[1]	[1]	[1]
Trading assets (HfT)	3,325	3,325	–	3,324	1
Loans and advances to other banks	7,995	7,817	[1]	[1]	[1]
Category LaR	7,995	7,817	[1]	[1]	[1]
Loans and advances to customers[2]	49,265	50,143	[1]	[1]	[1]
Category LaR	49,265	50,143	[1]	[1]	[1]
Real Estate Finance	20,747	21,104	[1]	[1]	[1]
Public Sector Finance	19,029	19,252	[1]	[1]	[1]
Other	9,531	9,829	[1]	[1]	[1]
Portfolio-based allowances	–42	–42	[1]	[1]	[1]
Financial investments	25,572	24,178	[1]	[1]	[1]
Category AfS	3,920	3,920	3,920	–	–
Category dFVTPL	83	83	83	–	–
Category LaR	21,569	20,175	[1]	[1]	[1]
Other assets	6,821	6,821	–	6,739	82
Fair value hedge derivatives	5,819	5,819	–	5,741	78
Cash flow hedge derivatives	1,002	1,002	–	998	4
Financial liabilities	**91,615**	**91,688**	**[1]**	**[1]**	**[1]**
at fair value through profit or loss	8,710	8,710	–	8,706	4
at fair value not affecting profit or loss	712	712	–	712	–
in balance sheet not measured at fair value	82,193	82,266	[1]	[1]	[1]
Liabilities to other banks	7,797	7,809	[1]	[1]	[1]
Liabilities to customers	11,895	12,159	[1]	[1]	[1]
Liabilities evidenced by certificates	52,550	52,487	[1]	[1]	[1]
Covered	48,091	48,085	[1]	[1]	[1]
Uncovered	4,459	4,402	[1]	[1]	[1]
Trading liabilities (HfT)	3,192	3,192	–	3,190	2
Other liabilities	14,188	14,194	[1]	[1]	[1]
Fair value hedge derivatives	5,515	5,515	–	5,513	2
Cash flow hedge derivatives	712	712	–	712	–
Derivatives hedging dFVTPL financial instruments	3	3	–	3	–
Other financial liabilities	7,958	7,964	[1]	[1]	[1]
Subordinated capital	1,993	1,847	[1]	[1]	[1]
Other items	**1,110**	**1,004**		**[1]**	**[1]**
Contingent liabilities	75	75	[1]	[1]	[1]
Irrevocable loan commitments	1,035	929	[1]	[1]	[1]

[1] Due to the prospective application of IFRS 13, the fair values of financial assets and liabilities are only broken down by level as at 31.12.2012 if they are regularly measured at fair value

[2] Reduced by allowances for losses on loans and advances

As in the previous year, no financial instruments measured at fair value were reclassified from Level 1 to Level 2 and vice versa. Not all inputs for certain assets that were previously allocated to Level 2 and measured at fair value were observable on the market in 2013. As a result, assets recognised at fair value in the amount of €18 million (2012: €1 million) and financial liabilities in the amount of €3 million (2012: €0 million) were reclassified from Level 2 to Level 3.

Disclosures to the Measurement Methods and Input Parameters

Measurement Process Both the Finance and the Risk Management & Control divisions play a role in the measurement process. The Finance division supplies accounting data. This includes:

> identification data, such as business identification numbers or International Securities Identification Numbers (ISINs)
> static data such as nominal amounts, counterparties, (remaining) terms and counterparty/issuer risk
> accounting data such as carrying amounts, accruals and the effects of hedge accounting

Risk Management & Control calculates additional data used to measure fair value such as interest rates, credit spreads and market prices, as well as internal ratings and LGDs for certain financial instruments.

Finance compiles the data and checks it for completeness. The division then calculates the fair values of the financial instruments using measurement methods determined by Risk Management & Control. Once measurement is complete, Finance performs quality assurance on the data and then approves it for further use.

Measurement of level 2 instruments as of 31 December 2013

	Fair value			
in € million	Assets	Liabilities	Measurement methods	Observable parameters
Trading assets/liabilities	1,642	1,451	DCF methods	Cap volatilities
				Inflation rates
				Reference interest rates
				Swaption volatilities
				Spot market exchange rates
				Yield curves
Fair value hedge derivatives	4,036	3,959	DCF methods	Cap volatilities
				Reference interest rates
				Swaption volatilities
				Yield curves
			Option pricing models	Cap volatilities
				Reference interest rates
				Swaption volatilities
				Spot market exchange rates
				Exchange rates volatilities
				Yield curves
Cash flow hedge derivatives	482	472	DCF methods	Reference interest rates
				Yield curves
			Option pricing models	Cap volatilities
				Reference interest rates
				Swaption volatilities
				Yield curves

Measurement of level 3 instruments as of 31 December 2013	Fair value					
in € million	Assets	Liabilities	Measurement methods	Observable parameters	Non-observable parameters	Parameter range (weighted average)
Trading assets/liabilities	–	2	Option pricing models	Cap volatilities	Asset swap spreads volatilities	64.44% (64.44%)
				Reference interest rates		
				Spot market exchange rates		
				Yield curves		
Fair value hedge derivatives	79	10	Option pricing models	Cap volatilities	Historical index/index correlations	0.26% to 75.52% (19.87%)
				Inflation rates	Volatility of EUROSTOXX50	19.26% (19.26%)
				Reference interest rates	Historical index/exchange rate correlations	−17.83% to 11.58% (−4.9%)
				Fixings on EUROSTOXX50	Dividends in EUROSTOXX50 (volatilities)	3.49% (3.49%)
				Swaption volatilities	Index/inflation correlations	0% (0%)
				Spot market exchange rates		
				Exchange rates volatilities		
				Yield curves		
Cash flow hedge derivatives	4	–	Option pricing models	Cap volatilities	Historical index/index correlations	15.61% (15.61%)
				Reference interest rates	Historical index/exchange rate correlations	−5.95% to −12.27% (−9.11%)
				Swaption volatilities		
				Spot market exchange rates		
				Exchange rates volatilities		
				Yield curves		

Financial instruments not measured at fair value as of 31. December 2013 in € million	Level 2		Level 3		
	Measurement methods	Observable parameters	Measurement methods	Observable parameters	Non-observable parameters
Financial assets					
Loans and receivables (LaR)	DCF models	Credit spreads	DCF models	Credit spreads	Internal rating classes
		Reference interest rates		Reference interest rates	Recovery rates
		Risk-free interest rate		Risk-free interest rate	Expected maturities
		Observable future cash flows		Observable future cash flows	Estimated future cash flows
	Quoted prices in non-active markets	Quoted prices for proxy trades	–	–	–
Financial liabilities					
Financial liabilities at amortised cost	DCF models	Observable future cash flows	DCF models	Observable future cash flows	Estimated future cash flows
		(Own) credit spreads		(Own) credit spreads	(Own) credit spreads (secondary market grid)
		Benchmark interest rates		Benchmark interest rates	–
	Quoted prices in non-active markets	Quoted prices for proxy trades	–	–	–

