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Press conference to present the  
**Results for 2010**

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The spoken word prevails.

## 1. Introduction

Good morning, ladies and gentlemen!

I would like to welcome you to our press conference today, where we will present the results for the year 2010. We will also provide an outlook for 2011. I am very glad that you have been able to attend today.

I would like to start with a brief **overview** (*diagram 1*):

- Whilst 2009 was characterised by stabilising and restructuring; the 2010 financial year saw the **transition from the restructuring process towards a newly positioned Group**. The Group now has a clear-cut structure, and we reduced total assets further. The Group's realignment is therefore largely completed.
- All of the Group's relevant entities reported a **profitable** fourth quarter; in fact, our core bank pbb Deutsche Pfandbriefbank had already achieved this in the third quarter of 2010. Overall, we **significantly reduced losses** during the year under review.
- We **further streamlined the existing portfolio**, by reducing and restructuring problematic exposures. We then split this restructured portfolio in two: a strategic part which forms the basis for future growth, and a second part that is earmarked to be reduced, in a value-preserving manner. The key step towards achieving this goal was the transfer of assets to FMS Wertmanagement.
- We are now focused again on the market, and on our clients: pbb Deutsche Pfandbriefbank is concentrating fully on its **core business – returning to the markets with full force** during the 2011 financial year. We have a profitable portfolio and we plan to originate new business of up to € 8 billion. We want, once again, to make an important contribution to the provision of finance to our clients and to restore our profile as an issuer on the Pfandbrief markets.
- Our medium- to long-term objective remains unchanged: the **re-privatisation of Deutsche Pfandbriefbank AG** as planned by the Federal Republic of Germany as the owner of Hypo Real Estate Holding. It was thanks to the support from the German government that we managed to re-position the bank, and I would like to take this opportunity to express my sincere thanks for this. Continuing to operate the newly-positioned bank – followed by re-privatisation – represents the best option to maximise value for the Federal Republic of Germany, and for taxpayers, and when exiting this investment. We have established the key prerequisites for this to happen.

I would now like to ask Alexander von Uslar to elaborate on the results in detail, as well as on the liquidity and capital situation of the HRE Group and the Deutsche Pfandbriefbank sub-group.

## **2. Results 2010**

Good morning, Ladies and Gentlemen. I would also like to extend a warm welcome to you.

I will now elaborate on the results of the HRE Group and the Deutsche Pfandbriefbank sub-group, on the basis of preliminary figures prior to the approval of the consolidated financial statements by the Supervisory Board. I would like to open with the following comments:

- Both sets of financial statements show that the Group's entities returned to a profit during the fourth quarter – in fact, Deutsche Pfandbriefbank had already posted a profit for the third quarter. We also significantly reduced losses compared to the previous year, having outperformed our own projections. Hence, the transition from a Group being restructured to a newly-positioned Group can also be seen in the quarterly results.
- However, the results still reflect various non-recurring effects, as a result of which the figures should not be extrapolated to subsequent quarters.
- During the financial year under review, the financial position and financial performance was materially influenced by the transfer of the positions, as well as by other stabilisation and restructuring measures. This led to a pre-tax loss in 2010.

I will now outline the two sets of financial statements in detail.

## 2.1 HRE Group results (diagram 2)

- At € -859 million, HRE Group's **pre-tax loss** was markedly lower than in the previous year (2009: € -2,221 million). Not only the profit of the fourth quarter of 2010 was significant in this respect: we also reduced the Group's losses in the first three quarters of 2010 compared with the corresponding quarters of 2009.
- **Operating revenues** for the fourth quarter totalled € 348 million. At € -259 million, operating revenues were negative in the first three quarters due to the charges incurred in conjunction with the restructuring process, guarantee fees payable to SoFFin as well as impairments recognised in relation to individual positions. Operating revenues amounted to € 89 million in the 2010 financial year (2009: € 419 million)
  - This was mainly due to lower **net interest income** of € 840 million (2009: € 1,396 million) and a higher burden from **net trading income**, which stood at € -364 million (2009: € -154 million).

Net interest income during the previous year had been influenced by favourable factors: in particular, higher drawdowns of liquidity facilities by DEPFA's clients, declining money-market interest rates, and the impairment of some subordinated capital instruments. Net trading income during the financial year under review was burdened by revaluation losses.

- The **net commission result** of € -319 million burdened operating revenues to a lesser extent than in the previous year (2009: € -642 million).

The largest individual items in the net commission result were expenses for **guarantees** and the utilisation of such guarantees, in connection with the liquidity support provided by SoFFin. Expenses for liquidity support totalled € 384 million (2009: € 741 million).

