NATIONAL-BANK
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ANNUAL REPORT 2018

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ANNUAL FINANCIAL STATEMENTS

Statement of Financial Position

ANNUAL STATEMENT OF FINANCIAL POSITION DECEMBER 31, 2018 OF NATIONAL-BANK AKTIENGESELLSCHAFT

IN €

Assets	12/31/2018	12/31/2017
Cash reserve	**691,248,173.22**	**725,143,902.55**
a) Cash on hand	13,461,449.52	14,049,331.05
b) Balances with central banks	677,786,723.70	711,094,571.50
including:		
At the German Federal Bank	677,786,723.70	711,094,571.50
Receivables from banks	**65,710,551.47**	**35,508,281.47**
a) On demand	44,661,522.13	34,610,849.88
b) Other receivables	21,049,029.34	897,431.59
Receivables from customers	**3,283,716,288.43**	**3,166,976,496.85**
including:		
Secured by mortgages	1,403,203,508.89	1,450,869,155.09
Communal loans	36,565,109.26	46,744,422.06
Bonds and other fixed-income securities	**523,028,803.58**	**525,351,925.08**
a) Bonds and notes	523,028,803.58	525,351,925.08
aa) Public issues	244,367,977.93	324,671,260.78
including:		
Eligible as collateral for borrowings from German Federal Bank [Deutsche Bundesbank]	244,367,977.93	324,671,260.78
ab) Other issuers	278,660,825.65	200,680,664.30
including:		
Eligible as collateral for borrowings from German Federal Bank [Deutsche Bundesbank]	199,730,295.54	198,179,047.84
Shares and other non-fixed interest securities	**90,642.21**	**308,044.33**
Equity investments	**448,086.45**	**504,400.21**
including:		
Investments in banks	11,877.31	11,877.31
Shares in financial institutions	(-)	(-)
Shares in affiliated companies	**413,833.42**	**413,833.42**
including:		
Investments in banks	(-)	(-)
Shares in financial institutions	251,929.84	251,929.84
Trust assets	**1,132.12**	**3,918.75**
including:		
Trust loans	1,132.12	3,918.75
Intangible assets	**2,235,964.17**	**2,273,878.70**
Purchased concessions, industrial property and similar rights and assets, and licenses in such rights	2,235,964.17	2,273,878.70
Tangible assets	**57,398,614.86**	**56,377,546.19**
Other assets	**16,317,038.78**	**5,246,580.89**
Prepaid expenses	**2,821,988.26**	**3,995,873.59**
Excess of plan assets over pension liabilities	**995,157.00**	**654,667.00**
Total assets	**4,644,426,273.97**	**4,522,759,349.03**

ANNUAL STATEMENT OF FINANCIAL POSITION DECEMBER 31, 2018 OF NATIONAL-BANK AKTIENGESELLSCHAFT

IN €

Liabilities	**12/31/2018**	**12/31/2017**
Liabilities to banks	**447,082,336.87**	**452,040,132.94**
a) On demand	9,417,203.65	14,909,943.91
b) With agreed maturity or periods of notice	437,665,133.22	437,130,189.03
Liabilities to customers	**3,757,358,436.98**	**3,622,107,949.33**
a) Savings deposits	248,672,449.47	260,105,219.14
aa) Redeemable at a period of notice of three months	246,471,177.78	257,268,894.62
ab) Redeemable at a period of notice of more than three months	2,201,271.69	2,836,324.52
b) Other liabilities	3,508,685,987.51	3,362,002,730.19
ba) On demand	2,969,706,633.18	3,016,719,914.39
bb) With agreed maturity or periods of notice	538,979,354.33	345,282,815.80
Securitized liabilities	**5,112.92**	**5,112.92**
a) Bonds issued	5,112.92	5,112.92
Trust liabilities	**1,132.12**	**3,918.75**
including:		
Trust loans	1,132.12	3,918.75
Other liabilities	**4,414,400.88**	**4,665,976.84**
Prepaid expenses	**2,751,383.36**	**3,415,270.01**
Provisions	**76,079,961.92**	**86,484,250.71**
a) Provisions for retirement pensions and similar obligations	61,755,448.47	56,502,101.29
b) Provisions for taxes	0.00	11,099,684.62
c) Other provisions	14,324,513.45	18,882,464.80
Subordinated liabilities	**10,470,890.41**	**10,470,890.41**
Fund for general banking risks	**15,500,000.00**	**15,000,000.00**
including: Special item pursuant to Section 340e of the German Commercial Code [HGB]	0.00	0.00
Equity capital	**330,762,618.51**	**328,565,847.12**
a) Called capital		
Subscribed capital	39,817,866.00	39,936,000.00
including: Purchased treasury shares	-118,134.00	0.00
b) Capital reserves	163,301,864.98	163,100,090.94
c) Retained earnings	116,993,287.53	114,880,156.18
ca) Legal reserves	990,883.67	990,883.67
cb) Other retained earnings	116,002,403.86	113,889,272.51
d) Net retained profits	10,649,600.00	10,649,600.00
Total liabilities	**4,644,426,273.97**	**4,522,759,349.03**

	12/31/2018	**12/31/2017**
Contingent liabilities	**97,444,013.35**	**88,360,469.90**
Liabilities from guarantees and warranties	97,444,013.35	88,360,469.90
Other liabilities	**425,415,598.94**	**416,527,917.80**
Irrevocable loan commitments	425,415,598.94	416,527,917.80

Income Statement

INCOME STATEMENT FOR THE PERIOD FROM JANUARY 1 TO DECEMBER 31, 2018 OF NATIONAL-BANK AKTIENGESELLSCHAFT

IN €

Expenses	**2018**	**2017**
Interest expenses	**12,582,455.96**	**15,509,075.58**
including:		
Negative interest from liabilities	638,951.45	320,247.45
Commission expenses	**4,157,425.74**	**3,741,329.89**
General administrative expenses	**89,494,079.35**	**89,243,267.42**
a) Personnel expenses	52,199,371.83	51,686,251.94
aa) Wages and salaries	42,235,646.65	42,670,282.04
ab) Social security contributions and expense for pensions and other benefits	9,963,725.18	9,015,969.90
including:		
For pensions	3,237,425.42	2,147,984.81
b) Other administrative expenses	37,294,707.52	37,557,015.48
Amortization/depreciation on and valuation allowances to intangible and tangible assets	**3,965,077.28**	**4,314,253.82**
Other operating expenses	**7,133,182.49**	**6,263,741.56**
Write-downs and allowances on receivables and certain securities and transfers to provisions for loan losses	**2,379,837.38**	**4,040,718.29**
Amortizations and write-downs and allowances on equity investments, shares in affiliated companies and securities recognized as assets	**178,880.62**	**102,116.66**
Transfers to funds for general banking risks	**500,000.00**	**3,500,000.00**
Extraordinary expenses	**1,026,865.56**	**1,026,865.56**
Taxes on income	**11,373,877.50**	**12,555,330.82**
Other taxes not disclosed in "other operating expenses"	**281,271.16**	**338,041.29**
Net Income	**13,881,066.55**	**15,892,600.00**
Total expenses	**146,954,019.59**	**156,527,340.89**

	2018	**2017**
Net Income	**13,881,066.55**	**15,892,600.00**
Transfers to retained earnings	**3,231,466.55**	**5,243,000.00**
Other retained earnings	3,231,466.55	5,243,000.00
Net retained profits	**10,649,600.00**	**10,649,600.00**

INCOME STATEMENT FOR THE PERIOD FROM JANUARY 1 TO DECEMBER 31, 2018 OF NATIONAL-BANK AKTIENGESELLSCHAFT

IN €

Income	**2018**	**2017**
Net interest income from	**95,870,186.35**	**101,757,728.73**
a) Loan and money markets transactions	95,004,554.18	100,746,008.63
b) Fixed interest securities and debt-register claims	865,632.17	1,011,720.10
including:		
Positive interest on receivables	3,277,757.84	1,912,069.76
Recurring income from	**100,331.94**	**165,179.30**
a) Shares and other non-fixed interest securities	6,736.16	4,286.12
b) Equity investments	93,595.78	160,893.18
c) Shares in affiliated companies	0.00	0.00
Commission income	**47,825.627.30**	**49,444,641.66**
Income from write-ups to equity investments, shares in affiliated companies and securities recognized as assets	**0.00**	**0.00**
Other operating income	**3,157,874.00**	**5,159,791.20**
Extraordinary income	**0.00**	**0.00**
Total income	**146,954,019.59**	**156,527,340.89**

MANAGEMENT REPORT

Fundamentals of the Company

NATIONAL-BANK (Bank) is one of the leading independent private regional banks in Germany for discerning private and corporate customers, as well as for medium-sized institutional investors. In addition to our competitive and customer group specific financial solutions, our individualized consulting and personalized services are a distinct competitive advantage. The same applies to our longstanding customer relationships, as well as the maintaining of the highest degree of customer satisfaction. Its regional core market is North Rhine-Westphalia. The Bank plans to continue to develop its defined target groups within its regional core market.