Sensitivities Although pbb Group believes that its estimates of fair values are appropriate, using reasonably possible alternative input factors will significantly impact the fair value. The following table shows the fair value sensitivity of level 3 instruments as of 31 December 2013 and as of 31 December 2012 which have been quantified on the basis of the specified valuation parameters taking account of usual market scenarios:

Sensitivities of level 3 instruments	31.12.2013		31.12.2012	
in € million	Positive changes	Negative changes	Positive changes	Negative changes
Assets				
Financial assets at fair value through profit or loss				
Fair value hedge derivatives	0.7	−0.7	5.2	−4.5
Total	**0.7**	**−0.7**	**5.2**	**−4.5**
Liabilities				
Financial liabilities at fair value through profit or loss				
Trading liabilities	–	–	0.1	−0.1
Fair value hedge derivatives	–	–	0.1	−0.1
Total	**–**	**–**	**0.2**	**−0.2**

The disclosed favourable and unfavourable changes are calculated independently from each other. Offsetting effects due to compensating derivatives and hedge relationships attenuate both favourable and unfavourable changes.

Changes in Level 3 Financial Instruments measured at Fair Value

Changes in level 3 financial assets	Financial assets at fair value through profit or loss		Financial assets at fair value not affecting profit or loss	
in € million	Trading assets	Fair value hedge derivatives	Cash flow hedge derivatives	**Total**
Balance at 1.1.2012	**–**	**49**	**2**	**51**
Comprehensive income				
Income statement	–	30	–	30
Revaluation reserve	–	–	2	2
Purchases	1	–	–	1
Sales	–	−2	–	−2
Issues	–	–	–	–
Settlements	–	–	–	–
Transfers into Level 3	–	1	–	1
Transfers out of Level 3	–	–	–	–
Balance at 31.12.2012	**1**	**78**	**4**	**83**
Balance at 1.1.2013	**1**	**78**	**4**	**83**
Comprehensive income				
Income statement	−1	−17	–	−18
Revaluation reserve	–	–	–	–
Purchases	–	8	–	8
Sales	–	−8	–	−8
Issues	–	–	–	–
Settlements	–	–	–	–
Reclassification into Level 3	–	18	–	18
Reclassification out of Level 3	–	–	–	–
Balance at 31.12.2013	**–**	**79**	**4**	**83**

Changes in level 3 financial liabilities	Financial liabilities at fair value through profit or loss		Financial liabilities at fair value not affecting profit or loss	
in € million	Trading liabilities	Fair value hedge derivatives	Cash flow hedge derivatives	**Total**
Balance at 1.1.2012	**1**	**18**	**–**	**19**
Comprehensive income				
Income statement	–	–9	–	–9
Revaluation reserve	–	–	–	–
Purchases	1	–	–	1
Sales	–	–7	–	–7
Issues	–	–	–	–
Settlements	–	–	–	–
Transfers into Level 3	–	–	–	–
Transfers out of Level 3	–	–	–	–
Balance at 31.12.2012	**2**	**2**	**–**	**4**
Balance at 1.1.2013	**2**	**2**	**–**	**4**
Comprehensive income	–	–	–	–
Income statement	–	–2	–	–2
Revaluation reserve	–	–	–	–
Purchases	–	9	–	9
Sales	–	–2	–	–2
Issues	–	–	–	–
Settlements	–	–	–	–
Reclassification into Level 3	–	3	–	3
Reclassification out of Level 3	–	–	–	–
Balance at 31.12.2013	**2**	**10**	**–**	**12**

Level 3 financial assets and liabilities measured at fair value through profit or loss generated a loss of €–16 million in 2013 (2012: gain of €39 million). The earnings contributions made by trading assets and trading liabilities are presented under net trading income, whereas the effects of hedge relationships recognised in profit or loss are reported under net income from hedge relationships.

There were no changes recognised directly in equity in 2013. In the previous year, changes to cash flow hedge derivatives amounting to €2 million were recognised in the cash flow hedge reserve.

Assets and Liabilities According to Measurement Categories and Classes

The carrying amounts reflect the maximum on balance sheet exposure to credit risk of the assets respectively the maximum amount the entity could have to pay of the other items according to IFRS 7.

Asset and liabilities according to measurement categories and classes in accordance with IAS 39 in € million	**31.12.2013**	**31.12.2012**
Assets	**72,559**	**94,915**
Loans and receivables (LaR)	58,500	78,829
Available for sale (AfS)	4,284	3,920
Held for trading (HfT)	1,642	3,325
dFVTPL assets (dFVTPL)	–	83
Cash reserve	3,532	1,937
Positive fair values from hedging derivatives	4,601	6,821
Liabilities	**68,954**	**91,615**
Held for trading (HfT)	1,453	3,192
Financial liabilities at amortised cost	63,060	82,193
Negative fair values from hedging derivatives	4,441	6,230

72 Exposure to Selected European Countries

Exposure to selected European countries as of 31 December 2013									
in € million	Counterparty	IAS 39 measurement category	Up to 3 months	From 3 months to 1 year	From 1 year to 5 years	From 5 years and over	**Total**	Notional amount	Fair value
Italy	Sovereign	LaR	–	–	107	149	256	253	227
		AfS	–	–	–	1,300	1,300	1,060	1,300
	Sub-sovereign	LaR	–	–	8	1,028	1,036	1,002	863
	State-guaranteed	LaR	–	–	176	404	580	505	521
Portugal	Sovereign	LaR	–	–	43	–	43	36	41
		AfS	–	–	46	109	155	165	155
	Sub-sovereign	LaR	–	–	130	200	330	330	254
	State-guaranteed	LaR	–	62	100	323	485	465	364
Spain	Sovereign	AfS	–	667	–	–	667	650	667
	Sub-sovereign	LaR	–	29	1,116	785	1,930	1,783	1,803
		HfT	–	–	–	3	3	35	3
	State-guaranteed	LaR	21	–	74	155	250	237	259

Exposure to selected European countries as of 31 December 2012

in € million	Counterparty	IAS 39 measurement category	Up to 3 months	From 3 months to 1 year	From 1 year to 5 years	From 5 years and over	**Total**	Notional amount	Fair value
Italy	Sovereign	LaR	–	–	98	150	248	242	197
		AfS	–	–	–	1,250	1,250	1,060	1,250
	Sub-sovereign	LaR	–	22	10	1,134	1,166	1,112	869
	State-guaranteed	LaR	–	–	26	674	700	595	581
Portugal	Sovereign	LaR	–	–	46	–	46	37	42
		AfS	–	–	44	101	145	165	145
	Sub-sovereign	LaR	100	–	86	244	430	430	301
	State-guaranteed	LaR	–	–	202	374	576	547	389
Spain	Sub-sovereign	LaR	–	6	832	1,282	2,120	1,888	1,554
		HfT	–	–	–	5	5	35	5
	State-guaranteed	LaR	42	100	106	174	422	399	375

As of 31 December 2013 and as of 31 December 2012 pbb Group did not have any exposure to sovereign counterparties of Greece, Cyprus and Ireland. The same applies for sub-sovereign or state-guaranteed counterparties.