The liquidity situation has been subject to considerable changes during the year under review. Until the transfer of assets to FMS Wertmanagement, the Group had to draw on the liquidity support facility (in the form of guarantees) provided by the German Financial Markets Stabilisation Fund (SoFFin), to an amount of up to € 124 billion. We have transferred all guaranteed bond issues to FMS Wertmanagement. Since October 2010, the Group has been **independent of the SoFFin liquidity support facility**.

The German government has not had to shoulder any burdens from the guarantees extended. On the contrary: HRE's aggregate payments for guarantees to the Federal Republic of Germany will amount to **approx. € 1.2 billion**

- The situation on the commercial real estate markets improved to a certain extent during 2010, but the overall situation remained difficult. As a consequence, it was again necessary to recognise additional provisions for losses on loans and advances in 2010 to an aggregate amount of € 865 million (2009: € 2330 million). Net of releases, provisions for losses on loans and advances amounted to € 445 million (2009: € 2,091 million). It is worth noting that these provisions had to be recognised primarily by the time of the transfer to FMS Wertmanagement, whereas portfolio improvements during the fourth quarter allowed for a net reversal of provisions.
- At € 516 million, **general administrative expenses** declined year-on-year (2009: € 541 million), despite the expenses incurred for the transfer of assets to FMS Wertmanagement. These expenses were seen in the increase of other administrative expenses, to € 371 million (2009: € 328 million), which were more than offset by lower personnel expenses of € 145 million (2009: € 213 million).

## 2.2 Deutsche Pfandbriefbank sub-group results

With your permission, I will now turn to the results of the Deutsche Pfandbriefbank sub-group (diagram 3).

- Following a loss during the first half of the year, the sub-group was profitable during the second half of 2010. At € -135 million, **pre-tax loss** was markedly lower than in the previous year (2009: € -1,525 million). In fact all quarterly results for 2010 showed year-on-year improvements. Moreover, a positive result of € 119 million was generated during the third quarter of 2010: this marked the first positive quarterly result since the autumn of 2008. The positive trend continued after the transfer of positions to FMS Wertmanagement during the fourth quarter of 2010: a pre-tax profit of € 98 million was achieved for the period.
- **Operating revenues** of € 652 million were in line with the previous year's figure of € 653 million. Lower net interest income was offset by lower charges attributable to liquidity support (reported in the net commission result), positive net trading income, and positive effects in the balance of other operating income and expenses.

Revenues were generated mainly during the third quarter (€ 241 million) and – following the transfer of positions – during the fourth quarter of 2010 (€ 191 million). This development reflects the success of the restructuring process as well as the profitability of the remaining portfolio after completion of the transfer process.

- The statements regarding provisions for losses on loans and advances at a Group level apply accordingly: full-year additions to provisions for losses on loans and advances amounted to € 766 million (2009: € 2,024 million); net of releases reversals, overall provisions for losses on loans and advanced amounted to € 443 million (2009: € 1,891 million). Again, these provisions had to be recognised primarily by the time of the transfer of assets – after the transfer of particularly high-risk exposures to FMS Wertmanagement, net additions to provisions for losses on loans and advances normalised during the fourth quarter of 2010, at only € 25 million.
- At € 352 million, **general administrative expenses** increased year-on-year (2009: € 305 million). However, the increase in other administrative expenses was partly offset by lower personnel expenses.

### **2.3 Consolidated total assets of HRE Group and the Deutsche Pfandbriefbank sub-group**

I would now like to turn to total assets (diagram 4).

**Consolidated total assets** of HRE Group and the Deutsche Pfandbriefbank sub-group **(in accordance with IFRS) declined** during the year under review, primarily as a result of the transfer of assets to FMS Wertmanagement.

Due in particular to the effects of funding passed on to FMS Wertmanagement and other effects arising in the context of the transfer of assets, **the reduction in consolidated total assets during the financial year** did not yet fully reflect the full amount of assets transferred to FMS Wertmanagement. Such additional effects included exposures where beneficial ownership could not be transferred to FMS Wertmanagement, or where derivatives positions remained in place. These counter-effects occurred as at 1 October 2010 (the date of the transfer); they were already partially reduced by the end of 2010 and will decline further in the future – albeit not to zero.

**Market-induced effects**, such as exchange rate fluctuations, also impacted on the level of total assets. For instance, the decline of the euro resulted in an extension of the balance sheet (which is denominated in euros), since currency translation increased the euro carrying amount of foreign-currency assets and liabilities.

