



## 2004 Annual Report



# Hypo Pfandbrief Bank International S.A.

## 2004 Annual Report

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# Management Report

Pfandbrief Bank International S.A. has been operating under a new name since September 2004: Hypo Pfandbrief Bank International S.A. We have made this change to emphasise the fact that Hypo Pfandbrief Bank International is part of the Hypo Real Estate Group. We have therefore adopted the Hypo Real Estate Group corporate design, replacing our existing image and thereby emphasising consistency within the Hypo Real Estate Group, not only in terms of market presence, but also design.

The past financial year was the first full financial year for the Hypo Real Estate Group in its new structure. It was also the year in which the Group established its presence on the capital markets. The parent company of Hypo Pfandbrief Bank International S.A., Hypo Real Estate Bank International, Dublin, successfully positioned itself in the relevant markets. Hypo Pfandbrief Bank International was able to benefit from this, increasing the volume of new issues and net profits for the year compared with the previous year. We have continued to work on the structuring and the processes concerning the issuance of mortgage-backed Pfandbriefe under Luxembourg Law secured by loans acquired by Hypo Real Estate Bank International. The reorganisation of our IT infrastructure necessitated by the spin-off has been, by and large, completed, bringing us clear benefits in

terms of efficiency. This is also becoming apparent in the Luxembourg subsidiary of our parent company conducted under the same management, through which a large volume of loans documented under the Debt Issuance Programme of Hypo Real Estate Bank International has already been transacted in the first financial year.

All banks in Europe are preparing for the changes imposed by the new regulatory capital regime which arise when Basle II is incorporated into European Law. As its contribution to the Hypo Real Estate Group's project in preparation for these changes, HPBI has accepted the task of establishing the internal ratings for public sector borrowers for all the entities of the Hypo Real Estate Group. This will enable Hypo Pfandbrief Bank International to use the expertise it has developed over the past years in the credit analysis of public sector debtors for the benefit of the Hypo Real Estate Group.

The rating agency, Standard & Poor's, has confirmed the AAA rating for our public sector Pfandbriefe.

The Board of Directors of HPBI has met three times to discuss and decide upon issues for which there is a reporting obligation under our Articles of Association and rules. These include staff procedures and

credit limits. The discussions also focused on the strategic positioning and development of HPBI within the Hypo Real Estate Group.

In order to reinforce capital, in preparation for the envisaged additional functions of the bank, we have retained the profit for the year in full.

Hypo Pfandbrief Bank International has thus concluded a successful financial year in another year of difficult operating conditions, at the same time using its skills and expertise to promote the further development of the Hypo Real Estate Group.

#### **Lending operations**

In the year under review, we have acquired claims of € 594 m (previous year € 1,055 m), including € 449 m (previous year € 915 m) in securities issued by public sector borrowers. This accrual is offset by disposals in the form of redemptions, maturities and sales of € 526 m (previous year € 1,058 m). A commercial real estate loan of € 21 m was included in the figure for the first time. Where appropriate, derivative financial instruments were used to hedge against risks arising from market fluctuations.

#### **Funding operations**

Covered bearer and registered public sector Pfandbriefe (lettres de gage publiques) were issued in a nominal volume of € 2,011 m (previous year € 1,138 m). Bearer bonds requiring no cover were not issued (previous year € 50 m), likewise no subordinated debt instruments were issued (previous year € 9 m).

Apart from drawings in EUR, we also issued in USD. The bearer issues were launched as part of our MTN-Programme (Programme for the Issuance of Debt Instruments).

Out of our issues in circulation, nine were scheduled for repayment during the year under review, totalling € 1,221 m (previous year € 826 m). 14 issues totalling € 337 m were redeemed in advance of maturity. Out of our holding of own bonds we were able to place € 100 m (previous year € 60 m) back on the market.

As at year end, the limits of our commercial paper programme were utilised up to € 122 m (previous year € 140 m). The average term of the CP issues during the year was 109 days. All new issues were denominated in EUR.

**Balance sheet movements and earnings**

The balance sheet total is € 7,094 m. This is equivalent to an increase of 11.0 % over the previous year (€ 6,391 m).

Receivables, including securities, stand at € 6,398 m. This represents an increase of 5.0 % over the previous year (€ 6,096 m).

Funding resources totalled € 6,767 m, up 11.7 % compared with the previous year (€ 6,056 m).

Due to a tightening of interest margins over the year, it was not quite possible to match the level of net interest income during the previous year (-6.1 %). On the other hand, while maintaining a very conservative risk policy, we were able to exploit the interest rate trends and so generate additional earnings from investment holdings.

We intend to retain the entire reported profit for the year in order to consolidate our capital base.

**Income statement in report form** in thousands of €

|  |       | 31.12.2004   | Previous year |
|--|-------|--------------|---------------|
| Net interest income                                  |       | 7,231        | 7,700         |
| Commission income                                    |       | -636         | -39           |
| Net earnings from financial transactions             |       | 25           | 1,113         |
| Personnel expenses                                   | 1,689 |              | 1,758         |
| Other administrative expenses                        | 2,346 |              | 2,014         |
| Depreciations on property, plant and equipment       | 133   |              | 115           |
| Current expenses                                     |       | 4,168        | 3,887         |
| Other operating earnings/expenses                    |       | 210          | 23            |
| Operating result before risk provision               |       | 2,662        | 4,910         |
| Balance on write-down's and write-up's on securities |       | 3,420        | 917           |
| Risk provision                                       |       | 150          | 100           |
| Operating result after risk provision                |       | 5,933        | 5,727         |
| Taxes  |       | 1,331        | 1,377         |
| <b>Net income for the year</b>                       |       | <b>4,602</b> | <b>4,350</b>  |

### **Net income and appropriation of profit**

We have achieved a profit for the year of € 4,602 k after tax (previous year € 4,350 k). This represents an increase of 5.8 %.

At the Annual General Meeting of shareholders, we shall propose transferring € 250 k to statutory reserves and € 4,352 k to retained earnings.