The exposure to selected countries shown in the table contains loans and advances and securities. In addition, it shows interest rate derivatives to sovereign and sub-sovereign counterparties. The interest rate derivatives are netted with collaterals. Time lags in providing the collaterals and haircuts are not taken into account. State-guaranteed exposure contains for example loans and advances to banks and corporations which are guaranteed by sovereigns or sub-sovereigns. As of 31 December 2013 and as of 31 December 2012 pbb Group did not have any credit default swaps whose underlyings are linked to sovereigns, sub-sovereigns and state-guaranteed exposures of the countries shown above.

For the total exposure as of 31 December 2013 and as of 31 December 2012 the exposure at default according to regions is disclosed in the risk and opportunity report.

For financial assets which are measured at fair value affecting income changes in value are directly included in the book value. pbb Group tests financial assets which are not measured at fair value affecting income for impairments. Allowances for loans and advance or impairments for securities are created if there is objective evidence that it will not be possible for the entire amount which is due according with the original contractual conditions to be recovered. As per 31 December 2013 and as of 31 December 2012 there was no such objective evidence.

The fair values of the exposure to selected European countries were determined by applying the measurement methods disclosed in the Note «Fair Values of Financial Instruments».

73 Past Due but Not Impaired Assets

The following table shows the total portfolio of the partly or completely past due but not impaired loans and advances as of 31 December 2013 and as of 31 December 2012. However, no individual allowances were made for these assets respectively the collaterals underlying these assets as pbb Group does not consider that there is any issue regarding their recoverability. Such timing issues in receipts of payments due occur regularly (up to three months) in the normal course of business and do not, by themselves, impair the quality of the asset.

LaR Assets

LaR assets: past due but not impaired (total investments) in € million	**31.12.2013**	**31.12.2012**
Up to 3 months	274	665
From 3 months to 6 months	40	71
From 6 months to 1 year	81	67
From 1 year and over	47	75
Total	**442**	**878**

Carrying amounts LaR assets in € billion	**31.12.2013**	**31.12.2012**
Carrying amount of LaR assets that are neither impaired nor past due	57.6	77.3
Carrying amount of LaR assets that are past due but not impaired (total investment)	0.4	0.9
Carrying amount of individually assessed impaired LaR assets (net)	0.4	0.6
Balance of individual allowances	0.1	0.3
Balance of portfolio-based allowances	0.1	0.1
Total	**58.6**	**79.2**
thereof: Loans and advances to other banks (including investments)	5.8	8.0
Loans and advances to customers (including investments)	36.2	49.6
Financial investments (gross)	16.6	21.6

The carrying amount of assets that would otherwise be past due or impaired and whose terms have been renegotiated amounts to €91 million (2012: €90 million).

The fair value of collaterals for the impaired financial assets amounts to approximately €0.4 billion (2012: €0.6 billion). The collaterals mainly consist of land charges.

AfS Assets As of 31 December 2013 and as of 31 December 2012 pbb Group has neither past due and not impaired nor impaired AfS financial investments in the portfolio.

74 Restructured Loans and Advances

As in the previous year, restructuring agreements mainly related to standstill agreements and to the discontinuation of contractual arrangements in the year under review.

Restructured loans and advances in € million	31.12.2013	31.12.2012
Carrying amount of loans and advances that are neither impaired nor past due	1,128	1,271
Carrying amount of loans that are past due but not impaired (gross)	89	4
Carrying amount of individually assessed impaired loans and advances (gross)	352	543
Total	**1,569**	**1,818**

Development of restructured loans and advances in € million	2013	2012
Balance at 1.1.	**1,818**	**1,704**
Additions	213	392
Disposals	−462	−278
Balance at 31.12.	**1,569**	**1,818**

Proportion of restructured loans and advances in the total stock in %	31.12.2013	31.12.2012
Proportion of restructured loans and advances in the total stock	3.7	3.2

Allowances for losses on restructured loans and advances in € million	31.12.2013	31.12.2012
Individual allowances	62	262
Portfolio-based allowances	7	8
Total	**69**	**270**

Proportion of allowances for losses in the restructured loans and advances stock in %	31.12.2013	31.12.2012
Proportion of allowances for losses in the restructured loans and advances stock	4.4	14.9

75 Netting of Financial Instruments

The following tables show the gross carrying amounts of recognised financial assets respectively liabilities, the gross carrying amounts of the items offset in the statement of financial position and the net amounts of the financial assets and liabilities recognised in the statement of financial position. They also show the rights of set-off that did not lead to an offsetting in the statement of financial position, the collateral received for financial assets, the collateral pledged for financial liabilities and the net amounts of financial assets and liabilities remaining following the application of the netting agreements and deduction of the collateral.

Netting agreements pbb Group routinely enters into standardised bilateral netting agreements in the derivatives business to minimise both legal risk and economic and regulatory counterparty credit risk. The national respectively international agreements used are the German Master Agreement for Financial Futures and the ISDA Master Agreement issued by the International Swaps and Derivatives Association. The derivatives cannot be offset in the statement of financial position since their conditions are not identical (e.g. different terms or currency underlyings).

Collateral In addition to the netting agreements, pbb Group also enters into collateral agreements to hedge the net receivables and net liabilities arising following offsetting using the netting agreements (collateral received or pledged). The collateral used is primarily cash collateral; however, securities are sometimes also used by way of title transfer. The collateral agreements likewise cannot be offset against the derivatives.

Netting of financial instruments as of 31 December 2013 in € billion	Gross carrying amounts of recognised financial assets/liabilities	Gross carrying amounts of the items offset in the statement of financial position	Net amounts presented in the statement of financial position	Rights of set-off that did not lead to an offsetting in the statement of financial position	Received respectively pledged collaterals	Remaining net amount
Financial assets	**6.2**	**–**	**6.2**	**4.4**	**1.4**	**0.4**
Positive fair values of derivatives	6.2	–	6.2	4.4	1.4	0.4
Financial liabilities	**5.9**	**–**	**5.9**	**4.4**	**1.4**	**0.1**
Negative fair values of derivatives	5.9	–	5.9	4.4	1.4	0.1

Netting of financial instruments as of 31 December 2012 in € billion	Gross carrying amounts of recognised financial assets/liabilities	Gross carrying amounts of the items offset in the statement of financial position	Net amounts presented in the statement of financial position	Rights of set-off that did not lead to an offsetting in the statement of financial position	Received respectively pledged collaterals	Remaining net amount
Financial assets	**10.1**	**–**	**10.1**	**6.5**	**2.8**	**0.8**
Positive fair values of derivatives	10.1	–	10.1	6.5	2.8	0.8
Financial liabilities	**9.4**	**–**	**9.4**	**6.5**	**2.4**	**0.5**
Negative fair values of derivatives	9.4	–	9.4	6.5	2.4	0.5

Other Notes

76 Contingent Liabilities and Other Commitments

Contingent liabilities and other commitments in € million	31.12.2013	31.12.2012
Contingent liabilities	**25**	**75**
Guarantees and indemnity agreements	25	75
Loan guarantees	4	4
Performance guarantees and indemnities	21	71
Other commitments	**2,569**	**1,035**
Irrevocable loan commitments	2,569	1,035
Book credits	–	102
Guarantees	30	31
Mortgage and public sector loans	2,539	902
Total	**2,594**	**1,110**

The former Hypo Real Estate Bank International AG, a predecessor institute of pbb, Munich, has overtaken with the announcement as of 2 January 2006 irrevocable and unconditional guarantees to fulfil all liabilities of Hypo Public Finance Bank puc, Dublin. By the fact that all shares of Hypo Public Finance Bank puc, Dublin, were sold, the commitment was limited according to the guarantee contract to all liabilities, which existed until the date of sale. Due to the current development in earnings, assets and financial position as well as the expected future development, pbb does not rule out the default of Hypo Public Finance Bank puc, Dublin, but a default should be rather unlikely.