Excluding these counter-effects induced by the transfer of assets, and also excluding market-induced effects, consolidated total assets in 2010 would have **fallen to a much greater extent**, because the volume of new business concluded in accordance with the new risk policy was significantly lower than the repayments and asset sales.

Against this background, total assets developed as follows:

- Consolidated total assets of **HRE** amounted to € 328.1 billion as at 31 December 2010, down € 31.6 billion from the previous year (31 December 2009: € 359.7 billion).
- Consolidated total assets of the **Deutsche Pfandbriefbank sub-group** as at 31 December 2010 fell to to € 186.8 billion, compared with € 215.2 billion as at the year-end 2009. On a pro-forma basis (i.e. excluding the extension effects of the transfer of assets), consolidated total assets would have amounted to € 104 billion.

### 3. Capital situation

I now want to turn to the Group's capital situation. We ascertained at a very early stage a capital requirement of up to € 10 billion for HRE. The **capital committed** by SoFFin amounts to € 9.95 billion.

- HRE had received a total of € 6.02 billion in capital support from the German Financial Markets Stabilisation Fund (SoFFin) by the end of 2009.

SoFFin granted a further € 1.85 billion in support during the year under review.

€ 1.4 billion of this has been disbursed up to now, with up to € 0.45 billion to follow under certain prerequisites upon approval by the EU Commission within the scope of the state aid control proceedings.

- The remaining € 2.08 billion – the difference to the full amount of € 9.95 billion – will not be disbursed to HRE Group as it stands now, but will flow to FMS Wertmanagement.

Additionally, as disclosed in October 2010, HRE Group may have to pay a one-off charge of up to € 1.59 billion for the use of FMS Wertmanagement as announced in October 2010. Such a charge may be set to prevent any competitive advantages, amongst other factors. The entities affiliated to the DEPPFA sub-group would probably have to fund the vast majority of this charge – subject, amongst other things, to the consent of the responsible regulatory authorities. The charge would be fully recognised in income for 2011 and would burden the results of the DEPPFA sub-group as well as of HRE Group. In practice, the Federal government would merely transfer equity from HRE to FMS Wertmanagement.

This is the calculation basis for the following **regulatory capital ratios** (which include 2010 losses):

- The further recapitalisation of **HRE** (which was necessary during the first half of the year, prior to the transfer of assets to FMS Wertmanagement) and the reduction of risk-weighted assets due to the transfer, drove up the tier 1 ratio from 7.8% as at the end of 2009 to 34.7% at year-end 2010.
- The **Deutsche Pfandbriefbank sub-group** did not receive any further recapitalisation measures during the 2010 financial year. However, the transfer of assets to FMS Wertmanagement reduced risk-weighted assets, resulting in a tier 1 ratio of 16.7% as at the end of 2010 (31 Dec 2009: 5.6%). pbb's capitalisation is therefore solid and adequate for meeting challenges that may arise in the future. Please note that these are pro-forma calculations, since we are exempt under the German Banking Act from having to calculate any capital ratios.

This brings to an end to my statements on the results for the year 2010 as a whole and the fourth quarter. Thank you very much for your attention.

#### 4. Review of the year 2010

Ladies and Gentlemen,

For more than two years now, we have **consistently pursued the realignment of the HRE Group**. The new management team has reigned in the business focus, adjusted capacities accordingly, revised the risk strategy, and streamlined the existing portfolio. Accordingly, we are now focusing on real estate finance and on selected areas of the public sector – in selected European core markets. Above all, we are focusing on the Pfandbrief as a refinancing tool, and are applying a balanced risk/return profile as a benchmark.

##### 4.1 Restructuring

A key prerequisite for successfully implementing this strategy required the **split of the existing portfolio**. Despite the continuous efforts to streamline the portfolio over the course of the past two years, some portfolio parts were not commensurate with the new strategy in relation to products, regions, risk profile or funding opportunities – which meant that they could no longer be managed in the core bank.

Consequently, we split the portfolio:

- One part was transferred to FMS Wertmanagement for liquidation, which can be undertaken in this environment in a value preserving matter. We transferred a portfolio that was restructured to the maximum extent possible, as well as approximately € 3.5 billion in provisions carried for the transferred assets.
- The remaining portfolio held by pbb Deutsche Pfandbriefbank is – in the current environment - profitable and represents the basis for further growth.

In this respect, the **transfer of assets to FMS Wertmanagement** – which we have already mentioned on several occasions today – represented another important milestone in the realignment of the Group. In fact, it was probably the most significant individual measure taken.