### **Risk report**

Our Risk Controlling Unit, reporting directly to the management, has kept pace with the bank's growth and has accordingly further developed risk measurement and management systems in response to the constantly evolving internal and external requirements. The core functions of this unit are:

- to measure and monitor, on a daily basis, market, credit, counterparty and liquidity risks, using the value at risk approach
- daily calculation of economic performance
- independent monitoring of the parameters used to measure risk and performance
- to refine and implement our management concepts.

The on-going improvements to our measurement and management systems and our integration into the Hypo Real Estate Group risk management framework have given the bank an effective risk management tool.

We have set up appropriate reporting lines and control measures in order to monitor and control individual risks. We would mention the following by way of example:

#### **LIQUIDITY RISK**

We are in partnership with a number of well-performing banks in order to meet our short-term liquidity requirements. We produce a daily statement of all future cash flows and cumulative balances, broken down by individual currency, showing the management of short-term payment obligations. A daily assessment of our assets and liabilities is also conducted on the basis of liquidity categories and time scales in order to manage and limit liquidity risks in the short-term, as well as for the purposes of medium- to long-term planning.

#### **COUNTERPARTY RISKS (CREDIT AND COUNTRY RISKS)**

Our counterparty and credit exposure is restricted to public sector borrowers and OECD banks. The counterparty risks from derivate business is presented

regularly on the basis of gross replacement values, that is to say, the positive net present values obtained using the marked-to-market method. The utilisation of all credit lines is available for each individual counterparty and also in aggregated form online (intraday) on a market value basis.

#### **MARKET RISKS**

As part of our asset/liability management, the interest rate risk for the bank's overall position is monitored on a daily basis. Risk Controlling determines the risk position and financial performance every day and checks that the established limits are being adhered to. The management receives daily information on risks and performance. In order to manage and quantify the interest rate risk, we apply the risk sensitivities and the value-at-risk concept introduced within the Group. This is on the basis of a 99 % level of confidence, with an assumed 10 day holding period. The average exposure to interest rate risks was € 1.3 m.

There were no significant currency risks. All assets and liabilities and off-balance sheet transactions are taken into account in the risk assessment.

In addition to the Risk Management Unit, with its focus on market, counterparty, liquidity and operational risks, our Credit Research - Public Sector Unit concentrates on analysis of credit quality in the pub-

lic sector. This includes the attractiveness of the public sector borrowers involved, going beyond the analysis of credit-worthiness alone, as well as region-specific and level-specific financing solutions within the OECD area.

Credit-worthiness is assessed on the basis of a scoring model, that takes into account not only political, economical and budgetary factors, as well as regulatory conditions, but also qualitative aspects of the borrower unit. The internal evaluation of the (potential) borrowers goes hand in hand with constant monitoring of credit-relevant information that can be useful as an early indicator of potential risks and credit trends.

On one level, therefore, Credit Research provides information about possible credit risks in our bank's portfolio. On the other, it also provides a sound basis for the pricing of potential new investments by the Treasury department at country, regional and product level, within the management of the portfolio. The credit, information and decision-making processes are organised on the basis of the "Minimum requirements for the Credit Business of Credit Institutions" introduced in Germany.

#### **Other information**

The Hypo Real Estate Bank International has provid-

ed a letter of comfort for the Hypo Pfandbrief Bank International. We are fully consolidated in the IFRS accounts of Hypo Real Estate Holding through Hypo Real Estate Bank International.

The Board of Directors

### **Outlook**

The Hypo Real Estate Group and, with it, Hypo Pfandbrief Bank International, has achieved a great deal in the past financial year. We still have many tasks and challenges facing us. We are committed during this year to push ahead with the further development of the Luxembourg Pfandbrief, the diversification of the credit risks to be funded, by branching out into the real estate financing business and the expansion of the refinancing potential for the Hypo Real Estate Group. In so doing, we shall remain true to our standard of quality and soundness in our business policy and procedures.

No events of particular significance as regards the asset, financial and operating position over the past financial year have arisen since the end of this financial year.

Business trends and earnings have continued to proceed as expected since 31st December 2004.

24th February 2005



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# Annual Financial Statements

## BALANCE SHEET AS AT 31ST DECEMBER 2004

| Assets in €  |               |                      |                      |
|--|---------------|----------------------|----------------------|
|  |               | 31.12.2004           | Previous year        |
| Cash in hand,<br>Balances at Central banks and Postal Cheque Offices |               | 4,402,738            | 34,002,571           |
| Receivables from banks   |               | 1,351,727,256        | 912,421,207          |
| Municipal loans and loans guaranteed by public institutions          | 635,850,549   |                      | 529,123,542          |
| Other loans and advances   | 715,876,707   |                      | 383,297,665          |
| of which: payable on demand  | 91,055,318    |                      | 393,706              |
| Loans and advances to customers                                      |               | 572,271,780          | 555,933,929          |
| Municipal loans and loans guaranteed by public institutions          | 552,313,575   |                      | 555,933,929          |
| Other receivables  | 19,958,205    |                      | –                    |
| Bonds and other fixed-income securities                              |               | 4,473,567,873        | 4,627,881,600        |
| Public sector issuers  | 2,230,099,414 |                      | 2,239,270,077        |
| Other issuers  | 2,071,257,521 |                      | 2,322,669,705        |
| Own issues   | 172,210,938   |                      | 65,941,818           |
| Property, plant and equipment  |               | 110,163              | 199,949              |
| Other assets   |               | 535,214              | 341,206              |
| Accruals and deferrals   |               | 691,709,848          | 260,451,119          |
| <b>Total assets</b>  |               | <b>7,094,324,872</b> | <b>6,391,231,581</b> |