In accordance with the framework agreement for transferring risk positions and non-strategic operations to a deconsolidated environment constituted under federal law in accordance with Section 8a of Finanzmarktstabilisierungsfondsgesetz pbb assumes joint and several liability for all payment obligations of its subsidiaries resulting from the transaction agreements which have been transferred as part of the process of transferring assets to FMS Wertmanagement.

The Restructuring Fund Ordinance specifies an additional charge for the so-called bank levy. The difference between the actually determined bank levy and the calculated standard amount for the years 2011 to 2019 can be subsequently charged in the following two years in each case. However, the obligation to pay the additional amount arises only if corresponding profits are generated in subsequent financial years; the amount of this payment is capped by the feasibility or charge specified in the ordinance. Whether the additional payment becomes due, and also the extent of such an additional payment, accordingly depend on profits being generated in subsequent years. The additional payment which pbb can be charged in 2014 and 2015 is €3 million. The additional payment of €32 million from previous years cannot be charged anymore according to transitional regulations to the Restructuring Fund Ordinance.

Due to a requirement in line with the principle of burden sharing required by the EU Commission, profits will be retained at pbb Group until reprivatisation, and will be used for repaying the silent participation of the Federal Republic of Germany.

pbb Group is a lessor of operating lease agreements. Non-terminable operating lease agreements for land and buildings as well as for operating and business equipment existed as of 31 December 2013. The minimum obligations arising from non-terminable leasing arrangements will result in expenses of €−11 million in 2014, €−36 million in total in the years 2015 to 2018 and €−31 million in total for 2019 and beyond. In the previous year the non-terminable operating lease agreements were as follows: for financial year 2013: €−14 million, in financial years 2014 to 2017 €−32 million in total and for 2018 and beyond €−35 million in total. Operating lease agreements were made on an arm's-length basis and are mainly related to the rental of land and buildings. The agreements include partial renewal options that the lease can be extended for several periods, and escalation clauses in the form of stepped rents or indexation clauses and release clauses as well.

For pbb Group irrevocable loan commitments form the largest part of other commitments. Irrevocable loan commitments comprise all commitments of a creditor which can grant a loan and advance at a later date and which can cause a credit risk. These are mainly credit commitments which are not fully drawn.

77 Key Regulatory Capital Ratios (Based on German Commercial Code)

In accordance with the waiver rule set out in section 2 a of the Kreditwesengesetz (KWG – German Banking Act), pbb is exempted from having to calculate equity and Tier 1 capital ratios at the level of the institution.

The waiver regulation set out in Section 2 a KWG states that a credit institution or financial services institution which has its registered offices within Germany and which is part of a regulated group of institutions or financial holding group does not have to comply with the following regulations if these regulations are complied with at the level of the ultimate parent company:

> Regulations regarding solvency (equity in relation to risk-weighted assets)
> Regulations regarding large loans (equity in relation to loans extended to individual borrower units)
> Regulations set out in Section 25 a (1) Sentense 3 No. 1 KWG for establishing and assuring risk-bearing capacity, defining strategies, setting up processes for identifying, assessing, managing, monitoring and communicating risks.

The pbb Group voluntarily discloses these figures on a pro forma basis.

pbb Group's regulatory capital in accordance with the Solvabilitätsverordnung (SolvV – German Solvency Regulation) is as follows:

Own funds[1] in € million	31.12.2013	31.12.2012
Core capital (Tier I)	2,825	2,898
Supplementary capital (Tier II)	835	1,179
Equity capital	**3,660**	4,077
Tier III capital	–	–
Total	**3,660**	4,077

[1] Consolidated in accordance with section 10 a of the KWG; pro forma in accordance with the prepared annual financial statements and following the appropriation of net profit

The risk-weighted assets, the operational risks and the market risk positions are as follows:

Risk-weighted assets[1] in € billion	**31.12.2013**	**31.12.2012**
Risk-weighted assets	14.1	15.3

[1] Including weighted credit risk positions and capital charges for market risk positions and operational risk, using a scaling factor of 12.5; according to Basel II advanced IRB approach for authorised portfolios, otherwise Basel II standardised approach; pro forma in accordance with the prepared annual financial statements and following the appropriation of net profit

Operational risks in € million	**31.12.2013**	**31.12.2012**
Total	74	86

Market risk positions in € million	**31.12.2013**	**31.12.2012**
Currency risks	6	6
Interest rate risks	–	–
Total	**6**	**6**

The capital ratios were calculated on the basis of the definition of equity given in the SolvV and using risk-weighted assets in accordance with Basel II and are as follows:

Key capital ratios[1] in %	**31.12.2013**	**31.12.2012**
Tier 1 capital ratio[2]	20.1	18.9
Equity capital ratio[3]	26.1	26.7
Own funds ratio (overall indicator)[2]	26.0	26.6

[1] Pro forma in accordance with the prepared annual financial statements and following the appropriation of net profit
[2] Including weighted credit risk positions and capital charges for market risk positions and operational risk, using a scaling factor of 12.5
[3] Including weighted credit risk positions and capital charges for operational risk, using a scaling factor of 12.5

78 Group Auditors' Fee

Group auditors' fee in € thousand	2013	2012
Audit	2,584	2,948
Other assurance services	632	611
Tax advisory services	2	2
Other non-audit services	3,193	4,291
Total	**6,411**	**7,852**

The table shows fees to the group auditor KPMG AG Wirtschaftsprüfungsgesellschaft.

79 Relationship with Related Parties

According to IAS 24 (Related-Party Disclosures), a party is related to an entity if, directly or indirectly through one or more intermediaries, the party controls or is controlled by the reporting entity, has an interest in the entity that gives it significant influence over the entity or has joint control over the entity as well as associates and joint ventures. In addition, retirement benefit schemes for post-employment benefits for employees are also included under related parties.