The independence of the Bank is an essential foundation for its success. The Bank's independence is to be bolstered and secured through active investor relationship measures. The objective is the creation of a sustainable shareholder structure. The Bank's objective is to generate sustainable added value for its customers, shareholders and employees. The objective is to keep the return of equity before taxes in a target range between 10 % to 15 % and a Common Equity Tier 1 capital ratio between 12 to 15 %.

The respective objective will only be achieved gradually, considering the current interest rate level and the planned increase of the loan portfolio, which is subject to minimum reserve requirements. The Management Board is willing to accept a longer transitional period, in particular if this is due to investment reasons. Overall development sustainability is also decisive in this case and not meeting individual key indicators.

The business is customer-driven. The Bank's target groups are discerning private and corporate customers. The Bank is pursuing a comprehensive consultation approach for its target groups. Private and corporate customers are discerning, if they hold competent and individualized consulting and personalized services in high regard. The same applies to the willingness to employ several financial solutions. Private and corporate customers not classified as discerning, also receive consultation based on their individual needs. In these cases, it is the Bank's objective to develop a business relationship with its customers by offering individualized financial solutions. The Bank continues to expand its collaboration with medium-sized institutional investors. Medium-sized institutional investors are comprised of foundations, regional utility companies and pension schemes, as well as smaller institutional investors.

Transactions with the target customers form our Bank's strategic areas of business in the business model. The sales organization and the sales-related i.e. profit-oriented management of the Bank are geared toward these divisions. For the purpose of internal segment reporting, additional segments have been added.

The Bank's objective is to consequently gear its financial solutions to the needs of its target customers. The Bank develops its financial solutions in-house or purchases them from independent third parties (Open Architecture). Cooperation partners are carefully selected and undergo regular reviews. The loan and deposit business is an integral component of the business model. In compliance with our business and risk strategy and the complementing credit risk strategy, loans are to be provided with the objective of having customers take advantage of the other financial solutions our Bank offers (strategic loan business). In each case, the price of the loan must cover the Bank's equity return target rate for the loan business. The Bank's objective is to optimally coordinate the sale of its financial solutions. This relates, on the one hand, to demand-oriented optimized sales within the individual divisions (cross selling), and on the other hand, to a sustainable optimized interrelationship between the service units of the individual customer segments (connectivity).

The net interest and commission income are the essential income components of the Bank. Based on their current distribution, a larger share of the overall income should continue to be generated by commission business, which does not tie up equity.

The Bank considers, in particular, savings institutions and people's banks in the Rhine/ Ruhr region, as well as major banks, and private banks in asset management business, as its main competitors. The Bank expects continuing intensive competition within its market territory from domestic and foreign major banks in the medium sized corporate business and private customer business segments.

Overall Economic Environment

In Germany, overall economic production markedly softened during 2018, the decline of important early indicators is, however, to be put into perspective against the backdrop of the prior very high reference base. The domestic economy, driven by a strong employment build-up and low interest rates, continues to be a main pillar. On the other hand, economic development was muted during the summer half year, primarily due to a phase of economic weakness in the most important German sales markets, in particular within the Eurozone. Moreover, many companies were confronted with noticeable supply-side bottlenecks, primarily as regards the labor market and intermediate goods. In addition to production losses due to strike and illness at the beginning of the year, significant problems of the German automotive industry with the certification of new vehicles arose during the summer months. A stronger production expansion was, however, also hampered by the high overall capacity utilization in conjunction with a marked shortage on the labor market and delays in the supply chains. Against the backdrop of continued sound global economic perspectives, we expect the German economic upturn to continue. Buoyant domestic demand, primarily founded on solid consumer spending remains the central pillar of economic activities. Consumer spending is not only supported by the strong rise of wages and salaries, but also, in particular, an expansive fiscal policy. The economic performance for the current year should increase by 1.6 % and as such should more or less be able to sustain the previous year's growth rate. In 2018, economic growth in Europe should still have been around 1.8 %. For the coming year, we project another slowing of growth rates to around 1.6 %. The growth rate will thereby remain above the long-term trend.

Situation and perspectives for the North Rhine Westphalia economy continue to remain solid, but the boom phase will, however, also taper off gradually in North Rhine Westphalia. At year's end, the ifo Business Climate Index for business, industry and trade in North Rhine Westphalia declined for the third consecutive time. Companies assess their business situation somewhat less positive. In addition, they assess development over the next six months more skeptical. Yet, the by far most informative economic barometer for the economic development in North Rhine Westphalia still remains above the average figure for the years since 2011. We expect, however, that the economic development in the Rhine and Ruhr region cannot decouple from the economic development pace in the Federal territory. On the other hand, the factors supporting growth throughout the federal territory are, of course, also determining factors for the economic development in North Rhine Westphalia. The business climate index reached a new record for the primary construction sector, which was primarily due to the extraordinary sound order situation. Regarding the future development, construction companies were, however, somewhat less optimistic than during the previous two months. This slight dampening of expectations must, however, be seen against the backdrop of an interest-induced longstanding boom.

With a view on the great importance the industry has for the economic development in North Rhine Westphalia, it must also be emphasized that the business climate in the manufacturing industry could even improve in spite of great global uncertainties. Industrial companies in the Rhine and Ruhr region no longer assessed, however, their business situation as good as before, but they were somewhat more optimistic for the future development. Retail was once again a relative weak point, where the climate index deteriorated more noticeable. It is to be expect that private spending, driven by continuing robust wage and salary increases and low interest rates, will continue to be the pillar for the economic activities and that for this reason the mood in retail should also improve again. Business climate also slightly cooled in wholesale. Because this decline also originated from an above average level, the perspectives for wholesale remain above average. For 2019, we expect for North Rhine Westphalia that total increases of GDP will be at the Federal level of around 1.6 % p.a.

Course of Business

2018, was again characterized by a very difficult and for the finance industry's unchanging complex environment.

In spite of these circumstances, the Bank reached a solid result in 2018. This is best expressed in the return on equity of 8.1 % (10.2 %). This result proves that the Bank's exclusively customer-driven business model, which we have been pursuing for decades, is successful even in the face of extremely low interest rates.

2018 generated a net income of € 13.9 million (€ 15.9 million). Based on this result and subject to the adoption of a corresponding resolution by the functional committees, the Bank is in a position to pay the same dividend as in the previous year of € 0.80 per share. This represents a total dividend of € 10.65 million and an additional € 3.2 million (€ 5.2 million) to the reserves.

As in the previous years, a brisk loan business was one of the Bank's business pillars. The loan business was characterized by sustained demand. In a year, in which investments decreased due to uncertainty, we were able to continue the targeted development of our business based on sound judgment. In spite of high redemptions, receivables from customers increased to € 3.3 billion as of the balance sheet date. Nonetheless, the development of the interest net income remains the Bank's greatest challenge.

After strong increases during previous years, commission income of € 43.7 million declined slightly. The favorable development is predominately the result of asset management, account and card services, as well as the hedging of interest and currency risks of our customers, in particular of the internationally active medium-sized customers.

Of particular note is the development of expenses. In spite of numerous new regulatory requirements, as well as substantial investments into infrastructure, administrative expenses declined by € 0.1 million to € 93.5 million.

Financial Performance

NET INTEREST INCOME

Net interest income decreased from € 86.4 million to € 83.4 million. This decrease by € 3.0 million is primarily the result of continuing extremely low and for banks even negative interest rates. Receivables from customers and customer deposits each increased by 3.7 %. The Bank's interest margin slightly declined as a result of new business, which was negatively affected by the low interest rates.

NET COMMISSION INCOME

After years of growth, net commission income declined for the first time as compared to the previous year by € 2.0 million to € 43.7 million. This was primarily caused by new regulatory requirements for securities trading, as well as deteriorating capital markets during the year, so that commission income from asset management declined to € 21.0 (23.2) million.

OTHER OPERATING INCOME AND EXPENSES

The negative balance from other operating income and expenses was € -4.0 (-1.1) million. The reason for this were, in particular, interest expenses for pension provisions of € 6.9 (5.6) million, which are the result of the discount rate decrease from 3.68 % to 3.21 %. These expenses were, in part, compensated by the complete or partial reversal of various provisions, which were created based on conservative assumptions.

GENERAL ADMINISTRATIVE EXPENSES

Overall, general administrative expenses were stable, in spite of manifold new regulatory requirements, as well as investments in IT infrastructure. Personnel expenses slightly rose from € 51.7 million to € 52.2 million. This was primarily caused by the adjustment of the income thresholds for contribution assessment in social security, as well as the update of the Heubeck biometric data 2018 as basis for the valuation of pension obligations. Operating expenses slightly decreased from € 37.6 million to € 37.3 million. This includes expenses for the outsourcing of data processing centers, as well as reorganization of securities processing in the amount of € 4.9 million to smoothen the operational risk profile.

DEPRECIATION OF TANGIBLE FIXED ASSETS

Depreciation of tangible fixed assets and amortization and write-downs of intangible fixed assets slightly declined from € 4.3 million to € 4.0 million as compared to the previous year.

RISK PROVISION

Expenses for risk provisions of € 2.6 million decreased compared to the previous year figure of € 4.1 million. The decrease is the result of the Bank’s conservative loan risk strategy and the positive economic development.
In lending business, we took all identifiable risks into account by creating valuation allowances on loan losses and provisions. Global valuation allowances for loan losses were created in the amount of € 0.2 (€ -0.9) million. The global valuation allowances are calculated according to the tax code and are contained in the risk provisions for loan business. Particular risk-increasing developments in the Bank’s lending portfolio have not been observed.