| <b>Liabilities</b> in €                            |               |               |                      |                      |
|--|---------------|---------------|----------------------|----------------------|
|  |               |               | <b>31.12.2004</b>    | <b>Previous year</b> |
| Liabilities to credit institutions                 |               |               | 1,253,790,037        | 1,243,175,411        |
| Registered public sector Pfandbriefe issued        |               | 40,000,000    |                      | 20,000,000           |
| Other liabilities                                  |               | 1,213,790,037 |                      | 1,223,175,411        |
| of which: payable on demand                        |               | 1,921,184     |                      | 2,244,464            |
| of which: with agreed maturity or period of notice |               | 1,211,868,853 |                      | 1,240,930,947        |
| Liabilities to customers                           |               |               | 701,856,573          | 162,200,000          |
| Other liabilities                                  |               | 701,856,573   |                      | 162,200,000          |
| Registered public sector Pfandbriefe issued        |               | 701,856,573   |                      | 162,200,000          |
| of which: with agreed maturity or period of notice |               | 701,856,573   |                      | 162,200,000          |
| Securitized liabilities                            |               |               | 4,811,831,822        | 4,650,789,539        |
| Issued bonds                                       |               | 4,689,831,822 |                      | 4,510,788,259        |
| Public sector Pfandbriefe                          | 4,689,831,822 |               |                      | 4,460,788,259        |
| Other bonds  |               |               |                      | 50,000,000           |
| Other  |               | 122,000,000   |                      | 140,001,280          |
| Other liabilities                                  |               |               | 460,643              | 175,638              |
| Deferred income                                    |               |               | 193,366,860          | 207,526,228          |
| Provisions   |               |               | 4,047,095            | 2,994,765            |
| Deferred taxes                                     |               | 3,395,295     |                      | 2,444,295            |
| Other  |               | 651,800       |                      | 550,470              |
| Subordinated liabilities                           |               |               | 34,000,000           | 34,000,000           |
| Subscribed capital                                 |               |               | 66,000,000           | 66,000,000           |
| Additional paid-in capital                         |               |               | 15,000,000           | 15,000,000           |
| Reserves   |               |               | 9,370,000            | 5,020,000            |
| Net income for the financial year                  |               |               | 4,601,842            | 4,350,000            |
| <b>Total liabilities</b>                           |               |               | <b>7,094,324,872</b> | <b>6,391,231,581</b> |

# Annual Financial Statements

## INCOME STATEMENT FOR THE PERIOD FROM 1ST JANUARY TO 31ST DECEMBER 2004

| Expenses in €   |           |           |                    |                    |
|---|-----------|-----------|--------------------|--------------------|
|   |           |           | 31.12.2004         | Previous year      |
| Interest paid and similar expenses  |           |           | 524,926,139        | 565,826,758        |
| Fee and commission expenses   |           |           | 635,650            | 518,737            |
| General administrative expenses   |           |           | 4,035,437          | 3,772,696          |
| Personnel expenses  |           | 1,689,037 |                    | 1,758,241          |
| of which for wages and salaries   | 1,364,984 |           |                    | 1,607,228          |
| of which for social security  | 169,899   |           |                    | 109,881            |
| of which for retirement pensions  | 122,589   |           |                    | 77,431             |
| Other staff expenses  | 154,154   |           |                    | 41,132             |
| Other administrative expenses   |           | 2,346,400 |                    | 2,014,455          |
| Amortization and depreciations of intangible assets and property, plant and equipment   |           |           | 132,703            | 114,861            |
| Other operating expenses  |           |           | 17,845             | 8,238              |
| Write-down's and provisions for placements, loans and advances, and additions to provisions for contingent liabilities and credit risks |           |           | 150,000            | 100,000            |
| Write-down's and allowances for securities held as investments, participating interests and shares in affiliated companies              |           |           | 62,500             | 15,300             |
| Taxes on income from ordinary activities  |           |           | 1,331,000          | 1,376,785          |
| Result for the financial year   |           |           | 4,601,842          | 4,350,000          |
| <b>Total expenses</b>   |           |           | <b>535,893,116</b> | <b>576,083,375</b> |

| Income in €  |  |             | 31.12.2004         | Previous year      |
|--|--|-------------|--------------------|--------------------|
| Interest received and similar income   |  |             | 532.157.399        | 573.526.946        |
| of which from fixed-income securities  |  | 245.648.149 |                    | 259.665.300        |
| Fee and commission income  |  |             |                    | 479.441            |
| Net income from financial transactions   |  |             | 24.864             | 1.113.163          |
| Other operating income   |  |             | 227.981            | 31.068             |
| Income from the reversal of write-down's on<br>Securities held as investments, participating<br>interests and shares in affiliated companies |  |             | 3.482.872          | 932.757            |
| of which profits from the sale of fixed-income<br>securities held as investments   |  | 3.482.872   |                    | 932.757            |
| <b>Total income</b>  |  |             | <b>535.893.116</b> | <b>576.083.375</b> |



Following our appointment by the Board of Directors we have audited the attached annual accounts of Hypo Pfandbrief Bank International S.A. for the year ended 31st December 2004 and have read the related management report. These annual accounts and the management report are the responsibility of the Board of Directors. Our responsibility is to express an opinion on these annual accounts based on our audit and to check the consistency of the management report with them.

We have conducted our audit in accordance with International Standards on Auditing. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the annual accounts are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the annual accounts. An audit also includes assessing the accounting principles used and significant estimates made by the Board of Directors, as well as evaluating the overall annual accounts presentation. We believe that our audit provides a reasonable basis for our opinion.

In our opinion, the attached annual accounts give, in conformity with the Luxembourg legal and regulatory requirements, a true and fair view of the financial position of Hypo Pfandbrief Bank International S.A. as of 31st December 2004 and of the results of its operations for the year then ended.

The management report is in accordance with the annual accounts.

Luxembourg, 24th February 2005  
KPMG Audit  
Réviseurs d'Entreprises

Thomas Feld  
Christian Brüne



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**1. | General  
comments**

Hypo Pfandbrief Bank International S.A. (HPBI) was established on 27th July 1999 in Luxembourg under its original name, Pfandbrief Bank International S.A. (PBI). On 14th September 1999, the bank was granted a licence by the Finance Minister of the Grand Duchy of Luxembourg to operate as a mortgage bank under Luxembourg Law (banque d'émission de lettres de gage).

The bank was registered in the Commercial Register on 16th August 1999 under number 71104 (Section B). The legal basis for the operation of a mortgage bank is laid down in the "Law of 5th April 1993 on the Financial Sector" (in the relevant version applicable at the time) in Articles 12-1 to 12-9.