Transactions with related entities or persons were performed on an arm's-length basis under consideration of the characteristics of section 311 et seq. AktG (German Stock Corporation Act). In accordance with Section 7 d FMStBG, the regulations of the Aktiengesetz (Stock Corporation Act) regarding controlling entities are not applicable to Finanzmarktstabilisierungsfonds-FMS, central government and the corporations, institutions and special funds established by central government as well as related persons or other companies which are directly or indirectly dependent on them. This is not applicable for the application of regulations regarding the representation of employees in the supervisory board of a company controlled by Finanzmarktstabilisierungsfonds-FMS. According to IAS 24.25, pbb Group is exempted from the requirement of reporting on events, receivables and liabilities including obligations with related parties in accordance with IAS 24.18 if these parties are also controlled by the Federal Republic of Germany or if the Federal Republic of Germany is involved in the joint management of such related parties or if it has a material influence over such parties.

Related Entities Finanzmarktstabilisierungsfonds-FMS, a special fund of the federal government in accordance with Section 2 (2) FMStFG, represents the ultimate parent entity of HRE Holding and thus also of pbb. Accordingly, pbb is a government-related entity and a related party to other companies which are controlled, jointly controlled or significantly influenced by the Federal Republic of Germany. In addition to the parent entity HRE Holding and the affiliated company DEPFA FMS Wertmanagement is also controlled by the Federal Republic of Germany and is thus a related party of pbb Group. In the year 2013, pbb Group reimbursed Finanzmarktstabilisierungsfonds-FMS no expenses (excluding bank levy) (2012: € 0 million).

There were no loans and advances (netted by liabilities) of pbb Group to its parent company HRE Holding as of 31 December 2013 and as of 31 December 2012. As of 31 December 2013, HRE Holding held financial investments of pbb Group amounting to € 0.8 billion (2012: € 0.8 billion). The net interest income of pbb Group to HRE Holding amounted to €–12 million (2012: €–2 million). A balance of € 5 million in other operating income/expenses (2012: € 5 million) resulted from the transfer of employees to HRE Holding and € 1 million (2012: € 2 million) is attributable to IT services for HRE Holding.

pbb Group had loans and advances (netted by liabilities) to its fellow subsidiary DEPFA of €0.2 billion as of 31 December 2013 (2012: €0.2 billion) and subordinated liabilities of €0.3 billion (2012: €0.3 billion). In the financial year 2013 pbb Group realised a net interest income of €−38 million (2012: €−43 million) and a net commission income of €0 million (2012: €2 million) to DEPFA. The net income from IT services provided to DEPFA was €36 million (2012: €40 million).

There were no business relationships with the fellow subsidiary Hypo Real Estate Finance B.V. i.L., Amsterdam in the years 2013 and 2012. Besides, assets and liabilities did not exist.

As of 31 December 2013, loans and advances to non-consolidated companies amounted to €0 million (2012: €1 million); the liabilties amounted to €0 million (2012: €0 million). Loans and advances to associated companies which were not measured with the equity method amounted to €41 million (2012: €43 million), whereas the liabilities were at €0 million (2012: €0 million).

The following major transactions with FMS Wertmanagement affected the development in assets and the financial position of pbb Group:

> pbb Group has transferred market risks to FMS Wertmanagement by means of back-to-back derivatives. Overall, the transfer has had the effect of boosting the balance sheet by €0.0 billion in the position trading assets (2012: €1.0 billion).

> The carrying amount of securities which were issued by FMS Wertmanagement declined from €2.2 billion as of 31 December 2012 to €0.0 billion as of 31 December 2013. These securities are disclosed as financial investments.

> Since 16 September 2013, pbb Group has no longer invested excess liquidity for FMS Wertmanagement with the central bank (2012: €0.5 billion). This resulted in a corresponding reduction in the loans and advances to other banks and liabilities to customers' balance sheet items.

> Mortgage loans were synthetically transferred to FMS Wertmanagement with effect from 1 October 2010 to transfer the economic risk, but remained in pbb's cover pool on the balance sheet. The obligation to transfer the resulting cash flows gave rise to a liability to FMS Wertmanagement in the same amount. These loans were transferred to FMS Wertmanagement and derecognised from the balance sheet in August 2013, at which point they had a carrying amount of €6.4 billion (2012: €7.5 billion). As a result, the loans and advances to customers and other liabilities balance sheet items declined.

The development in assets and liabilities resulted in effects with FMS Wertmanagement which were recognised in profit or loss. However, because these effects were almost completely cancelled out by the corresponding market transactions, they had only an immaterial impact on profit or loss. The only material effect in the income statement resulted from servicing for the ongoing operations of FMS Wertmanagement. The balance of other operating income/expenses of €60 million (2012: €106 million) compensated for the expenses which were incurred by pbb Group for servicing. The servicing discontinuated to a large extend as mandated by the the European Commission on 30 September 2013.

All further transactions carried out in the current financial year and in the previous period with companies, which were controlled, jointly controlled or significantly influenced by the Federal Republic of Germany, related to operational business, and overall were immaterial for pbb Group.

On 31 December 2013 liabilities to defined contribution plans amounted to €3 million (2012: €3 million).

Related Persons pbb Group defines related persons as the Management Board, the Supervisory Board, employees in the second tier of management at pbb as well as members of management of the subsidiaries of pbb as well as their respective close relatives. pbb paid neither fixed remuneration nor severance payments to the Management Board during the financial years 2013 and 2012. For 2013, the total remuneration paid to former members of the Management Board and their surviving dependants amounted to €5,173 thousand (2012: €5,133 thousand). The Supervisory Board remuneration for the reporting period amounted to € 100 thousand (2012: €84 thousand). This figure was composed exclusively of fixed remuneration. There were no receivables to related persons from loans or advanves at balance sheet date.

Vested remuneration paid to persons with key function in the Group (Senior Management)[1]			**2013**	**2012**
in € thousand	Remuneration[2]	Severance payments	**Total**	**Total**
Total	6,858	–	**6,858**	**9,121**

[1] Members of the second management level of pbb and managing directors of subsidiaries of pbb
[2] Reporting follows the so-called vested principle. The components of compensation which were vested in the relevant period 2013 are reported

Pension obligations to persons with key function in pbb Group (Senior Management) in € thousand	**31.12.2013**	**31.12.2012**
Total[1]	73,963	77,552

[1] Thereof €63,404 thousand (2012: €67,434 thousand) for pensioners and surviving dependants

Statement according to section 15a WpHG During the complete financial years 2013 and 2012 HRE Holding held all shares of pbb. Hence, members of the Management Board and the Supervisory Board did not hold shares of the Company as at 31 December 2013 and as at 31 December 2012. In the years 2013 and 2012 no shares or share derivatives of pbb were purchased or sold by members of the Management Board and the Supervisory Board.