OPERATING PROFIT

The operating result of € 27.1 million was below the previous year’s level by € 6.3 million. Reduced gross profits could only be compensated in part by reduced expenses.

EXTRAORDINARY RESULT

From the remaining required proportionate allocation to pension provisions resulted as in the previous year an extraordinary result of € -1.0 million.

NET INCOME

Net income was € 13.9 million after € 15.9 million in the previous year. Net income decline was primarily caused by declining gross profits that could only be compensated in part by reduced expenses.

STRATEGIC KEY FIGURES

The return on equity before taxes decreased from 10.2 % to 8.1 %. Accordingly, return on equity is below the target range of 10 to 15 %. In 2017, a return on equity around the lower target range was forecast for this reporting year.

Due to the largely completed major IT projects, cost income ratio, i.e. the ratio between administrative expenses and gross profits, increased from 71.4 % to 75.9 %, which is outside the target range of 65 to 70 %. The previous year's report stated the expectation that this ratio will presumably be in the range of around 70 %. Without the cost for the major IT projects, cost income ratio would be 72.0%.

The respective objective will only be achieved gradually, considering the current interest rate level and the planned increase of the loan portfolio, which is subject to minimum reserve requirements. The Management Board is willing to accept a longer transitional period, in particular if this is due to investment reasons. Overall development sustainability is also decisive in this case and not meeting individual key indicators.

FUND FOR GENERAL BANKING RISKS

Based on reasonable business assessment, € 0.5 million were allocated to the fund for general banking risks in accordance with Section 340g German Commercial Code.

Financial Position

TOTAL ASSETS AND BUSINESS VOLUME

Total assets at € 4.6 billion (4.5 %) were slightly above the previous year's level.

REFINANCING STRUCTURE AND LIQUIDITY

The Bank predominately refinances itself through customer deposits and equity capital. Liabilities to customers were € 3.8 billion on the balance sheet date (€ 3.6 billion). This results in the Bank being largely independent of capital market refinancing.

In light of the sustained low interest rate phase, inflows of highly liquid investments in the form of demand deposits and overnight money deposits could be observed. Consequently, the share of customer deposits with a short notice period continued to increase, so that, from a legal perspective, the capital lock-up on the liability side of the balance sheet is significantly shorter than on the asset side of the balance sheet. This creates a theoretical refinancing risk. Day-to-day banking shows, however, that the short-term deposits are to a great extent available to the Bank on a permanent basis. For this reason, the Bank's liquidity management employs the concept of dynamic replication based on the "deposit base" for the modeling of a longer availability period for these deposits. The underlying model assumptions are validated annually within the scope of statistical analyses.

The Bank continues to maintain a stable and balanced financing structure, even though short-term demand deposits increased.

The Bank's liquidity situation was unchanged solid. The liquidity coverage ratio (LCR) achieved 118.0 % at year's end. The regulatory minimum requirement was 100 %. The Bank's liquidity and risk measurement and control system ensures that adequate liquidity is always available.

The refinancing facilities at the German Federal Bank are comprised of a pool of pledged assets, consisting of securities and promissory notes.

LOAN BUSINESS

In spite of moderate loan demand, new business volume could be increased to € 528 (€ 482) million. High loan repayments, for example in connection with interest rate renewal dates, negatively affected an increase in loan holdings. The willingness of borrowers to repay their loans is mainly due to low interest rates.

Receivables from customers increased by € 117 million to € 3.3 (3.2) billion. In regard to our lending portfolio control, we continued our broad diversification policy, also with a view to our risk-bearing capacity. We continued to apply strict credit rating standards to creditworthiness and collaterals to new business.

DEPOSIT BUSINESS

Liabilities to customers increased by € 0.2 billion to € 3.8 billion. Short-term demand deposits were essentially unchanged. However, time deposits and savings deposits increased in total by € 0.2 billion. This development confirms the high level of trust customers have in the Bank, in spite of the fact that the interest rates for our products were adjusted to reflect the money and capital market levels on an ongoing basis.

INTERBANK BUSINESS

Regarding liabilities to banks, the emphasis remained on long-term funding under public sector lending programs. Due to scheduled maturities and unscheduled repayments on corresponding customer loans by customers, loan holdings decreased to € 435.8 million (€ 436.0 million). On the asset side receivables from banks amounted in total to € 65.7 million (€ 35.5 million). Liquidity maintained with the German Federal Bank and other cash reserves held at the end of the reporting period totaled € 691.2 million, which is slightly below the previous year's figure of € 725.1 million. As in previous years, in 2018 the Bank made use of the money market for liquidity controlling purposes and entered into overnight and time deposit transactions with other banks. The Bank maintained a generously dimensioned collateral pool of eligible securities with the German Federal Bank in the form of liquidity reserves during the reporting year. Within liquid securities holdings, in total € 186.7 (€ 145.0) million were securities issued by financial institutions.

SECURITIES HOLDINGS

The existing investments in bonds and other fixed interest securities in the amount of € 523.0 (€ 525.4) million include investments with high credit ratings, in particular domestic government bonds, which to a large extent are eligible as collateral at the German Federal Bank. The balance sheet item "shares and other non-fixed income securities" declined from € 0.3 million to € 0.09 million.

DERIVATIVES

The bank does not trade in derivatives with the intention to generate significant profits. Financial derivative transactions are almost exclusively made to cover customer positions. The nominal volume of derivatives was in total € 1.4 billion (€ 1.4 billion). 99.0 % were related to OTC products. In addition, the Bank held € 14.9 million of publicly traded products. Broken down by business segments, a nominal volume of € 0.5 billion was attributable to currency and € 0.9 billion to interest rate related contracts, including positions to control the Bank's interest rate risk. Since transactions with customers are directly collateralized by transactions with other banks or on the stock exchange via perfect "micro hedges" and the Bank's positions serve to limit interest rate and currency risks of the bank book, the Bank's positions were virtually not exposed to any market price-dependent risks arising from financial derivatives, the Bank was only exposed to market price-dependent counterparty default risks.

FUND FOR GENERAL BANKING RISKS

During the reporting year, the fund for general banking risks was increased from € 15.0 million to € 15.5 million in accordance with reasonable commercial judgment.

EQUITY CAPITAL

Retained earnings were strengthened by an additional € 3.2 million (€ 5.2 million) from the 2018 annual result. The regulatory own funds, whose components are presented in detail in the disclosure report, amount to — including subordinated loans and the fund for general banking risks — € 356.7 million (€ 357.0 million). The Bank's own funds — measured as the ratio of regulatory relevant equity capital in terms of the Capital Requirements Regulation [CRR] to risk-weighted assets – after the approval of the annual financial statements — were 12.4 % (13.5 %). Equity Tier 1 capital ratio is 11.3 (12.2) %.

STRATEGIC KEY FIGURES

The regulatory Common Equity Tier 1 capital ratio of 11.3 (12.2) % after retention of earnings is below the target range of 12 to 15 %. In the report on expected developments 2017, it was expected that the total capital ratio would be at the lower end of the target range in 2018 and 2019.

The loan to deposit ratio should not exceed a figure of 1. This figure was 0.76 % on the balance sheet date.

EVENTS AFTER THE BALANCE SHEET DATE

No events of special importance occured after the end of the fiscal year.

PARTICIPATION OF WOMEN AND MEN IN LEADERSHIP POSITIONS

Based on the Act on the Equal Participation of Women and Men in management positions in the Private and Public Sectors of April 24, 2015, companies with more than 500 employees that are subject to the one-third co-determination at the Supervisory Board level, such as the bank, are obligated to determine target figures for an increase in the representation of women on the Supervisory Board, Management Board (Vorstand) and the top two management levels reporting to the Management Board and are to decide on a schedule according to which the target figures are to be met.

The Supervisory Board resolved that the target figure for women represented on the Supervisory Board will be one member on or before June 30, 2022. Due to the risk that a separation of the women's quota into the employer and the employee side could result in an "empty chair", such separation was not considered. This does not mean that there will be a targeted reduction of the current number of female Supervisory Board members (three of nine Supervisory Board members).

The target figure for women represented on the Management Board will be unchanged zero on or before June 30, 2022.

For the management levels reporting to the Management Board, the target quota for the first management level (division, branch and regional managers) is 10 % and 18 % for the second management level (department managers). At 6 % and 12 %, both quotas are below the target quota.
The main reason for this situation was that open management positions were filled with better qualified male applicants.

Risk and Opportunity Report

RISK STRATEGY / RISK INVENTORY

The Bank's risk management guidelines are defined in the form of a risk strategy and are published within the Bank. The risk strategy is derived from the Bank's business activities, as defined in the Bank's business strategy and their associated risks. The risk strategy forms the framework for risk type-specific sub-strategies, which in turn implements the requirements for the management of risks within the structural and process-oriented organization.

The Bank's business strategy principally only includes such business activities for which reasonable risk management has been adopted in advance in the risk strategy, including sub-strategies and which have been implemented in the Bank's structural and process-oriented organization.