The bank was originally established by the Bayerische Hypo- und Vereinsbank AG (HVB) and its German mortgage bank subsidiaries, each having an equal capital holding through a holding company.

As part of the restructuring process of the HVB-Group, the commercial property business was hived off via a "spin-off" and grouped with other mortgage bank activities in the Hypo Real Estate Group. This transformation involved all the shares of HPBI being taken over by Hypo Real Estate Bank International, Dublin.

Hypo Real Estate Bank International, Dublin, now holds all the bank's capital, except for one share, which is held by a trustee. The subscribed capital of the bank is fully paid up. With effect from 1st September 2004, the bank's name was changed to Hypo Pfandbrief Bank International S.A. in order to emphasise the fact that it is part of the Hypo Real Estate Group.

Hypo Pfandbrief Bank International S.A. is included in the Consolidated Accounts of Hypo Real Estate Holding AG. The Consolidated Accounts are available at the company's registered office in Munich.

**2. | Balance sheet  
presentation and  
valuation methods**

The methods of balance sheet presentation and valuation used by the bank comply with the regulations applying in the Grand Duchy of Luxembourg and, specifically, with the Law of 17th June 1992 concerning the Annual Statement of Accounts and Consolidated Accounts of Credit Institutions ("Law"). Any classification structure used in the balance sheet which deviates from the provisions of the Law is based on the recommendation drawn up by the CSSF for the annual accounts of mortgage banks.

The capital currency is euros (€).

Provisions

In principle, the bank has adopted the policy of setting up specific provisions in order to cover the risk of loss and default on existing claims.

In accordance with the tax provisions in Luxembourg, the option to use an overall provision to provide against latent credit risks is exercised. The upper limit of 1.25 % of the risk weighted counterparty risks which must be observed in this connection is utilised in part.

## 2.1 Fixed assets

### Property, plant and equipment

Property, plant and equipment are stated in the balance sheet at acquisition or production cost, less accumulated depreciations. Property, plant and equipment are subject to value impairment over time and are accounted for by scheduled depreciations. The depreciations are based on the standard operational useful life.

The rates of adjustment applied as at the balance sheet date are shown in the table below.

Assets acquired with acquisition/production costs of no more than € 870 or with a standard useful life of less than one year are depreciated in full in the year of acquisition.

|                               | Rate of adjustment | Method        |
|-------------------------------|--------------------|---------------|
| Office and business equipment | 20.00 %            | straight-line |
| Computer equipment            | 33.33 %            | straight-line |

### Financial assets

The holding of bonds and other fixed-income securities which are intended to serve the business on a permanent basis, and which meet the bank's regulatory conditions, has been valued at acquisition cost or, if long-term depreciation is expected, at the stock exchange or market price, whichever is lower. All securities of the cover fund have been valued at acquisition cost. Securities which are covered by interest rate swaps (asset swap) have also been valued at acquisition cost.

The other fixed-income securities have been valued at the stock exchange or market price, whichever is lower.

Premiums and discounts arising are distributed pro rata over the remaining term of the securities in the income statement.

## 2.2 Current Assets

### Bonds and other fixed-income securities

Bonds and other fixed-income securities, which are not classified as financial assets, are entered at acquisition cost and allocated to liquid assets in full.

The securities are valued on the basis of the rigorous lowest value principle in accordance with the "retention principle". The value is then shown at the lower stock market price of the balance sheet date or, if this cannot be established, at the probable sale value or the price which best reflects the value of the securities.

Redeemed own bonds which are hedged by way of an asset swap are valued at acquisition cost.

### Receivables

Receivables are shown at their nominal values. Interest accrued, but which is not yet due, is entered under accruals on the asset side of the balance sheet. Premiums and discounts are accrued according to their term.

### **2.3 Liabilities/Provisions**

Liabilities are entered at their nominal or repayment amount, provisions at the amount required on the basis of reasonable commercial estimates.

### **2.4 Acquisition or production costs of similar stock items and all fungible assets, including securities**

The bank uses the weighted average price method to determine the acquisition cost.

### **2.5 Currency conversion**

Assets and liabilities not denominated in euros are converted into the capital currency at the middle spot rate of the balance sheet date.

Income and expenses in foreign currency are converted into the capital currency at the relevant daily rate.

Losses on exchange arising from these valuation principles are taken into account in the income statement.

The imparity principle is applied to the valuation results from uncovered items. Covered spot and forward items are valued without effect on the income statement.

### **2.6 Valuation of financial derivatives**

Derivative financial instruments are recorded on the date of the deal conclusion as off-balance sheet items. They are valued at market prices, on the relevant trading date, unless they are being used to hedge against the bank's market risks.

**3. | Notes on the assets**

**3.1 Presentation of assets as at 31st December 2004**

Maturity schedule

| in thousands of €               | Receivables from credit institutions<br>(including central bank balances) |                | Receivables from customers |                |
|---------------------------------|---|----------------|----------------------------|----------------|
|                                 | 31.12.2004  | Previous year  | 31.12.2004                 | Previous year  |
| Payable on demand               | 95,458  | 34,396         | 13                         | –              |
| Up to 3 months                  | 655,488   | 385,460        | 16,192                     | –              |
| More than 3 months up to 1 year | 51,417  | 4,602          | –                          | 20,452         |
| More than 1 year up to 5 years  | 328,335   | 285,179        | 138,119                    | 117,854        |
| More than 5 years               | 225,432   | 236,787        | 417,948                    | 417,628        |
| <b>Total</b>                    | <b>1,356,130</b>  | <b>946,424</b> | <b>572,272</b>             | <b>555,934</b> |
| Of which subordinated claims    | –   | –              | –                          | –              |

The receivables payable on demand from credit institutions include balances with the Central Bank of € 4,403 k.