80 Employees

Average number of employees	**2013**	**2012**
Employees (excluding apprentices)	960	1,042
thereof: senior staff in Germany	17	20
Total	**960**	**1,042**

81 Members of the Supervisory Board and of the Management Board

Supervisory Board of pbb
as of 31 December 2013

			Function in the Committees of the Supervisory Board	
Name and place of residence	Principal activity	Function in the Supervisory Board	Audit Committee	Risk Management and Liquidity Strategy Committee
Dr. Bernd Thiemann Münster	Former Chairman of the Management Board of DG Bank AG	Chairman	Member	Member
Dagmar Kollmann Vienna	Entrepreneur	Deputy Chairperson	Chairperson	Member
Dr. Günther Bräunig Frankfurt/Main	Member of the Management Board of KfW	Member	Member	Chairman
Dr. Christian Gebauer-Rochholz Hochheim	Bank employee	Workers' Council Representative		
Dr. Alexander Groß Teltow	Head of the Economic Policy department in the Bundesministerium für Wirtschaft und Energie	Member		
Georg Kordick Poing	Bank employee	Workers' Council Representative		
Dr. Ludger Schuknecht Frankfurt/Main	Director General for economic and fiscal policy strategy; international economy and finance in the Bundesministerium der Finanzen	Member		
Heike Theißing Munich	Bank employee	Workers' Council Representative		
Dr. Hedda von Wedel Andernach	President of the Bundesrechnungshof, retired	Member	Member	

Management Board of pbb
as of 31 December 2013

Name and place of residence	Function in the Management Board	Mandates held in Supervisory Bodies under the Respective Law for Major Corporations
Manuela Better Munich	CEO/CRO	> Non-executive Director of DEPFA Bank plc > Non-executive Director of DEPFA ACS Bank > Non-executive Director of Hypo Public Finance Bank
Wolfgang Groth Tawern	Treasury/Asset Management	> Non-executive Director of DEPFA Bank plc > Chairman and Non-executive Director of Hypo Public Finance Bank
Dr. Bernhard Scholz Regensburg	Real Estate Finance/Public Investment Finance	
Alexander von Uslar Gruenwald	CFO/COO	> Non-executive Director of DEPFA Bank plc > Non-executive Director of DEPFA ACS Bank

82 Holdings of pbb

Holdings of pbb as of 31 December 2013
Additional statement according to HGB

	Interest in %				
Name and place of business	Total Sec 16 (4) Aktiengesetz	of which held indirectly	Currency	Equity in thousands	Net income/loss in thousands
Subsidiaries					
Consolidated subsidiaries					
Hayabusa Godo Kaisha, Tokyo	100.00	100.00	JPY	–243,846	–148,386
House of Europe Funding I Ltd.[1], George Town	–	–	EUR	1	–
Hypo Real Estate Capital India Corp. Private Ltd. i.L., Mumbai	100.00	–	INR	19,632	–154
Hypo Real Estate Capital Japan Corp., Tokyo	100.00	–	JPY	30,603,480	68,458
Hypo Real Estate International LLC I, Wilmington	100.00	–	EUR	–232,755	36,750
Hypo Real Estate International Trust I, Wilmington	100.00	–	EUR	–232,700	36,750
IMMO Immobilien Management GmbH & Co. KG, Munich	100.00	–	EUR	1,234	–1,893
Ragnarök Vermögensverwaltung AG & Co. KG[2], Munich	100.00	6.00	EUR	1,224	–2,644
RPPSE Espacio Oviedo S.L.U.[1], Madrid	–	–	EUR	–42,912	–25,732
Non-consolidated subsidiaries					
DEPFA Finance N.V., Amsterdam	100.00	–	EUR	5,326	485
GfI-Gesellschaft für Immobilienentwicklung und -verwaltung mbH i.L., Stuttgart	100.00	–	EUR	10	–
Immo Immobilien Management Beteiligungsgesellschaft mbH, Munich	100.00	–	EUR	29	–3
IMMO Invest Real Estate GmbH[3], Munich	100.00	–	EUR	28	–41
Associated companies					
SANO Grundstücks-Vermietungsgesellschaft mbH & Co. Objekt Dresden KG, Düsseldorf	33.33	–	EUR	–3,876	504
SOMA Grundstücks-Vermietungsgesellschaft mbH & Co. Objekt Darmstadt KG, Düsseldorf	33.33	–	EUR	–10,230	31
WISUS Beteiligungs GmbH & Co. Zweite Vermietungs-KG, Munich	33.00	–	EUR	–2,266	271

[1] Special-purpose entity without capital investment consolidated according to SIC-12
[2] General partner liability (Komplementärhaftung) of pbb
[3] Profit transfer by shareholders on the basis of profit and loss transfer agreement

Exchange rates € 1 corresponds to		31.12.2013
India	INR	85.3660
Japan	JPY	144.7200

Munich, 18 March 2014

Deutsche Pfandbriefbank Aktiengesellschaft
The Management Board

Manuela Better

Wolfgang Groth

Andreas Schenk

Dr. Bernhard Scholz

Alexander von Uslar

Responsibility Statement

To the best of our knowledge, and in accordance with the applicable reporting principles, the consolidated financial statements give a true and fair view of the assets, liabilities, financial position and profit or loss of the Group, and the Group management report includes a fair review of the development and performance of the business and the position of the Group, together with a description of the material opportunities and risks associated with the expected development of the Group.

Munich, 18 March 2014

Deutsche Pfandbriefbank Aktiengesellschaft
The Management Board

Manuela Better

Wolfgang Groth

Andreas Schenk

Dr. Bernhard Scholz

Alexander von Uslar

Auditor's Report

We have audited the consolidated financial statements prepared by the Deutsche Pfandbriefbank AG, Munich, comprising consolidated statement of financial position, consolidated income statement, consolidated statement of comprehensive income, consolidated statement of changes in equity, consolidated statement of cash flows and notes, together with the Group management report for the financial year from 1 January to 31 December 2013. The preparation of the consolidated financial statements and the Group management report in accordance with IFRSs, as adopted by the EU, and the additional requirements of German commercial law pursuant to § 315 a Abs. 1 HGB [Handelsgesetzbuch «German Commercial Code»] are the responsibility of the parent company's management. Our responsibility is to express an opinion on the consolidated financial statements and on the Group management report based on our audit.

We conducted our audit of the consolidated financial statements in accordance with § 317 HGB [Handelsgesetzbuch «German Commercial Code»] and German generally accepted standards for the audit of financial statements promulgated by the Institut der Wirtschaftsprüfer [Institute of Public Auditors in Germany] (IDW). Those standards require that we plan and perform the audit such that misstatements materially affecting the presentation of the development in assets, financial position and earnings in the consolidated financial statements in accordance with the applicable financial reporting framework and in the Group management report are detected with reasonable assurance. Knowledge of the business activities and the economic and legal environment of the Group and expectations as to possible misstatements are taken into account in the determination of audit procedures. The effectiveness of the accounting-related internal control system and the evidence supporting the disclosures in the consolidated financial statements and the Group management report are examined primarily on a test basis within the framework of the audit. The audit includes assessing the annual financial statements of those entities included in consolidation, the determination of entities to be included in consolidation, the accounting and consolidation principles used and significant estimates made by management, as well as evaluating the overall presentation of the consolidated financial statements and Group management report. We believe that our audit provides a reasonable basis for our opinion.

Our audit has not led to any reservations.