From these business activities arise the following risks, which the Bank classifies as material in terms of MaRisk:

- Counterparty default risks
- Market price risks, including foreign currency risks
- Interest rate risks
- Operational risks, including legal risks and associated sub-risks and cross-sectional risks
- Liquidity risks
- Business risks and
- Reputational risks

Regarding the quantitative analysis i.e. the inclusion within the analysis of the risk capacity from an economic perspective, the following table provides the current detailed status on the reporting date as the result of the risk inventory.

RESULT OF THE RISK INVENTORY

RISK CATEGORY (1st and 2nd level)	Inclusion into the risk capacity analysis from an economic perspective
Counterparty default risks	**Yes**
Credit default risk	Via counterparty default risks
Counterparty risk	Via counterparty default risks
Issuer risk	Via counterparty default risks
Migration risk	Via spread risk
Country risk	Via counterparty default risks
investment risk	Via counterparty default risks
Market price risks	**Yes**
Price risk (share, funds and bond price risks)	Via market price risks
Credit rating risk (spread risk)	Via market price risks
Market price risk arising from commodity trades	No
Foreign exchange risk	Via market price risks
Interest rate risks	**Yes**
Interest rate risk banking business	Via interest rate risks
Business risk interest-earning operations	Via interest rate risks
Interest structure risk	Via interest rate risks
Pension risk	Via interest rate risks
Operational risks	**Yes**
Personnel risk	Via operational risks
Conduct risk	Via operational risks
General legal risk	Via operational risks
Compliance risk	Via operational risks
Fraud risk	Via operational risks
Information security risk	Via operational risks
Outsourcing risk	Via operational risks
Going concern risk	Via operational risks
Data protection risk	Via operational risks
Tax law risk	Via operational risks
Methods and model risk	Via operational risks
Lease risk	Via operational risks
Liquidity risks	**Yes**
Own illiquidity	No
Liquidity cost risk (increased refinancing cost)	Yes
Market illiquidity	Via spread risk
Business risks	**No**
Commission business	For methodological reasons no
Interest-earning operations (see above interest rate risk)	For methodological reasons no
Reputational risks	**Yes**

Initially each individual risk type is analyzed separately. The comprehensive risk capacity calculation from the economic perspective then integrates the quantitative results for counterparty default risk, market price risk, interest rate risk, operational risk, liquidity risk and the reputational risk into a standard model and subjects the risks to a stress test. A risk contribution is not determined for the business risk classified as material, because the corresponding current result is not included with the risk covering potential. Risk concentrations and interactions with the other material risk types are analyzed and assessed to determine, if controlling actions are required.

The risk management focus is to contain the material risks within the specified limits from an economic perspective for the risk capacity or to reduce such risks within the specified limit, as well as to counterbalance foreseeable unfavorable developments of risk capacity, liquidity, as well as the reputation of the Bank. The enforcement of risk-adjusted terms in the market for all business activities from which quantifiable risks for the Bank's risk-bearing capacity arise is a material principle of risk management. However, the risk situation in a market, a business segment or for a business partner may subsequently develop negatively for the bank, without the option of being able to adjust the terms accordingly. For this reason active risk management within the Bank's processes is necessary, in addition to the enforcement of reasonable terms at the conclusion of a business transaction.

The risk management implemented in the Bank's processes contains the following four basic strategies:

RISK ASSUMPTION

The assumption of risks is a prerequisite for the generation of income. The Bank pursues business, which corresponds to the business strategy and internal risk-return requirements. Principally, the Bank assumes the risks associated with these business transactions. Transactions that show an insufficient opportunity risk profile at the closing date are not completed. An insufficient opportunity risk profile exists e.g., if loans do not meet the minimum margin requirement and such insufficient margin cannot be compensated by other income from the associated customer base.

RISK REDUCTION

In the event, assumed risks for individual transactions or for a portfolio increase, the Bank may demand additional securities or enter into hedging transactions and reduce the respective business activities.

RISK TRANSFER TO THIRD PARTIES

The Bank may transfer partial risks or the entire risk to other market participants (e.g. insurances), if business transactions do not meet the Bank's risk profile requirements and risk reduction is not possible.

RISK AVOIDANCE

Business transactions with customers, whose potential risk could threaten the Bank's risk-bearing capacity, may not be entered into. This applies, in particular, to business transactions with customers, in which the monetary damage could exceed major portions of the operating profit before risk provisions minus expected losses, if such risks materialize. In addition, business activities that may damage the Bank's reputation are also to be avoided or discontinued.

OVERALL RISK POSITION / RISK-BEARING CAPACITY

The determination of risk capacity serves both, the objective of a going-concern for the institute and the protection of creditors against losses. To meet these two protection objectives, the German banking supervisory authorities expect from the institutes that they analyze two perspectives within the scope of their risk capacity concept: a normative and an economical perspective.

The normative perspective is to be understood as the regulatory requirements as a whole. The relevant controlling parameters are, in particular, the supervisory requirements

- regarding capital (Common Equity Tier 1 Capital requirement, SREP total capital requirement and the combined buffer requirement),
- regarding the own funds target key figure and
- regarding the capital structure.

For this reason, the starting point for these analyses are the regulatory key figures, as well as their calculation logic, which are all taken from the supervisory reporting system. In addition to meeting the regulatory requirements as of the reporting date, a capital planning is prepared that covers at least a period of three years and which is updated at least once a quarter. The calculation logic for future periods is also specified by the supervisory authorities. Only the parameter variation for various scenarios (plan scenario and at least one adverse scenario) may be determined by the institute.

The risk capacity analysis in the economic perspective is used to secure the substance of the institute for the long-term and as such to protect creditors against losses. Within the scope of risk capacity analysis from the economic perspective, the sum of risk contributions is compared with the risk covering potential. The risk capacity requirement is met, if the risk covering potential is at least equal to or exceeds the sum of risk contributions.

Risk capacity requirements were met throughout the reporting period. As of the reporting date, a free risk capital of € 198.6 million results from the difference between risk covering potentials of € 297.3 million and risk potentials of € 98.6 million based on the analysis from the economic perspective.

RISK-BEARING CAPACITY OVERVIEW
IN € MILLION

Internal capital supply risk covering potential (RCP)	**qualifying date**
Risk covering potential	**297.3**
internal economic capital needed risk potentials	
VaR counterparty default risk	56.8
VaR market price risks liquid securities holdings plus spread risks	8.8
VaR market price risks money market transaction plus spread risks	0.0
VaR market price risks foreign currency	0.1
Interest rate risk	27.7
Operational risks	4.9
Liquidity cost risk	0.3
Reputational Risk	0.1
Total limits / total risk position	**98.6**
Available risk capital	**198.6**

Within the scope of the risk capacity anal sis from an economic perspective a comprehensive s ess scenario simulating a severe economic downturn i conducted. In addition, stress tests are performed on naterial risk types, as well as an inverse stress test anc cross-risk stress tests based on causes originating f om the Bank and/or the market at large. The stress sce arios take risk concentrations into account.

STRUCTURE OF RISK MONITORING AND CONTROL

The Management Board is responsible for the Bank's overall risk management, specifically risk-bearing capacity, including the set limits, liquidity and the Bank's reputation. This is supported by cross-functional committees.

Relating to risks associated with the individual business activities, risk management is performed by the following organizational units:

- The management of counterparty default risks is the responsibility of Credit Risk Management — Quality Management.
- The management of the interest rate and liquidity risk is the responsibility of the Treasury department.
- The management of market price risks is the responsibility of Credit Risk Management — Quality Management.
- The management of operational risk is performed in a decentralized manner by all organizational units.
- Controlling of the business risk is the responsibility of the units managing sales.
- The management of the Bank's reputation, as well as potential reputational risks is the responsibility of all Management Board members. Operational execution is the responsibility of the reputational risk representative.

The Risk Management division / Risk Controlling department is responsible for the identification, measurement and analysis of risk potentials, as well as the determination and analysis of risk capacity from an economic perspective and has, in particular, the following responsibilities:

- Consultation of management in risk policy issues, in particular as regards the development and implementation of risk strategies and the design/implementation of a system to limit risks
- Support of management regarding risk inventory and preparation of an overall risk profile
- Responsibility for the implementation and development of risk management and risk controlling processes
- Monitoring of risk capacity and risk limit compliance from an economic perspective
- Preparation of risk reports for management
- Immediate communication of material risk-related information to management, the respective managers and, if needed, to the Internal Audit department

The head of the Risk Management division assumes the risk controlling function according to AT 4.4.1 MaRisk.

RISK CATEGORIES

To identify, assess, manage, monitor and communicate all individual risks, as well as the Bank's risk-bearing capacity, we employ and are continually enhancing a comprehensive risk management and reporting system. Regarding risk reporting, we refer to the respective segment. The handling and processing of the individual risk categories that are considered material is illustrated below.

COUNTERPARTY DEFAULT RISK

Counterparty default risk is defined as the risk that occurs when the Bank suffers a loss through the default of a counterparty with whom the bank maintains a business relationship.