Receivables from credit institutions include return claims arising from lent securities of € 403,021 k

**3.2 Presentation of receivables and/or bonds and other fixed-income securities vis-à-vis associate companies or companies with which there is a holding relationship**

| in thousands of €                       | Associate companies |                | Companies with which there<br>is a holding relationship |               |
|---|---------------------|----------------|---|---------------|
|   | 31.12.2004          | Previous year  | 31.12.2004  | Previous year |
| Receivables from credit institutions    | 240,000             | 100,484        | –   | –             |
| Receivables from customers              | –                   | –              | –   | –             |
| Bonds and other fixed-income securities | 312,181             | 223,362        | –   | –             |
| <b>Total</b>                            | <b>552,181</b>      | <b>323,846</b> | <b>–</b>  | <b>–</b>      |
| Of which own bonds                      | 172,211             | 65,942         | –   | –             |
| Of which subordinated claims            | –                   | –              | –   | –             |

## 3.3 Breakdown on the basis of standardised risk weightings

| Calculation of balance sheet risk volume in thousands of €        |                  |           |                 |
|---|------------------|-----------|-----------------|
|   | Nominal amount   | Weighting | Risk equivalent |
| Asset items covered by cash deposits internally                   | 350,000          | 0 %       | –               |
| Secured by local administrative bodies of Zone A (20 % weighting) | 20,287           | 20 %      | 4,057           |
| Due from central governments and central banks of Zone A          | 1,672,132        | 0 %       | –               |
| Due from regional and local governments (0 % weighting)           | 1,371,391        | 0 %       | –               |
| Due from regional and local governments (20 % weighting)          | 986,493          | 20 %      | 197,299         |
| Due from credit institutions of Zone A ≤ 1 year                   | 440,738          | 20 %      | 88,148          |
| Due from credit institutions of Zone A > 1 year                   | 271,150          | 20 %      | 54,230          |
| Bonds CI as per circular 10/2000, Part VIII, Point 10.2.          | 760,673          | 10 %      | 76,067          |
| Due from multilateral development banks                           | 258,027          | 20 %      | 51,605          |
| Receivables from other customers                                  | 20,022           | 100 %     | 20,022          |
| Collection items  | 115              | 20 %      | 23              |
| Accruals  | 86,208           | 50 %      | 43,104          |
| Property, plant and equipment                                     | 204              | 100 %     | 204             |
| <b>Total</b>  | <b>6,237,440</b> |           | <b>534,759</b>  |

| Derivatives in thousands of €                                 |                      |             |                 |
|---|----------------------|-------------|-----------------|
|   | Replacement value *) | Weighting   | Risk equivalent |
| <b>Deals without netting</b>                                  |                      |             |                 |
| Interest-related deals ≤ 1 year remaining term                | –                    | 20 %        | –               |
| Interest-related deals > 1 year ≤ 5 years remaining term      | 1.477                | 20 %        | 295             |
| Interest-related deals > 5 years remaining term               | 6.609                | 20 %        | 1.322           |
| Exchange rate-related deals ≤ 1 year remaining term           | –                    | 20 %        | –               |
| Exchange rate-related deals > 1 year ≤ 5 years remaining term | –                    | 20 %        | –               |
| Exchange rate-related deals > 5 years remaining term          | 26.080               | 20 %        | 5.216           |
| <b>Deals with netting</b>                                     | <b>70.950</b>        | <b>20 %</b> | <b>14.190</b>   |
| <b>Total</b>  | <b>105.116</b>       |             | <b>21.023</b>   |

\*) For explanatory note, see point 5.

### 3.4 Information on credit risk

Receivables and bonds and the other fixed-income securities (before deduction of depreciations) are classified as follows as at the balance sheet date:

| in thousands of €  |                  |                       |                         |                  |                  |
|--|------------------|-----------------------|-------------------------|------------------|------------------|
| Remaining term   | ≤ 1 year         | ≥ 1 year<br>≤ 5 years | > 5 years<br>≤ 10 years | > 10 years       | Total            |
| <b>Credit institutions</b>   |                  |                       |                         |                  |                  |
| Europe   | 1,066,854        | 1,030,184             | 604,923                 | 61,216           | 2,763,177        |
| Japan  | 12,783           | 46,784                | 47,692                  | –                | 107,259          |
| Canada   | 21,800           | –                     | –                       | –                | 21,800           |
| USA  | 11,000           | –                     | 19,947                  | –                | 30,947           |
| <b>Total</b>   | <b>1,112,437</b> | <b>1,076,968</b>      | <b>672,562</b>          | <b>61,216</b>    | <b>2,923,183</b> |
| <b>Public sector borrowers (not including credit institutions)</b> |                  |                       |                         |                  |                  |
| Europe   | 162,878          | 683,921               | 718,798                 | 1,118,725        | 2,684,322        |
| Japan  | 51,716           | 113,233               | 71,103                  | 102,815          | 338,867          |
| Canada   | 11,026           | 48,486                | 81,614                  | 208,179          | 349,305          |
| USA  | 3,675            | 70,057                | 1,801                   | 6,861            | 82,394           |
| <b>Total</b>   | <b>229,295</b>   | <b>915,697</b>        | <b>873,316</b>          | <b>1,436,580</b> | <b>3,454,888</b> |
| <b>Other borrowers (not including credit institutions)</b>         |                  |                       |                         |                  |                  |
| Europe   | –                | 19,950                | –                       | –                | 19,950           |
| <b>Total</b>   | <b>–</b>         | <b>19,950</b>         | <b>–</b>                | <b>–</b>         | <b>19,950</b>    |
| <b>Overall total</b>   | <b>1,341,732</b> | <b>2,012,615</b>      | <b>1,545,878</b>        | <b>1,497,796</b> | <b>6,398,021</b> |

### 3.5 Bonds and other fixed-income securities and holdings

| in thousands of €   |                  |                  |
|---------------------|------------------|------------------|
|                     | 31.12.2004       | Previous year    |
| Listed securities   | 4,350,029        | 4,476,585        |
| Unlisted securities | 123,539          | 151,297          |
| <b>Total</b>        | <b>4,473,568</b> | <b>4,627,882</b> |

The bonds and other fixed-income securities becoming due in the following year stand at € 406,571 k.