The following figures will highlight the **complexity of the transaction**: overall, we transferred more than 12,500 individual items from almost 70 different jurisdictions. This transfer took place on the weekend after October 1<sup>st</sup>. We are proud of having executed this complicated transaction without any major hitches.

The transfer of assets was **crucially important** in many respects:

- We **improved our balance sheet structure**, so that we no longer needed to rely upon liquidity support provided by the German Financial Markets Stabilisation Fund (SoFFin).

As you will recall, the liquidity needs resulted largely from DEPFAs portfolio, where long-term receivables were funded through short-term unsecured liabilities. This funding requirement no longer applied after the transfer. Together with the assets, we have therefore transferred all pbb Deutsche Pfandbriefbank's issues which had SoF-Fin guarantess to FMS Wertmanagement.

- We **re-positioned pbb Deutsche Pfandbriefbank and focused its business on the European markets**: we now manage portfolios which are in line with our strategy in the two business segments of Real Estate Finance and Public Sector Finance. We essentially refinance these portfolios on a matched-maturity basis through German Pfandbriefe.

Looking at its portfolio and funding mix, pbb Deutsche Pfandbriefbank has already undertaken the restructuring measures that other providers on the market may yet have to face.

#### 4.2 Portfolios

I would now like to take a look at the **portfolios** of pbb Deutsche Pfandbriefbank and DEPFAs (diagram 5), based on exposure at default (EaD), as defined in Basel II. This parameter cannot be directly reconciled with the nominal volume of assets transferred to FMS Wertmanagement – around € 173 billion – or with total assets.

- As at the end of December 2010, total exposure for **pbb's portfolio** was € 86.3 billion, compared with € 132.1 billion prior to the transfer to FMS Wertmanagement. Real Estate Finance accounted for € 26.4 billion of this amount, and Public Sector Finance for € 59.9 billion.
  - In **Real Estate Finance**, the lion's share of the portfolio – an exposure of € 14 billion or 53% – is accounted for by Germany, in line with our strategy; this is followed by France and the UK.
  - In the **Public Sector Finance segment**, at € 26.2 billion, slightly less than half of the exposure is accounted for by Germany, followed by Austria, Italy, Spain, France, the UK and Portugal.
- As at the end of December 2010, the exposure of the **DEPFA** portfolio amounted to € 63.1 billion, compared with € 224.6 billion as at the end of September – prior to the transfer to FMS Wertmanagement (diagram 6).

The US and Germany accounted for the largest share thereof, at € 9.8 billion and € 9.7 billion respectively, followed by Spain, France and the UK.

- We have significantly reduced our exposure to **European countries currently in focus** to zero in some cases (diagram 7).

- pbb Deutsche Pfandbriefbank no longer has any exposure to Greece and Ireland, nor to Spain. Sovereign exposure to Portugal is very low at € 0.3 billion. We have reduced exposure to Italy to € 2.9 billion.

We still have sub-sovereign exposure to Italy, Portugal and Spain, some of which was reduced significantly.

The real estate finance portfolio in these countries is very small.

- We also significantly reduced DEPFA's sovereign and sub-sovereign exposure to European countries in focus: exposure to Portugal and Greece is practically at zero. The figure is € 0.6 billion for Ireland, whilst total exposure to Italy and Spain is € 3.0 billion and € 4.3 billion respectively.

- Two other countries are currently in focus – the **US** and **Japan**, the latter on account of the natural disaster:

- pbb has no exposure to the US public sector. The bank's € 1.7 billion US exposure relates to banks domiciled in the US, but not to the government or local authorities.

DEPFA has exposure of € 9.8 billion.

We no longer have any real estate finance portfolio in the US.

- pbb Deutsche Pfandbriefbank's exposure to Japan was around € 2.2 billion at the year-end; it has been reduced since then, to € 1.4 billion, through scheduled repayments. Based on our current knowledge, the properties we have financed are not directly affected by the catastrophe. DEPFA's exposure to Japan stands at around € 1.3 billion.

At present, our main focus with respect to Japan is on our colleagues working locally: around 40 staff. We are currently in the process of moving the majority of our operations from Tokyo to Osaka. We have also offered support to our colleagues if they wish to temporarily leave the country, together with their immediate family members; some have availed of this option.

#### 4.3 New business and refinancing

I would like to conclude my review by looking at new business and refinancing.