In regard to the essential loan business, the counterparty default risk is defined as the risk that a borrower does not meet or only partially meets its contractually agreed obligations to make interest or redemption payments when due and in the specified amount. Regarding the issuer and counterparty business segments, the counterparty default risk is defined as the risk that the Bank suffers a loss through the default of an issuer or a counterparty with which the Bank entered into a debt or equity instrument or derivative transaction. The default of an equity investment is also a counterparty default risk. The counterparty default risk also takes negative changes to the assessed value of loan collaterals into account.

Beside the interest rate risk at net present value, the counterparty default risk - as defined by the business model - represents the greatest quantitative risk capacity share among the individual risk types. This results from the Bank's strategic emphasis on customer loan business.

The Management Board members are responsible for the proper organization of the loan business segment and its continued development, as well as the proper control and monitoring of loan business risks, irrespective of the internal organizational structure.

The sales units and back office are integrated into the loan process. The sales units and back office functions are separated — also in the case of substitution — up to and including the management level and the organizational structure.

The weekly quantification of risks is based on the expected loss and unexpected loss concepts (value at risk). Quantification, analysis and control of the counterparty default risk is performed on the individual transaction level, as well as on the portfolio level and includes the sub-portfolios Private Customers, Freelance Professions, Corporate Customers, Treasury (issuers and counterparties), and Equity Investments. All individual credit risks are aggregated into groups of affiliated customers.
Risk concentrations are mapped and controlled at this level.

Central parameters for the determination of the expected and unexpected loss are the defaulting probability of the borrowers and the unsecured total loan. The unsecured total loan in the primary customer loan business is determined by subtracting the measurable loan collaterals from the total loan. In the sub-portfolio Treasury, also issuer-and counterparty group-related loss ratios are applied. In relation to the essential customer loan business in the sub-portfolios Private Customers, Freelance Professions and Corporate Customers, the defaulting probability is determined on the basis of the annually validated rating system CredaRate. The default probabilities in the sub-portfolios Treasury and Equity Investments are primarily derived from external ratings.

At the end of the reporting period, the Bank's expected loss was € 20.8 million according to the standard scenario (€ 18.9 million). Of that, the main portion of € 19.7 million (€ 18.1 million) is attributable to the essential customer loan business in the sub-portfolios Private Customers, Freelance Professions and Corporate Customers:

SUB-PORTFOLIOS WITHIN THE LENDING PORTFOLIO
IN € MILLION

	12/31/2017	12/31/2018
Private Customers	0.5	0.5
Freelance Professions	2.3	2.4
Corporate Customers	15.2	16.8
Treasury	0.7	1.0
Equity investments	0.1	0.1
Total	**18.9**	**20.8**

Regarding, individual borrowers of the primary customer loan business, total loan, unsecured total loan and the expected loss of € 19.7 million are distributed between the rating scales and the corresponding average default probabilities of the respective rating scales as follows:

LENDING PORTFOLIO ACCORDING TO RATING CLASSES
IN %

Rating scale	Average default probability of the rating class	Share of total loan	Share of unsecured total loan	Share of expected loss
nor rated	0.340	3.1	4.4	1.4
1	0.030	5.5	6.8	0.2
2	0.058	3.6	3.1	0.2
3	0.108	7.0	4.5	0.4
4	0.190	8.3	8.0	1.4
5	0.340	12.8	11.6	3.6
6	0.553	13.0	15.0	7.6
7	0.808	12.4	13.1	9.6
8	1.188	12.5	12.6	13.6
9	1.788	10.7	9.7	15.9
10	2.725	7.1	6.8	16.9
11	4.150	2.2	2.0	7.7
12	6.250	0.8	1.4	7.7
13	9.375	0.1	0.1	0.6
14	14.000	0.5	0.5	6.7
15	20.000	0.5	0.4	6.6
Total		**100.0**	**100.0**	**100.0**

Value at risk is a risk measure that indicates, which loss value is not exceeded by a risk position (in this case the loan portfolio) under the assumption of a set probability (confidence level) and within a set period (as a rule one year). The basic idea behind value at risk determination is that the repeated simulation of borrower defaults provides a basis for the projection of the probability for potential loss arising from loan business. The risk calculation system applies the statistical portfolio model "Credit Risk+" for the value at risk determination and complements this model with a correlation model for industry-specific default rates based on Federal Office of Statistics data.

The unexpected loss of € 56.8 million (€ 48.5 million) is determined on the basis of the internal categorization system and is quantified with a confidence level of 99.9 % and an observation period of one year.

isk concentration analyses for regions, industry sectors and credit rating categories are also components of risk reporting, in addition to volume concentrations that are principally considered in the determination of unexpected losses in the value at risk model. The main regional focus of our customer loan business is North Rhine-Westphalia (92.3 % of committed loans that did not default). 74.9 % of the committed credit lines in the issuer and counterparty business segments are attributable to domestic issuers and counterparties.

Collateral values are generally determined prior to each loan decision to measure expected collateral revenues. For this purpose, minimum haircuts are defined for the determination of the collateral values depending on the provided collateral type. If there are indications that these values have changed, the collateral values are updated. Within the scope of risk measurement these collateral valuations are applied.

Imminent default risks are taken into account through the creation of specific valuation allowances and provisions. An imminent default risk arises, if the Bank considers it improbable that a debtor is in a position to pay all of its liabilities to the Bank. An important criterion for the identification of an imminent risk is the assessment of the borrower's sustained capacity to provide net debt service i.e. to which extent the borrower will likely be in a position to provide net debt service from expected future inflows (cash flow, salary, other income). The assessment of the individual risk provision considers the probable realization value from available collaterals. In addition, payment inflows are taken into account that can be used during the next five years for the reduction of the Bank's claim.

During the reporting year, the share of non-performing loans was reduced from 2.5 % to 2.2 % and since 2014 this share was reduced in total by 4.5 % points.

MARKET PRICE RISK

Market price risk is defined as the risk that market parameters and consequently the value of positions exposed to market price risks develop unfavorably for the bank due to general market movements. Corresponding to the different market transaction parameters, market price risks are differentiated into price, interest and currency risks. Price risk is defined as the risk that may result from currency or price fluctuationswithin a certain period of time. The individual funds risk is depending on the funds composition (shares, bonds and property funds or hybrid forms). Negative economic developments on markets, market segments, in industries or companies may result in lower funds valuations. Potential price declines of interest-bearing instruments due to deteriorating credit ratings (changes of the spreads), are also classified as market price risk.

The Bank invests in securities and enters into money market transactions within the investment book. The Bank holds investment funds to a limited extent for the processing of capital-forming schemes and standing orders. In addition, the Bank's investment book , macro and micro interest swaps are also included to hedge the fiscal year's net interest income. These are components of interest rate risk management.

Open foreign currency positions from interest and currency transactions with customers within the scope of interest and currency management (currency exchange rate peaks) are to be kept to a strict minimum.

The Bank does not engage in proprietary trading on this basis. Corresponding processes for the daily monitoring and immediate closure of open positions have been implemented.

Option risks result exclusively from interest and currency transactions with customers and are generally hedged by equivalent transactions in the interbank market.

The weekly market price risk report is prepared by the Risk Management division / Risk Controlling department. Within the scope of interest and currency management for customers, a risk contribution is determined and reported weekly for all of the Bank's own investments, as well as for interest and currency transactions. The report is provided to the Management Board, the responsible division and department heads, as well as to the Credit Risk Management division / Quality Management department and the functional responsible employees of the affected divisions. In addition, all market price risks are reported within the scope of quarterly reporting.

The material elements of risk management are risk and loss limits. Risk limits and warning levels are set on an annual basis for the Bank's own investments, as well as for interest and currency transactions. Loss limits are also defined for shares, funds and bonds. These limits cap the permitted pending portfolio losses. Expected losses from the purchase of interest bearing securities above par price are proportionately added to the loss limits for bonds on a daily basis. During the course of the year realized losses also cut the set loss limits.

To monitor used limits, the Risk Controlling department provides a market risk report on the existing risk and loss limits to the Credit Risk Management division / Quality Management department on a weekly basis and at month's end.

If warning levels, risk limits or loss limits are reached or exceeded, as well as in the case of controlling relevant back testing deviations, Risk Controlling calls a Market Price Risk Committee meeting.

If warning levels, risk limits or loss limits are reached or exceeded, this committee will prepare a base strategy in accordance with the business and risk strategy for the next steps, as well as associated controlling measures in a timely manner. In the case of controlling relevant back testing deviations, the Market Price Risk Committee proposes possible measures. Permanent participants in the Market Price Risk Committee for controlling relevant back testing deviations are representatives of the risk controlling department, as well as of the department Treasury and the department Credit Risk Management and in the case risk limits, loss limits or their warning levels are exceeded, representatives of the Accounting & Controlling department will also participate in Market Price Risk Committee meetings.

For the value at risk determination the risk calculation system applies the so-called variance-covariance approach. The determination of the value at risk with the support of the variance-covariance approach is based on the assumption that past fluctuation ranges (volatilities) measured for various assets is a good indicator for the fluctuation range of the future market prices of these assets. According to the portfolio theory, the fluctuation range of the market price of an entire portfolio can be derived from the fluctuation ranges of the market prices of the individual assets of a portfolio, if the weights of the individual positions (investments) in the portfolio and their correlations amongst each other are known. In this context, the focus is not placed on the volatilities and correlations of the specific investment objects' market prices, rather the focus is placed on categorized standard market objects.