Bonds of a Member State of the European Union which participates in the Euro, eligible for refinancing at a Central Bank of the Eurozone, stand at a nominal € 3,076 m as at the balance sheet date.

The “Bonds” holding (after deduction of depreciations) is broken down as follows:

| in thousands of € |                  |                  |
|-------------------|------------------|------------------|
|                   | 31.12.2004       | Previous year    |
| Financial assets  | 4,101,361        | 4,561,940        |
| Liquid assets     | 372,207          | 65,942           |
| <b>Total</b>      | <b>4,473,568</b> | <b>4,627,882</b> |

As at the balance sheet date, the accumulated premiums stand at € 4,239 k, accumulated discounts are shown as € 3,112 k. Repurchase commitments under sale and repurchase agreements stand at € 452,619 k.

### 3.6 Other assets

The Other assets heading mainly consists of the outstanding claim on the Association Momentanée Hypo Real Estate ASMO, which handles the settlement of administrative expenses between the HPBI and Hypo Real Estate Bank International, Luxembourg branch. Both entities are run under the same management by HPBI.

### 3.7 Accruals

Accruals mainly involve interest accruals and premium and discount depreciations arising from issuing and lending business. Discounts from issue business stand at € 8,078 k.

## 4. Notes on liabilities

### 4.1 Presentation of liabilities as at 31st December 2004

#### Maturity schedule

| in thousands of €               | Liabilities to credit institutions |                  | Liabilities to customers |                |
|---------------------------------|------------------------------------|------------------|--------------------------|----------------|
|                                 | 31.12.2004                         | Previous year    | 31.12.2004               | Previous year  |
| Payable on demand               | 1,921                              | 2,244            | –                        | –              |
| Up to 3 months                  | 1,186,869                          | 1,165,931        | 25,000                   | –              |
| More than 3 months up to 1 year | 25,000                             | 55,000           | 3,000                    | –              |
| More than 1 year up to 5 years  | –                                  | –                | –                        | 28,000         |
| More than 5 years               | 40,000                             | 20,000           | 673,857                  | 134,200        |
| <b>Total</b>                    | <b>1,253,790</b>                   | <b>1,243,175</b> | <b>701,857</b>           | <b>162,200</b> |

Out of liabilities to credit institutions, € 452,619 k arises from sale and repurchase agreements.

| Debts evidenced by certificates as at 31.12.2004 in thousands of € |                              |                |                |                  |
|--|------------------------------|----------------|----------------|------------------|
|  | Public sector<br>Pfandbriefe | Other<br>bonds | Other          | Total            |
| Payable on demand  | –                            | –              | –              | –                |
| Up to 3 months   | 434.300                      | –              | 100.000        | 534.300          |
| More than 3 months up to 1 year                                    | 950.000                      | –              | 22.000         | 972.000          |
| More than 1 year up to 5 years                                     | 3.124.600                    | –              | –              | 3.124.600        |
| More than 5 years  | 180.931                      | –              | –              | 180.931          |
| <b>Total</b>   | <b>4.689.831</b>             | <b>–</b>       | <b>122.000</b> | <b>4.811.831</b> |

Securitized liabilities falling due in the next year amount to € 1,506,300 k.

#### 4.2 Presentation of liabilities to associate companies or companies with which there is a holding relationship

Liabilities to associate companies consist of one securities loan transaction of € 200 m.

#### 4.3 Other liabilities

The other liabilities as at the balance sheet date mainly consist of outstanding payments for various accounts.

#### 4.4 Deferred income

Deferred income mainly consists of interest deferrals and premiums and discounts.

#### 4.5 Provisions

The other provisions shown were set up for liabilities to staff existing as at the balance sheet date, together with liabilities to third parties applying to the previous financial year (audit costs, consultation costs, etc.).

#### 4.6 Subordinated liabilities

As at 28th December 2000, the bank accepted a “silent participation” of € 9,000,000. The term was indefinite, with profit-related interest. For bank regulatory purposes, this had to be classified as upper Tier II capital. With effect from 1st January 2003, the silent participation was converted into a subordinated debt issue. The interest is still profit-related, the term remains indefinite, and the regulatory classification is upper Tier II capital. In the year under review, interest of € 753 k was charged to the income statement.

On 18th May 2001, the bank issued subordinated debt of € 15,000,000. The subordinated debt which is to be repaid in instalments as from 18th May 2017 will be finally repaid on 18th May 2026, the interest rate being 6.8 % p.a. The subordinated debt was increased by € 10,000,000 to € 25,000,000 on 30th January 2002 with the same loan conditions. In the year under review, interest of € 1,703 k was charged to the income statement. For bank regulatory purposes, this is classified as supplementary Tier II capital.

#### 4.7 Equity capital

The subscribed capital is € 66,000 k and is divided into 66,000 no par value registered shares.

Under the Luxembourg Law of 10th August 1915 on commercial companies, the bank must allocate a sum equivalent to at least 5 % of its annual net profit to a statutory reserve every year, until such time as the reserve reaches 10 % of the subscribed capital. No distribution may be made from the statutory reserve. As at the balance sheet date, there was a statutory reserve of € 625 k and retained earnings of € 8,745 k.

The bank exercises the tax credit option for property tax payment purposes. The retained earnings contain € 5,000 k for the property tax credit. Another appropriate allocation to reserves will be made for the year under review.

In accordance with the proposed appropriation of profit, a sum of € 250 k is to be allocated to the statutory reserves and € 4,351 k to retained earnings.

#### 4.8 Assets deposited as security for own liabilities

Assets of a nominal amount of € 20,000 k have been deposited with the Central Bank as security.

### 5. | Notes on the off-balance sheet items

#### 5.1 Derivative financial instruments

Transactions in derivative instruments on the OTC market are effected exclusively for hedging purposes as part of the bank's asset/liability management process. No trading operations involving derivatives were conducted. We have, as a general rule, entered into netting agreements with our trading partners in derivative business as a risk reduction measure.

During the year under review, we included a very small number of interest rate and currency swaps in the cover pool. We have entered into contractual agreements with the counterparties concerned to regulate the duties of information and co-operation obligations. The procedure has been approved by the regulatory authorities and the trustee.