- Despite having devoted considerable resources to the transfer of assets, we originated **new business to the amount of € 4.1 billion** during the year under review, with the Real Estate Finance segment accounting for € 3.1 billion and the Public Sector Finance segment for € 1 billion.
- In the **Real Estate Finance** segment, real new business accounts for roughly half of the volume, while the other half is accounted for by renewals of existing loans. The average term is 3.9 years, and the average loan-to-value ratio is 66 per cent. On average, we achieved a gross margin in excess of 200 basis points. A total of 65 transactions were concluded.
- We concluded a total of 51 transactions in the **Public Sector Finance** segment. The average term here is 7.4 years, and the average gross margin is more than 100 basis points – a clear improvement over pre-financial crisis levels.

On the liabilities side, we raised € 4.6 billion in funding during 2010, through long-term Pfandbrief issues and unsecured funding. At the same time, we continued to reduce the share of outstanding short-term funding, this significantly improving our funding profile.

## 5. Strategic priorities and outlook for 2011

This brings me to the strategic priorities and the outlook for 2011.

The **strategic priorities** are focused on the medium- to long-term objective of re-privatising the HRE Group entities and maximising company value in the process (diagram 8). We want to achieve a scenario whereby we will repay the support provided by the Federal Republic of Germany – which was funded by tax revenue – to the maximum extent possible.

- This means for pbb in particular that we will **fully restore our origination strength**. We have set ambitious targets for our new business that should significantly exceed 2010 levels but that will of course also have to fit our risk profile.

The focus on new business goes hand in hand with our efforts to establish and expand pbb's access to capital market funding. Optimal and cost-effective refinancing is a fundamental prerequisite for realising the planned volume of new business.

- As a **portfolio manager and service provider, we support FMS Wertmanagement** – within the framework of servicing – in its task of successfully reducing the portfolios that were transferred by HRE.
- We assume that the **EU state aid proceedings** will be concluded during the first half of 2011. Within the scope of these proceedings, the European Commission is examining the permissibility of the support measures that HRE received from the Federal Republic of Germany. Any conditions imposed in this context might require us to make further adjustments to the restructuring measures we have already taken. The discussions held with the EU Commission are extremely constructive.

The good **start to 2011** strengthens our conviction of achieving the new business targets we have set. This applies to both the new business already originated and to transactions in the pipeline that we have initiated.

Overall, we feel we are **very well positioned** in what we consider to be a positive market environment for our business.

- We will continue to consistently gear our range of products and services towards meeting client requirements. We can leverage a well-established client base.
- Clients welcome the competence we have demonstrated in arranging individual financing solutions that require specific sector know-how, or where syndications or club deals are required. We are able to offer a cross-border, European approach.
- We are convinced that the demand for such solutions will continue to increase. At the same time, the number of competitors offering such financing solutions is falling. As you can see, we are operating in market that offers great potential.

On this basis, we have arrived at the following **assessments for the year 2011**:

- The Management Board anticipates posting a profit for the Deutsche Pfandbriefbank sub-group during 2011. We plan to provide a more precise assessment once the EU state aid proceedings have been concluded.

We expect the volume of new business originated to exceed the previous year's levels, to grow to up to € 8 billion, and to be originated primarily in the Real Estate Finance segment. On the whole, the new business forecasts depend on the outcome of the EU state aid proceedings.

- HRE Group's results for 2011 may still be burdened by a potential one-off charge of up to € 1.59 billion for the stabilisation measures provided; this would lead to a net loss. Without such a charge, the Management Board anticipates posting a profit for 2011.

## 6. Summary

I would like to summarise our statements in four key messages:

- First, HRE Group's **financial position** has improved considerably: having posted a profit for the fourth quarter, we once again reduced losses significantly during the financial year under review.
- Second, the restructuring of the strategic core bank is largely completed – **pbb Deutsche Pfandbriefbank is repositioned and ready to return to the markets**: the existing portfolio is now in line with our strategy, and our lending activities are funded largely on a matched-maturity basis and predominantly through German Pfandbrief issues. The final stage of the restructuring process – the positive conclusion of EU state aid proceedings – is still pending.
- Third, in a competitive environment that is favourable overall, we want to **fully restore our origination strength**. Taking into account the favourable start in the current financial year, we are confident of achieving our objectives. We aim to originate new business of up to € 8 billion, primarily in Real Estate Finance. The Management Board anticipates posting a profit for the Deutsche Pfandbriefbank sub-group in 2011.
- Fourth, we are preparing pbb Deutsche Pfandbriefbank for **re-privatisation**. Continuing to manage the newly-positioned bank, followed by re-privatisation, represents the best option to maximise value for the Federal Republic of Germany to exit from its participation.

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Ladies and Gentlemen,

This brings me to the conclusion of my comments. I would like to thank you all for your interest and attention. We now look forward to answering your questions.