For weekly quantification and management of the market price risk of the Bank's own investments, as well as transactions within the scope of interest and currency management, a value at risk model is applied, which determines the value at risk for a holding period of 250 days with a confidence level of 99.9 %. Furthermore, the value at risk concept is supplemented by hypothetical and historical scenario calculations and a comprehensive stress test.

Credit spread risks are determined using a scenario analysis. For this purpose, a premium is added to the interest curves used for the valuation and the portfolio's modified daily quotes. Prices calculated on the basis of this fictitious interest curve are subsequently compared with the prices calculated without the premium.

The Risk Controlling department checks the forecast quality of the risk model underlying the market price risk report during the preparation back testing reports. Back testing compares the value at risk calculated on the day before the qualifying date with the actual market movements on the qualifying date. The Risk Controlling department calls for a meeting of the Market Price Risk Committee, as soon as the calculated value at risk varies from the actual market movements to a controlling relevant extent.

On the reporting date, the value at risk contribution (value at risk and credit spreads) for the market price risk from the Bank's own investments was around € 8.8 (2.7) million due to spread increases, which could be observed since mid-October 2018, and associated price reductions on the European bond market. On the reporting date, the value at risk for the market price risk from interest and currency transactions was around € 0.1 (0.2) million.

INTEREST RATE RISK

Interest rate risk is a sub-category of the market price risk. Interest rate risk is understood as the risk of negative effects on the Bank's financial performance and financial position arising from interest rate level and interest structure developments, as well as developments regarding the interest book's volume and structure. The interest rate risk is assessed on the one hand based on a periodic dimension and on the other hand based on a net present value dimension.

The interest rate risk quantification and the interest rate risk reports are prepared by the Risk Management division / Risk Controlling department. The management of the Bank's entire bank book is the responsibility of the Management Board on the basis of suggestions put forth by the Treasury department and the interest rate risk committee.

The interest rate risk quantification is based on a periodic net interest income simulation, as well as an analysis of the interest book at net present value. The interest book contains all of the Bank's business transactions that are exposed to a interest rate risk. Reports are provided to the Management Board and the Supervisory Board at least on a quarterly basis.

Within the scope of the interest income simulation for the fiscal year, the net interest income for the next twelve months is determined based on various interest scenarios under the assumption of a constant balance sheet structure. The applied interest rate scenarios include a constant interest rate level, parallel shifts and reversals of the interest rate structure curve upward and downward, as well as the Bank's interest rate forecast.

In addition, historically derived and hypothetical stress scenarios are simulated. Increases or decreases in holdings are also simulated, in addition to interest structure changes, to take risk concentrations in the analyses into account. Furthermore, depending on the scenario the simulation period is extended.

Periodic interest rate risk components are the interest rate risk arising from the banking business and the pension risk. The interest rate risk arising from the banking business is composed of the business risk interest business and the interest structure risk arising from interest rate level and interest structure changes.

At the end of the reporting period, periodic interest rate risk was around € 1.4 (2.7) million. The interest rate risk at the net present value, which is relevant for the analysis of risk capacity from an economic perspective, is derived from a negative change of the economic value in the case of a sudden and unexpected positive or negative interest rate change by 100 base points. At the end of the reporting period 2017, the interest rate risk at the net present value was € 27.7 million (€ 20.0 million).

In addition to the interest rate risk at the net present value, the interest rate coefficient is determined based on Section 25a Para 2 German Banking Act according to the 9/2018 circular of the Federal Financial Supervisory Authority. This key indicator shows the highest negative change of the interest book's economic value in relation to the regulatory own funds in the event of an upward or downward parallel shift in the interest rate yield curve by 200 base points. If this interest rate coefficient exceeds 20.0 %, the institute is considered to be a "credit institute with an increased interest rate risk". Reporting is provided quarterly according to the regulatory requirements. The determined net present value development remained markedly below this value on all qualifying dates. At the end of the year, the negative net present value development was 15.4 % (11.0 %).

LIQUIDITY RISK

Under the term liquidity risk several risk factors are summarized. The definition of the liquidity risk includes, in addition to the risk of the Bank's illiquidity, the liquidity cost risk and the risk of market illiquidity (or market liquidity risk). Liquidity costs can arise, if liquidity can only be achieved through higher prices.
The market illiquidity risk includes the risk that assets can be converted into cash in principle, cannot be converted into cash or only if price reductions are accepted.

The Bank's liquidity risk management is to ensure that current and future payment obligations can be met in full at any time. In addition to the regulatory liquidity requirements, liquidity risk management must also ensure short-term (dispositive) and long-term (structural) liquidity.

The liquidity risk management is anchored in the line processes of the bank under consideration of required organizational separations. The daily dispositive liquidity risk measurement is performed by the Risk Management division / Accounting & Controlling department. The Risk Management division / Risk Controlling department is responsible for the structural liquidity risk measurement. Liquidity risk management is the responsibility of the Treasury department. The determination of the liquidity cost risk is performed within the scope of the monthly risk capacity analysis from an economic perspective by the Risk Management division / Risk Controlling department.

Liquidity management is performed on the basis of daily liquidity key indicators, i.e. on the strategic liquidity positions. The investment and refinancing options offered by the European Central Bank are used within the scope of dispositive liquidity management. In addition, money transactions are entered into with other banks and a select group of non-banks. Measures such as issuance of promissory notes or sale of promissory notes or of securities that are not eligible for the pool of pledged assets, as well as potential structural customer deposit changes are available for structural liquidity controlling.

Close monitoring by the Treasury department and the Risk Management division / Risk Controlling department provides for initiating measures at an early stage to optimize the liquidity structure and thus avoid potential liquidity shortfalls. The purpose of the liquidity risk committee is to ensure consistency of activities and measures.

The dispositive liquidity controlling core responsibilities are to ensure the Bank's ability to meet its payment obligations, to invest excess liquidity, to efficiently perform refinancing, to ensure compliance with minimum reserve requirements, as well as to ensure compliance with regulatory requirements concerning the liquidity coverage ratio. Various key indicators are determined on a daily basis to monitor the dispositive liquidity situation. In 2018, indications of a liquidity bottleneck were not identified.

A liquidity overview with expected funds inflows and outflows is prepared to assess the structural liquidity position. Assumptions on customer deposit withdrawals, including deposit concentrations, credit line use, as well as disposal of securities, are made, in particular, to determine these liquidity cash flows. The liquidity cash flows are simulated in the form of a standard scenario and of stress scenarios.

The standard scenario (observation period five years) and the stress scenario (observation period six months) produced only positive cumulated liquidity cash flows.

The liquidity cost risk (refinancing risk) is taken into account within the scope of the Risk Controlling department's monthly risk capacity analysis from an economic perspective. Due to the high concentration of refinancing via customer deposits, liquidity costs (all other things being equal) may be incurred on the liabilities side of the balance sheet through an increase in interest rates to be paid to the customers and the associated liquidity-based margin reduction. The liquidity cost risk was € 0.3 million on the reporting date (€ 0.3 million).

OPERATIONAL RISK

Operational risk is the risk of losses that are caused by inadequate or failing internal procedures, individuals and systems or that are caused by external events, including residual risks.

The objective of operational risk management is to minimize these risks to the extent possible under consideration of cost-benefit aspects. The characteristics of the specific risk (probability, effects of its occurrence, in particular the potential loss amount) determine how the Bank manages operational risks.

The identification of operational risks, as well as damages arising from materialized operational risks, the assessment of such operational risks and the development and implementation of controlling measures for specific operational risks is not performed centrally in the organizational units and in the affiliated companies, which caused the operational risks. For these purposes, the Risk Management division / Risk Controlling department is the central contact for the entire Bank.

Identification of significant operational risks is determined by an expert survey based on a risk identification sheet. The heads of the Bank's organizational units are responsible for the preparation and updating of the so-called risk inventory for their divisions/departments. In addition to the risks identified in the risk inventory, an overall Bank assessment is performed; i.e. branch risks, branch office risks, as well as risks for the affiliated companies are also included in the risk inventory. The assessment of the operational risks is updated quarterly. The Risk Management division / Risk Controlling department assesses the plausibility of the individual risk inventories, which are then aggregated into the overall Bank risk inventory.

The risk inventory was further detailed due to banking law, regulatory and technological developments in the Bank's business environment. The risk contribution from operational risks was € 4.9 million on the reporting date (€ 4.9 million).
Losses arising from operational risks exceeding € 1.0 thousand are entered into a central loss database. The Management Board receives routine reports, as well as event-driven ad-hoc reporting on the current risk situation, as well as control measure recommendations, if required.

BUSINESS RISK

Business risk is defined as negative deviation of the realized, i.e. expected net interest income and net commission income from the planned net interest income and net commission income, unless the deviation is caused by other risk factors, in particular, the interest rate risk.

The Bank's business risk is comprised of the respective risks arising from commission and interest business.