At the end of 2004, the nominal volume of the outstanding off-balance sheet transactions was € 8,797 m, out of which € 58 m involved associate companies. The counterparty risk arising from derivatives was determined, inter alia, on the basis of the gross replacement value (replacement costs). This is calculated as the total of all positive market values, not taking into account netting agreements. At the end of 2004, the counterparty risk defined in this way (maximum risk of default) was € 230 m, or 2.6 % of the outstanding nominal volume. Once netting agreements are taken into account, the counterparty risk is reduced to € 93 m.

If, in accordance with banking regulatory standards, the add-ons together with risk weightings are additionally taken into account for potential future risk, there is a counterparty risk using the market value method of € 21 m at the end of 2004. We shall also be very careful in future to ensure that the counterparty risk is kept within tight confines through active management. Our counterparties in derivative business are all OECD banks.

| in millions of €                     |  |  |   |                            |                              |                            |
|--------------------------------------|--|--|---|----------------------------|------------------------------|----------------------------|
|                                      | Nominal amount<br>Remaining term<br>≤ 1 year | Nominal amount<br>Remaining term<br>≤ 5 year | Nominal amount<br>Remaining term<br>> 5 years | Total<br>nominal<br>amount | Positive<br>market<br>values | Counter-<br>party<br>risks |
| <b>Interest-related transactions</b> |  |  |   |                            |                              |                            |
| IR swaps (same currency)             | 1,432  | 2,691  | 2,536   | 6,659                      | 119                          |                            |
| Interest rate options – purchases    | –  | 131  | 82  | 213                        | 3                            |                            |
| Interest rate options – sales        | –  | 30   | 62  | 92                         | –                            |                            |
| Other interest rate contracts        | –  | –  | –   | –                          | –                            |                            |
| <b>Currency-rated transactions</b>   |  |  |   |                            |                              |                            |
| Foreign exchange swaps               | 959  | –  | –   | 959                        | 12                           |                            |
| Cross-Currency-Swaps                 | 162  | 483  | 229   | 874                        | 96                           |                            |
| <b>Total</b>                         | <b>2,553</b>                                 | <b>3,335</b>                                 | <b>2,909</b>                                  | <b>8,797</b>               | <b>230</b>                   | <b>21</b>                  |

### 5.2. Firm credit commitments

During the year under review, a commercial property credit was granted for the first time. Out of a total commitment of € 21 m, € 20 m was drawn as at 31st December 2004.

## 6. | Notes to the income statement

### 6.1 Geographical origin of income

The bank's income were primarily sourced from business relationships with counterparties registered in Europe.

### 6.2 Balance of expenses/income from financial transactions

This item contains the results from securities attributed to liquid assets. The voting right arising from Article 62 of the "Law" was not utilised.

### 6.3 Other operating income

Other operating income involves the adjustment for liabilities arising from Turnover Tax to be paid to the Tax Office and the writing back of provisions.

## 7. | Other explanatory notes

### 7.1 Staff

The average staff numbers employed during the year were as follows:

Management, including departmental managers: 6.0

Other staff: 15.0

At the end of the year, the management team comprised two individuals. There were another 22 employees on the staff.

### 7.2 Payments and loans to management and supervisory bodies

No loans have been granted to members of the executive bodies (management) or to other members of the Board of Directors.

The members of the executive bodies (managers and departmental managers) were paid salaries totalling € 900,100 for the financial year.

### 7.3 Deposit guarantee system

The bank is a member of the “Association pour la Garantie des Dépôts, Luxembourg” (AGDL) and, through this, a member of the deposit guarantee association of the banking sector in the Grand Duchy of Luxembourg. It was not necessary to set up a reserve.

### 7.4 Items not denominated in the balance sheet currency

The total amount of assets in foreign currency (not including € currencies) is € 1,284,188 k. At the end of the year, liabilities in foreign currencies were € 1,873,539 k. These items are virtually all covered by currency and interest/currency swaps.

## 8. | Asset overview

| Asset overview in thousands of € |                    |                         |                          |                             |                          |                                |                                   |
|----------------------------------|--------------------|-------------------------|--------------------------|-----------------------------|--------------------------|--------------------------------|-----------------------------------|
|                                  | Acquisition costs  | Accruals Financial year | Disposals Financial year | Depreciation Financial year | Accumulated depreciation | Residual book value 31.12.2004 | Residual book value Previous year |
| Office and business equipment    | 2,303.6            | 78.7                    | -1,778.5                 | -132.7                      | -493.6                   | 110.2                          | 200.0                             |
| of which computer equipment      | 1,979.4            | 44.7                    | -1,692.1                 | -77                         | -287                     | 44.7                           | 76.7                              |
| Investment securities            | 4,561,939.8        | 185,714.0               | -646,293.0               | -                           | -                        | 4,101,360.8                    | 4,561,939.8                       |
| <b>Total</b>                     | <b>4,564,243.4</b> | <b>185,792.7</b>        | <b>-648,071.5</b>        | <b>-132.7</b>               | <b>-493.6</b>            | <b>4,101,471.0</b>             | <b>4,562,139.8</b>                |

## 9. | Special information

### Statement of covering assets held in accordance with Art. 12-1 to 12-9 of the Law of 5th April 1993 on the financial sector

The information is confined to the presentation of public sector Pfandbriefe. No mortgage-backed Pfandbriefe were issued. Derivative financial instruments with a total value of € 44,897 k were used for cover as at the balance sheet date.