In our opinion, based on the findings of our audit, the consolidated financial statements comply with IFRSs, as adopted by the EU, the additional requirements of German commercial law pursuant to § 15 a Abs. 1 HGB and give a true and fair view of the development in assets, financial position and earnings of the Group in accordance with these requirements. The Group management report is consistent with the consolidated financial statements and as a whole provides a suitable view of the Group's position and suitably presents the opportunities and risks of future development.

Munich, 19 March 2014

KPMG AG
Wirtschaftsprüfungsgesellschaft
[original German version signed by:]

Wiechens Wirtschaftsprüfer [German Public Auditor]	Schmidt Wirtschaftsprüferin [German Public Auditor]

Summary of Quarterly Financial Data

pbb Group	2012	2013			
in € million	4th quarter	1st quarter	2nd quarter	3rd quarter	4th quarter
Operating performance					
Operating revenues	114	101	113	155	113
Net interest income and similar income	74	79	74	79	87
Net commission income	3	1	1	3	4
Net trading income	11	−12	10	−51	2
Net income from financial investments	2	1	–	97	-2
Net income from hedge relationships	−6	–	4	3	2
Balance of other operating income/expenses	30	32	24	24	20
Provisions for losses on loans and advances	6	4	−3	−9	–
General administrative expenses	−88	−76	−80	−84	−72
Balance of other income/expenses	−8	–	1	–	2
Pre-tax profit/loss	24	29	31	62	43

Real Estate Finance	2012	2013			
in € million	4th quarter	1st quarter	2nd quarter	3rd quarter	4th quarter
Operating performance					
Operating revenues	68	57	66	140	71
Net interest income and similar income	62	59	58	60	63
Net commission income	3	1	2	3	4
Net trading income	3	−5	4	−19	−1
Net income from financial investments	4	–	1	93	2
Net income from hedge relationships	−2	–	2	1	1
Balance of other operating income/expenses	−2	2	−1	2	2
Provisions for losses on loans and advances	6	4	−4	-9	8
General administrative expenses	−36	−34	−32	−39	−42
Balance of other income/expenses	−4	–	1	–	1
Pre-tax profit/loss	34	27	31	92	38

Public Sector Finance	2012				2013
in € million	4th quarter	1st quarter	2nd quarter	3rd quarter	4th quarter
Operating performance					
Operating revenues	15	8	12	−13	21
Net interest income and similar income	15	16	13	14	19
Net commission income	1	–	–	–	–
Net trading income	8	−7	6	−32	3
Net income from financial investments	−1	1	−1	4	−4
Net income from hedge relationships	−4	–	2	2	1
Balance of other operating income/expenses	−4	−2	−8	−1	2
Provisions for losses on loans and advances	−2	–	1	–	−8
General administrative expenses	−14	−12	−12	−14	−16
Balance of other income/expenses	−1	–	–	–	1
Pre-tax profit/loss	−2	−4	1	−27	−2

Value Portfolio	2012				2013
in € million	4th quarter	1st quarter	2nd quarter	3rd quarter	4th quarter
Operating performance					
Operating revenues	28	32	32	21	17
Net interest income and similar income	−6	–	–	–	–
Net commission income	−1	–	–	–	–
Net trading income	–	–	–	–	–
Net income from financial investments	−1	–	–	–	–
Net income from hedge relationships	–	–	–	–	–
Balance of other operating income/expenses	36	32	32	21	17
Provisions for losses on loans and advances	2	–	–	–	–
General administrative expenses	−38	−30	−36	−30	−15
Balance of other income/expenses	−3	–	–	–	–
Pre-tax profit/loss	−11	2	−4	-9	2

Consolidation & Adjustments	2012				2013
in € million	4th quarter	1st quarter	2nd quarter	3rd quarter	4th quarter
Operating performance					
Operating revenues	3	4	3	7	4
Net interest income and similar income	3	4	3	5	5
Net commission income	–	–	–1	–	–
Net trading income	–	–	–	–	–
Net income from financial investments	–	–	–	–	–
Net income from hedge relationships	–	–	–	–	–
Balance of other operating income/expenses	–	–	1	2	–1
Provisions for losses on loans and advances	–	–	–	–	–
General administrative expenses	–	–	–	–1	1
Balance of other income/expenses	–	–	–	–	–
Pre-tax profit/loss	3	4	3	6	5

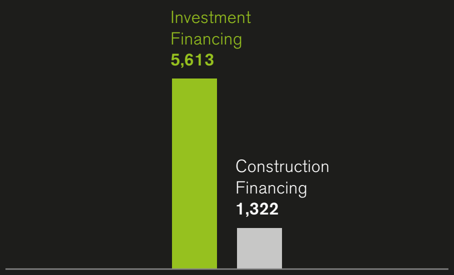
London Office Portfolio/Shopping Centre and Retail Park in Corby

€ 120 million

Investment financing
United Kingdom
December 2013

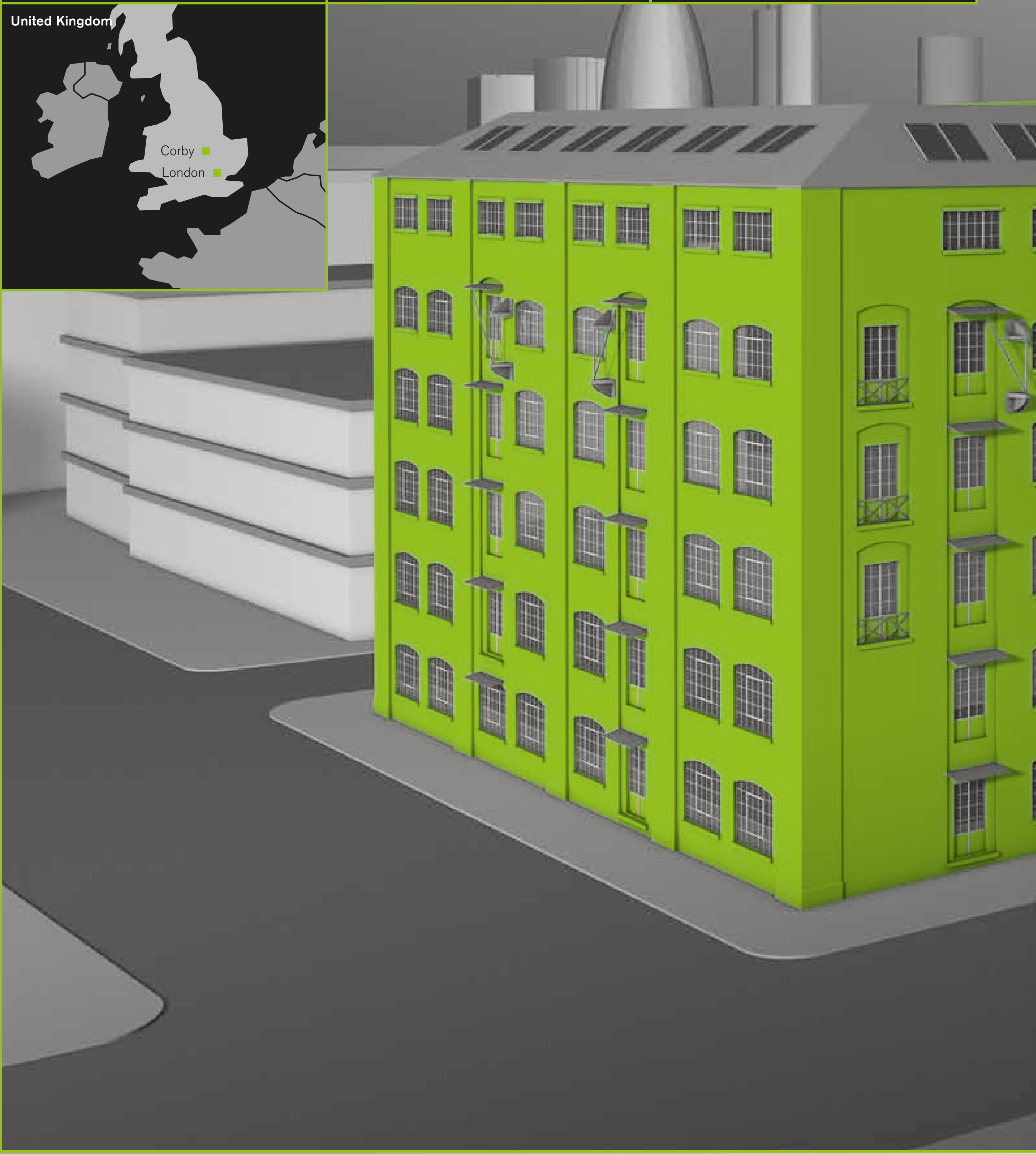
The metropolitan region of London is pbb's largest sub-market. After Munich, the company has here its largest sales team and provides services for customers with cross-border activities. The majority of real estate finance business in London relates to office buildings. At the end of 2013, Helical Bar refinanced three office buildings in London as well as a shopping centre and retail park owned by Corby with funding from pbb. Helical Bar will partly use the pbb's funding to renovate one of the offices and extend the shopping centre. Such development components often form part of financing transactions.