The risk of sales objective shortfalls is determined in the form of two components. The business risk from interest-earning operations as a part of the periodic interest rate risk is simulated as a potential negative deviation of the future interest net income, simulated on the basis of constant interest rates and portfolios, from the current reference interest net income. The business risk from commission business is, on the basis of the annual plan, the potential negative deviation from the expected figure.

REPUTATIONAL RISK

Reputational risk is defined as the risk of an unexpected loss due to reactions of stakeholders based on a changed perception of NATIONAL-BANK.

The NATIONAL-BANK business model's sustainability concerning its market success, its capital basis, as well as the quality of its products and services is determined to a high degree by its reputation in the public (customer, shareholders, creditors, business partners, banking supervisory authorities, other governmental institutions) and the perception by its employees. The sum of the aspects, which characterize the Bank's image to the outside and inside, is defined as reputation. Safeguarding an impeccable reputation at any time is a central maxim within the NATIONAL-BANK strategy.

The management of the Bank's reputation, as well as potential reputational risks is the responsibility of all Management Board members. Operational execution is the responsibility of the reputational risk representative and, if necessary, in cooperation with the involved divisions, departments or functions. To ensure adequate bank-wide risk control, this task is also supported by the reputational risk committee and the Management Board. The Bank took adequate measures against all identifiable risks to the Bank's reputation.

METHODS, PROCESSES AND IT SYSTEMS

The Bank conducts routine reviews on the adequacy of the methods and processes used to determine and analyze risk potentials and risk-bearing capacity; adjustments are made as needed. Within the scope of risk capacity assessment from an economic perspective, risk-reducing effects resulting from diversification among individual risk types are not taken into account. However, assumptions on risk reducing diversification are applied to the value at risk calculations of the counterparty default risk and the market price risk. These are based on customary models used in the banking industry; the Bank's individual parameters are routinely reviewed and adjusted as needed.

A state-of-the-art risk information technology system is used to prepare the Bank's risk calculation, analysis and reporting. This system is based on externally developed standard software and a central data warehouse for the calculation of counterparty default risk, interest rate risk, market price risk and liquidity risk. The Risk-IT system is operated by an organizational unit that is separate from the Risk Management division.

COMPENSATION AND SUPPORT MEASURES

Due to our membership in the Compensation Scheme of German Banks [Entschädigungseinrichtung deutscher Banken GmbH] and based on the European Bank Levy, special payments may be requested from the Bank in the event of compensation and support measures that result in a funding shortfall of these institutions. If and in which amount such payments will materialize is currently not foreseeable due to the calculation scheme, which, in particular, considers the relative development of bank-specific parameters as compared to the banking industry for the calculation of payments. In general, such payments may, however, put pressure on the Bank's financial position and performance, as well as the Bank's liquidity position.

ONGOING DEVELOPMENT IN 2019

One of NATIONAL-BANK's principles is the ongoing development of risk management. We are committed to ensuring that the full depth and breadth of market developments are taken into account and that all regulatory requirements are complied with.

RISK REPORTING

		Reporting Cycle	Created by	Recipient
All Risk Types	Quarterly Report (on all risk types, including stress tests, as well as new supervisory regulations on risk relevant topics)	Quarterly	Risk Controlling among others	Management Board / Supervisory Board
	Analysis risk capacity economic perspective	Monthly	Risk Controlling	Management Board
	Profit and loss statement	Monthly	Accounting & Controlling	Management Board / Supervisory Board
	Risk Inventory	Annually	Risk Controlling	Management Board
Counterparty default risk	Loan Risk Report	Monthly	Risk Controlling / Credit Risk Management	Management Board
	Major commitments according to the Audit Report of the Annual Financial Statements	Annually	Credit Risk Management	Management Board / Supervisory Board
	Loan commitments with risk-relevant circumstances	Quarterly	Credit Risk Management	Management Board / Supervisory Board
	Loans to executive bodies	Event-driven	Credit Risk Management/ Personnel	Management Board / Supervisory Board
	Counterparty and Issuer risks	Annually	Credit Risk Management	Management Board / Supervisory Board
	Development loan risk provisions and commitments with special risks	Monthly	Credit Risk Management	Management Board
Market price risk	Market Price Risk Report	Weekly	Risk Controlling	Management Board
	Back-testing analysis market price risk	Event-driven	Risk Controlling	Management Board
Liquidity risk	Liquidity Risk Report	Quarterly	Risk Controlling	Management Board
	Liquidity status	Weekly	Treasury	Management Board
Interest rate risk	Interest Rate Risk Report	Quarterly	Risk Controlling	Management Board
	Treasury Report	Monthly	Treasury	Management Board
Operational Risk	OpRisk Report	Annually	Risk Controlling	Management Board
	Report on Significant Losses	Event-driven	Responsible division	Management Board
Reputational Risk	Reporting on reputational risks	Event-driven or quarterly	responsible division	Management Board / Supervisory Board
Internal Control Functions	Quarterly / Annual Report of Internal Audit	Quarterly/ Annually	Audit	Management Board / Supervisory Board
	Quarterly / annual report of the compliance representative within the report of the staff functions	Quarterly/ Annually	Compliance Officer	Management Board / Supervisory Board
	Quarterly / annual report of the money laundering representative within the report of the staff functions	Quarterly/ Annually	Anti-Money Laundering Officer	Management Board / Supervisory Board
	Quarterly / annual report of the information security representative within the report of the staff functions	Quarterly/ Annually	Information security representative	Management Board / Supervisory Board
	Quarterly / annual report of the data protection coordinator within the report of the staff functions	Quarterly/ Annually	Data Protection Coordinator	Management Board / Supervisory Board

OPPORTUNITIES

The model-based quantification of the expected and unexpected loss in the counterparty default risk segment is performed on the basis of statistical methods and on the basis of historical observations. Opportunities arise, if the actual credit rating development of the loan risk-carrying positions takes on a more positive course than that observed in the past. In this case the loan risk provisions are below the calculated credit default risk and fewer migrations occur into the weaker (lower) credit rating levels.

In addition, in regard to positions with a counterparty default risk that meet the default definition, higher revenues than estimated can be realized within the scope of the disposal of securities or the credit rating of such positions can develop more favorably than estimated.

The development of the interest rate level and the interest structure — under consideration of the structure of the Bank's interest book — can create opportunities in regard to net interest income and the interest book's economic value.

The market price risk is determined according to a model. High volatilities, which result in a high market price risk, can, however, be associated with a positive overall development of the instruments with a market price risk.

Liquidity potentials held to ensure liquidity may be used to react flexibly to arising business opportunities.

In regard to the development of the Bank's business, opportunities can arise, if the realized net interest income and net commission income is above the planned net interest income and net commission income.

Opportunities from the operational risk arise if the actual loss occurrences fall short of the imputed risk potentials. Loss occurrences are the impetus for continued improvements.

In addition to risks, opportunities for the Bank's reputation may also arise through e.g. external positive reports.

Regarding the risk-bearing capacity of the Bank and considering all risks, it is possible that, the actual risks fall short of the imputed risks.

Internal Control System regarding the Financial Reporting Process

The Internal Control System (ICS) in Accounting is a component of the Bank's comprehensive overall internal control system. It is comprised of principles, processes and measures, designed to ensure that the Bank's accounting is correct, complete and efficient and that all statutory requirements are complied with. It ensures that the annual financial statements give a true and fair view of the Bank's financial position and performance.

The Bank employs standardized software components throughout the Bank, so that business transactions are predominantly posted and recorded electronically. The systems used for this can only be operated by employees specifically authorized for this purpose. Manual postings are limited to certain types of commission business. Manual postings are subject to dual control, if manual posting is required in individual cases. The system parameters are set under strict compliance with the separation of functions and is expressly provided for in numerous guidelines and policies.

A comprehensively regulated process for new business ensures that new financial products are accounted for appropriately in the accounting system through the inclusion of the accounting and controlling department. Numerous established coordination processes also ensure that all business transactions recorded in the systems are properly and completely depicted.

Independent reports prepared by Controlling, in which the Bank's individual result components are broken down to individual cost centers and profit centers, ensure ongoing plausibility checks and monitoring of accounting. Another major quality control component is the provision of monthly reports to the Management Board, the market divisions and the branches.

The Internal Audit department, which monitors the internal accounting control system, regularly checks the IT systems and work processes within the scope of accounting. The Internal Audit department is involved in all internal accounting control system development projects.

Report on Expected Developments

The Bank expects that the global economy's perspectives will remain solid, in spite of manifold negative geopolitical factors. Economic activities in the United States of America show a very robust development, which is also reflected in the most recent figures. The financial situation of US budgets was until recently in such solid shape that private spending could even gain additional dynamic in the coming years. Of particular importance are also the continued strong investment increases, which will even accelerate over the course of this year based on the relevant early indicators. For the current year, we expect still considerable overall economic growth rates of around 2.6 %, which will fall just short of the previous year's growth rate of 3 %. After economic dynamic significantly weakened during the year's first half in the Eurozone as compared to the previous year, economic dynamic further deteriorated also in the third and fourth quarter of 2018. While private and public spending continued to support the expansion, the negative foreign trade balance had a dampening effect. Also in Germany, overall economic production dynamic noticeable weakened over the course of the year. This was mainly caused by a deterioration of global economic perspectives due to the trade conflict, which of course also affected the most important German sales markets in the Eurozone. Beyond these interconnected global effects, a stronger production expansion was, however, also hampered by the high overall capacity utilization in conjunction with a marked shortage on the labor market and delays in the supply chains. Domestic economy continued, however, to be a main pillar, which will be stimulated also in the future by a strong employment build-up and unchanged low interest rates. With a view on the coming year, we remain optimistic, because we expect a softening of the trade conflict's intensity and a noticeable upturn of the global economy. Against this backdrop, we expect that the economic upswing in Germany will also continue in principle in 2019 with a GDP increase of around 1.6 %.