#### 9.1 Statement of covering assets for public sector Pfandbriefe

| in €                                       |                      |
|--|----------------------|
| Covering assets                            | 5,094,952,147        |
| Substitute cover assets                    |                      |
| Securities                                 | -                    |
| Bank balances                              | -                    |
| <b>Total cover</b>                         | <b>5,094,952,147</b> |
| In circulation                             |                      |
| Bearer securities                          | 4,518,431,822        |
| Registered securities                      | 319,071,410          |
| <b>Total circulation (requiring cover)</b> | <b>4,837,503,232</b> |
| <b>Surplus cover</b>                       | <b>257,448,915</b>   |

## 9.2 Additional breakdown

### 9.2.1 Covering assets

| Standard cover in €   |                      |
|---|----------------------|
| Receivables from credit institutions                                |                      |
| Municipal loans or credits guaranteed by public institutions        | 575,173,035          |
| Receivables from customers  |                      |
| Municipal loans or credits guaranteed by public institutions        | 552,313,575          |
| Bonds of public sector issuers or guaranteed by public institutions | 3,269,474,962        |
| Covered public sector Pfandbriefe                                   | 653,093,471          |
| Derivative products   | 44,897,104           |
| <b>Sub-total</b>  | <b>5,094,952,147</b> |
| Substitute cover assets   |                      |
| Other receivables from credit institutions                          | –                    |
| Bonds under Art. 42 (3) of the UCITS Act                            | –                    |
| Cash  | –                    |
| <b>Total</b>  | <b>5,094,952,147</b> |

### 9.2.2 Cover pool

| Breakdown according to size categories |        |                      |
|--|--------|----------------------|
|  | Number | in €                 |
| Up to € 10 million                     | 29     | 147,325,033          |
| Up to € 25 million                     | 27     | 437,872,729          |
| Over € 25 million                      | 70     | 4,509,754,385        |
| <b>Total</b>                           |        | <b>5,094,952,147</b> |

| Breakdown by country |                      |              |
|----------------------|----------------------|--------------|
|                      | in €                 | as a %       |
| Germany              | 1,830,081,434        | 35.9         |
| Italy                | 888,070,309          | 17.4         |
| Canada               | 304,284,349          | 6.0          |
| Switzerland          | 353,321,243          | 6.9          |
| Int. organisations   | 293,579,193          | 5.8          |
| Japan                | 265,063,622          | 5.2          |
| Spain                | 159,888,233          | 3.1          |
| Austria              | 203,866,353          | 4.0          |
| Belgium              | 165,687,379          | 3.3          |
| Finland              | 112,649,482          | 2.2          |
| USA                  | 101,582,842          | 2.0          |
| Portugal             | 125,000,000          | 2.5          |
| France               | 117,033,348          | 2.3          |
| Sweden               | 68,004,647           | 1.3          |
| Luxembourg           | 52,000,000           | 1.0          |
| United Kingdom       | 51,882,202           | 1.0          |
| Denmark              | 2,957,511            | 0.1          |
| <b>Total</b>         | <b>5,094,952,147</b> | <b>100.0</b> |

### 9.2.3 Statement of covering assets by net present value

| in millions of €                        |            |  |               |        |
|---|------------|--|---------------|--------|
|   | Cover fund | Public sector Pfandbriefe requiring cover *) | Surplus cover | as a % |
| Nominal                                 | 5,095      | 4,838  | 257           | 5.3    |
| Net present value                       | 5,662      | 4,931  | 731           | 14.8   |
| Net present value if yield curve shifts |            |  |               |        |
| + 100 bp                                | 5,431      | 4,841  | 590           | 12.2   |
| - 100 bp                                | 5,892      | 5,021  | 871           | 17.3   |

\*) Lettres de gage publiques

### 9.3 Accruals and deferred income

| in €                              |                    |
|-----------------------------------|--------------------|
| <b>Accruals</b>                   |                    |
| Interest accruals                 | 181.853.991        |
| From issuing and lending business | 434.740.034        |
| Other                             | 75.115.823         |
| <b>Total</b>                      | <b>691.709.848</b> |
| <b>Deferred income</b>            |                    |
| Interest deferrals                | 178.032.773        |
| From issuing and lending business | 4.650.023          |
| Other                             | 10.684.064         |
| <b>Total</b>                      | <b>193.366.860</b> |

### 9.4 Own public sector Pfandbriefe redeemed

During the year under review, we redeemed nominal € 288 m of our own public sector Pfandbriefe for price regulating purposes. In the course of this process, we were able to place nominal € 100 m own bonds back on the market. A volume of € 49.2 m was redeemed as scheduled and € 32.4 m was redeemed prior to final maturity by the trustee. A holding with a book value of € 172.2 m is shown as at the balance sheet date. Further placement in the market is planned, where current market conditions permit.

### 9.5 Interest arrears

The interest due from receivables and securities during the year has been received in full.

There are no arrears. No depreciations or adjustments have been made on interest.

## Executive bodies

#### Board of Directors

|                                 |  |
|---------------------------------|--|
| <b>Stephan Bub</b>              | Member of the Board of Directors of Hypo Real Estate Bank International, Westport from 26th March 2004               |
| <b>Eckehard Dettinger-Klemm</b> | Member of the Board of Directors of Hypo Real Estate Bank International, Dublin (Chairman of the Board of Directors) |
| <b>Dr. Paul Eisele</b>          | Spokesman of the Board of Directors of Württembergischen Hypothekenbank AG, Göppingen from 1st August 2004           |
| <b>Dr. Markus Fell</b>          | Member of the Board of Directors of Hypo Real Estate Holding AG, Sandycove   |
| <b>Theodor Knepper</b>          | Member of the Board of Directors of Hypo Real Estate Bank AG (Germany), Riemerling up until 26th March 2004          |
| <b>Ralph Brödel</b>             | Administrateur-Délégué, Trier  |
| <b>Gerhard M. Kainz</b>         | Administrateur-Délégué, Luxembourg up until 31st July 2004   |
| <b>Martin Schulte</b>           | Administrateur-Délégué, Trier  |

#### Management

|                         |  |
|-------------------------|--|
| <b>Ralph Brödel</b>     | Administrateur-Délégué                         |
| <b>Gerhard M. Kainz</b> | Administrateur-Délégué up until 31st July 2004 |
| <b>Martin Schulte</b>   | Administrateur-Délégué                         |

#### Réviseur Spécial

PricewaterhouseCoopers S.à.r.l.

Layout: medienfabrik trier GmbH  
Pictures: City of Arts and Sciences in Valencia, Spanien  
Architect: Santiago Calatrava





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