Real Estate Finance: new business by type of loan
Commitments in € million



United Kingdom

Corby
London



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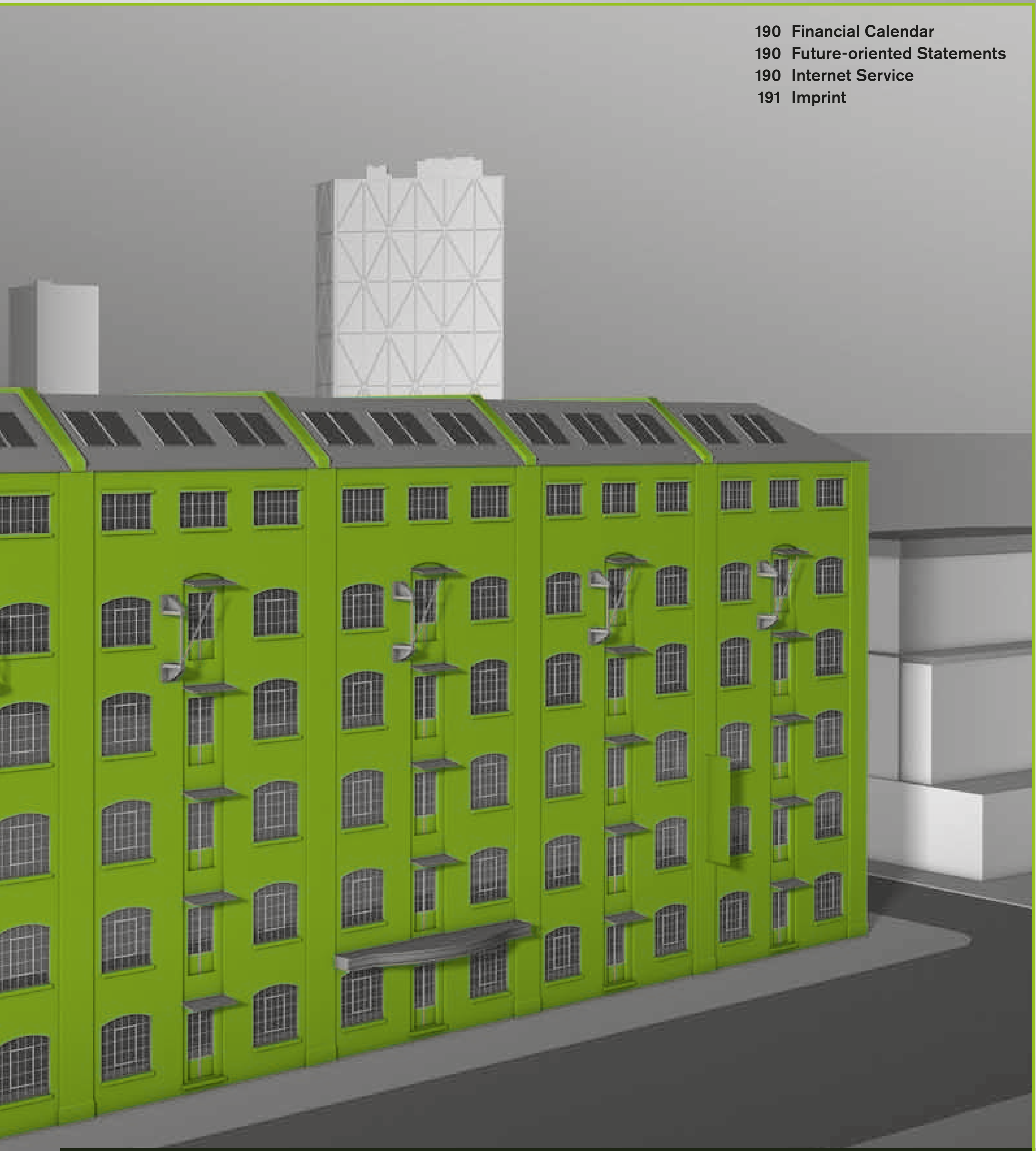

Additional Information

Financial Calendar
Future-oriented Statements
Internet Service

Financial calendar	
10 March 2014	Preliminary Annual Results 2013
3 April 2014	Annual Report 2013
2 June 2014	Q1 Results 2014
14 August 2014	Q2 Results 2014
14 November 2014	Q2 Results 2014

Future-oriented Statements

This report contains future-oriented statements in the form of intentions, assumptions, expectations or forecasts. These statements are based on the plans, estimates and predictions currently available to the management of Deutsche Pfandbriefbank AG. Future-oriented statements therefore only apply on the day on which they are made. We do not undertake any obligation to update such statements in light of new information or future events. By their nature, future-oriented statements contain risks and factors of uncertainty. A number of important factors can contribute to actual results deviating considerably from future-oriented statements. Such factors include the condition of the financial markets in Germany, Europe and the USA, the possible default of borrowers or counterparties of trading companies, the reliability of our principles, procedures and methods for risk management as well as other risks associated with our business activity.

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