In this global scenario, the global expansion phase continuation should be the fundamental driver of the monetary reversal. With a view on the further course of the Federal Bank of the USA, we expect that the Fed will continue with its monetary course of a gradual and data-driven increase of base interest rates. Beyond the strains caused by the trade conflict, the economy of the USA remains robust, also in the perception of the Federal Bank of the USA. For this reason we expect that the Fed's interest cycle is not yet completed. Based on our estimate that the economy of the USA will at least remain in the expansion phase, we consider it likely that the rates of return in the USA can even increase during this global economic cycle. For the year's end, we expect rates of return around 3.3 %. With a view on the European bond market, this scenario raises the question of how the European interest structure will react to a continued interest increase in the USA. We expect that the current decoupling of interest rates will continue and will under certain circumstances be even more pronounced. With a view on the structural weaknesses, the ECB will decouple its monetary policy from the international trend for many years. This means that the development of interest rates in Europe will become more and more a factor that is predominately depending on the politico-economic development in the future. For this reason and with a view to the next year, in spite of the upwards forces on the international capital markets a way below average yield level of around 0.6 % for ten-year government bonds is to be expected. Finally, we expect that current and future interest and growth differences will result in a structural devaluation of the Euro.

Accordingly, the environment in which the banking industry operates will continue to be a challenge: The foreseeable ever increasing politicization of European monetary policy will move a normalization of the interest environment in Germany and Europe more and more into a distant future. In spite of the economic recovery in Europe, a noticeable reversal of the ECB's monetary policy is becoming more and more improbable, because the better economic environment was not used for reforms, primarily the monetary union. Moreover, the monetary union resulted in a political and economical division of Europe, which can hardly be covered. At its core, the fixed exchange rate places too great demands on countries to the present day, so that structural problems were created that are a latent threat to the monetary union's stability. In this context, the Target-2-Receivables of the German Federal Bank, which had their strongest increase during 2018 since the financial crisis, are also an expression of the increasing intra-European imbalances. Southern Europe will not get rid of its base unemployment - at least not during this economic cycle - in spite of a relative long recovery phase and the financial stability of public finances continued to worsen in spite of low interest rates over several years and an economic recovery. The European region's structural fragility continued to increase in spite of the economic recovery. Finally, the ECB will be forced to counteract with continued artificially low interest rates, so that the extraordinary low interest rate level will continue to put a strain on the banks' net interest income. For this reason, the banking and financial business environment will remain fragile also in 2019. Also beyond the trade conflict, global economic and political conditions will remain characterized by a multitude of geopolitical and military-strategic disputes.

In addition, the finance sector is being asked to shoulder additional direct financial burdens. These burdens include, in particular, the bank levy (including the exclusion of the bank levy as tax-deductible expenses), the increase of the financial supervisory authorities costs through the creation of supervisory functions at the European Central Bank and, finally, the increasing capital costs due to the "phasing-in" according to CRR/CRD IV.

Against this backdrop, we will maintain our exclusively customer-driven business model that has proven itself particularly under difficult conditions. We plan to intensify and increase our organic growth and develop new income sources to hedge our earnings power. We will expand digitalization in line with demand. Our digitalization strategy is determined by the focus of our business and risk strategy on comprehensive consulting, advice and excellent service.

We extended our positioning as an attractive employer through systematic personnel management for the long-term development of our human resources, as well as through the safeguarding of our excellent competitive position for attracting first-rate talent.

Considering the aforementioned legal, political and economic environment, our 2019 - 2023 business planning is based on the assumption that the extremely low interest rates will continue, which will have a negative effect on the interest net income. We expect that the 2018 interest net income will only be significantly exceeded from 2021 onward.

According to our plan, the net commission income will continue to increase gradually, without tying-up additional equity. The major drivers of this development will be Asset Management, but also International Business, Account and Card Services, as well as the Loan Business. We expect that gross profits will be noticeable above the 2018 level from 2020 onward. Personnel expenses will increase marginally and operating expenses will slightly decrease. Due to the expected economic development, we updated credit risk provisions for the plan years at a bandwidth of between € 7.0 and 8.0 million. Overall, the business plan through 2021 foresees annual net incomes at the 2018 level and from 2022 onward significantly increasing annual net incomes.

STRATEGIC KEY FIGURES

The strategic target ranges should ensure that the sustained development of our Bank is not solely focused on the achievement of a singular return objective.

The plan figures for the strategic target ranges are as follows:

- The target range for return on equity before taxes is 10 to 15 %.
- The regulatory relevant core capital (CET 1 / Common Equity Tier 1 Capital) should be within a target range of 12 to 15 %.
- Cost income ratio should be within a target range of 65 to 70 %.
- The loan to deposit ratio should not exceed a figure of 1.

Common Equity Tier 1 capital ratio will be below the 12 to 15 % target range in 2019 and 2020. This forecast is subject to the proviso of the Shareholders' Meeting resolution on the appropriation of earnings for the respective budget years.

The return on equity will also be below the target range of 10 to 15 % over the next two years due to sustained low interest rates and the increased expenses associated with the implementation of regulatory requirements.

The cost-income ratio will be above 70 % in 2019 and 2020.

The respective objective will only be achieved gradually, considering the current interest rate level and the planned increase of the loan portfolio, which is subject to minimum reserve requirements. The Management Board is willing to accept a longer transitional period, in particular if this is due to investment reasons. Overall development sustainability is also decisive in this case and not meeting individual key indicators.

As in the previous years, the loan to deposit ratio will be steady below 1 in the next two years.

SEPARATE NON-FINANCIAL REPORT

NATIONAL-BANK uses for its non-financial report in terms of Sections 289b, 289c, 340a Para 1a German Commercial Code [HGB] according to Section 289d German Commercial Code [HGB] the framework “German Sustainability Code [Deutscher Nachhaltigkeitskodex] (DNK)”, supplemented by the performance indicators according to the Sustainability Reporting Standards (SRS) of the Global Reporting Initiative (GRI), and publishes this report at www.national-bank.de and at www.deutscher-nachhaltigkeitskodex.de.

Balance sheet figures In € million	**12/31/2016**	**12/31/2017**	**12/31/2018**	**Adjustment 2017/2018**
Receivables from customers	3,165.2	3,167.0	3,283.7	3.7 %
Guarantees	89.1	88.4	97.4	10.2 %
Customer deposits	3,388.1	3,622.1	3,757.4	3.7 %
Receivables from banks	63.3	35.5	65.7	85.1 %
Deposits from banks	440.2	452.0	447.1	-1.1 %
Bonds and notes	674.1	525.4	523.0	-0.5 %
Stocks and other non-fixed interest securities	0.6	0.3	0.1	-66.7 %
Equity (excluding subordinated loans)	317.0	332.9	335.6	0.8 %
Subordinated loans (excluding accrued/deferred interest)	20.0	10.0	10.0	0.0 %
Total assets	4,265.7	4,522.8	4,644.4	2.7 %
Business volume	4,354.8	4,611.1	4,741.9	2.8 %

Income statement In € million	**2016**	**2017**	**2018**	**Adjustment 2017/2018**
Gross profits	**133.1**	**131.0**	**123.1**	**-6.0 %**
Net interest income	93.3	86.4	83.4	-3.5 %
Commission net income	45.4	45.7	43.7	-4.4 %
Other income and expenses	-5.6	-1.1	-4.0	263.6 %
Administrative expenses	**96.2**	**93.6**	**93.5**	**-0.1 %**
Personnel expenses	55.7	51.7	52.2	1.0 %
Operating expenses	35.6	37.6	37.3	-0.8 %
Depreciation on tangible assets	4.9	4.3	4.0	-7.0 %
Risk provision	**9.7**	**4.1**	**2.6**	**-36.6 %**
Operating result	**27.2**	**33.3**	**27.1**	**-18.6 %**
Extraordinary result	**6.9**	**-1.0**	**-1.0**	**0.0 %**
Net Income	**15.1**	**15.9**	**13.9**	**-12.6 %**

Key figures, other information	**12/31/2016**	**12/31/2017**	**12/31/2018**
Total capital ratio	12.7 %	13.5 %	12.4 %
Common Equity Tier 1 capital ratio	11.4 %	12.2 %	11.3 %
Number of shareholders (approx.)	5,200	5,200	5,200
Dividend	0.80 €	0.80 €	0.80 €
Dividend yield in %	2.48 %	2.48 %	2.55 %
Earnings per share in €	1.40 €	1.46 €	1.08 €

This document is an excerpt from the German version of our Annual Report.
Due to the fact that the English version is a translation, the German version is binding.

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