

Press release

Hypo Real Estate Group continues to be profitable in Q2

- **Adjusted pre-tax profit up to € 40 million compared with Q1**
- **Core capital ratio has increased to 8.6%**
- **CDO effects of € 145 million recognised in results**
- **High-interest and high-margin new business in Public Sector Finance**
- **Positive pre-tax results at all operating business segments**
- **Market conditions are still uncertain and difficult**

Munich, 13 August 2008 – The Hypo Real Estate Group has again operated profitably in the second quarter of 2008 despite unfavourable market conditions. Pre-tax profit, calculated without the effect of the Mandatory Convertible Bond issued for financing the DEPFA acquisition, has improved to € 40 million (Q1: € 6 million). All operating business segments – Commercial Real Estate Financing, Public Sector & Infrastructure Finance as well as Capital Markets & Asset Management – have reported positive pre-tax results. There has been a particularly positive development in net interest income in Public Sector Finance. The core capital ratio increased to 8.6% as of 30 June, compared with 8.3% at the end of March 2008.

In the second quarter of 2007, before the outbreak of the international financial crisis, the pro-forma consolidated pre-tax profit calculated including DEPFA figures amounted to € 320 million.

The current pre-tax profit includes revaluations of € 145 million in the CDO portfolio recognised in the income statement, with which the Hypo Real Estate Group reflects the market environment. Such valuation changes had a negative impact of € 175 million upon results in the first quarter.

With regard to new business in the second quarter, the Hypo Real Estate Group again gave priority to reducing risk and assuring liquidity ahead of achieving higher market shares, particularly in infrastructure and real estate financing. In the field of public sector finance, the company again succeeded in generating above-average margins of around 40 basis points and yields in excess of 30%.

"We have presented a respectable result in view of the difficult conditions. This result confirms our course of continuing to focus on safety in terms of new business as well as risk and cost management", says **CEO Georg Funke**. "The next months will continue to be challenging for the entire financial sector. The fact that market prospects are still uncertain means that it is almost impossible to make reliable forecasts. However, one aspect has been demonstrated by recent months: Our business model is profitable, particularly following the acquisition of DEPFA, even in this difficult market climate. Its two main pillars, namely commercial real estate and public finance, are strong and viable on the basis of strict risk management and on-balance-sheet lending. This assessment should be fundamentally confirmed by developments in the remainder of the year unless further external shocks dash all the hopes of market participants."

Group development, an overview (in € million)

Hypo Real Estate Group	2nd Quarter 2008	1st Quarter 2008	2nd Quarter 2007 (Pro forma)	H1 2008	H1 2007 (Pro forma)
Operating performance					
Operating revenues	236	184	520	420	1,018
Net interest income and similar income	304	299	335	603	674
Net commission income	34	35	55	69	109
Net trading income	12	-98	23	-86	51
thereof: Valuation result on synthetic CDOs affecting income	-19	-87	-	-106	-
Net income from financial investments	-135	-29	86	-164	163
thereof: Valuation result on cash CDOs affecting income	-126	-88	-	-214	-
Net income from hedge relationships	15	-19	19	-4	19
Balance of other operating income/expenses	6	-4	2	2	2
Provisions for losses on loans and advances	37	33	30	70	64
General administrative expenses	160	145	170	305	330
Balance of other income/expenses (including effects from the Depfa acquisition)	-22	184	-	162	-
Pre-tax profit ¹	17	190	320	207	624
Effects from the Depfa acquisition	-23	184	-	161	-
Pre tax profit²	40	6	320	46	624
Net income/loss³	29	11	-	40	-
Net income/loss IFRS	12	148	-	160	-

¹ including the effect from the embedded derivative relating to the Mandatory Convertible Bond

² excluding the effect from the embedded derivative relating to the Mandatory Convertible Bond

³ excluding the effect from the embedded derivative relating to the Mandatory Convertible Bond; including the effects from capitalised losses carried forward relating to other periods

Group development Q2 2008

- Operating revenues (sum of net interest income and similar income, net commission income, net trading income, net income from financial investments, net income from hedge relationships and the balance of other operating income / expenses) were reported as € 236 million in the second quarter of 2008, which was considerably higher than the figure of € 184 million reported for the previous quarter. It was not possible to repeat the pro forma figure of € 520 million (including DEPFAs) for the second quarter of 2007 as a result of the international financial crisis and the associated value adjustments in relation to the CDO portfolio recognised in the income statement.
- Compared with the previous quarter, net interest income and similar income improved slightly to € 304 (299) million. This was due to various factors, including the positive development in margins in the public sector finance portfolio. The figure for the second quarter of 2007 was € 335 million.
- Net commission income of € 34 (35) million remained at the relatively low level seen in the previous quarter, and was thus considerably lower than the figure of € 55 million reported for the previous year. This reflects mainly the conservative new business in real estate and infrastructure financing.
- On this occasion, trading reported a positive result of € 12 million (previous quarter: € -98 million). This includes negative valuation effects on CDOs of € 19 (87) million. Net trading income in the second quarter of 2007 amounted to € 23 million.
- Net income from financial investments was reported as € -135 million, considerably lower than the figure of € -29 million for the previous quarter and far below the previous year figure of € 86 million. This development is due to negative valuation effects on CDOs of € 126 reflected in this position (previous quarter: € 88 million). In addition, the previous quarter figure benefited from the effect of the initial consolidation of Quadra Realty Trust. In the second quarter of 2008, the positive result attributable to the planned sale of a property of Hypo Real Estate Bank in Munich was offset by

an impairment of a similar amount in relation to the equity participation in Babcock & Brown.

- With regard to the valuation of the Group portfolio of Collateralised Debt Obligations (CDO), the Hypo Real Estate Group has reduced the model reserve which was created and recognised in the income statement in 2007 with regard to uncertainty for the assumptions and estimates which have been made; it has been reduced from € 90 million to around € 20 million. **CFO Dr. Markus Fell** explained: "The fact that the model reserve has been to a large extent released was appropriate because the risks attributable to the method of valuing the CDO portfolio are now of manageable proportions. This is also applicable for the possible extent of the value adjustments which still have to be made. We are assuming that any necessary CDO adjustments which will have to be recognised in the income statement will to a large extent have been completed by the end of 2008."
- Net income from hedge relationships has improved appreciably to € 15 million (previous quarter: € -19 million), and was thus just lower than the corresponding previous year level of € 19 million.
- Provisions for losses on loans and advances in the second quarter were higher than the corresponding figure for the previous quarter (€ 37 million compared with € 33 million) and also higher than the corresponding figure for the second quarter of 2007 (€ 30 million). This item was however still below the pro-rata forecast for 2008.
- General administrative expenses of € 160 million were € 10 million lower than the corresponding previous year, but they were € 15 million higher than in the first quarter of 2008. This discrepancy reflects synergies attributable to the integration of DEPFA. On the other hand, the selection process in connection with the participation of strategic investors in the Hypo Real Estate Group resulted in consultancy fees of € 10 million.

- At € -22 million (previous quarter: € +184 million) the balance of other income / expenses was again dominated by the mandatory market valuation of a derivative based on shares of Hypo Real Estate Holding AG, which is embedded in the mandatory convertible bond issued for partially financing the DEPFA acquisition. Following the mandatory conversion of the bond into shares of Hypo Real Estate Holding AG on 20 August 2008, this aspect will not have any further effects recognised in the income statement.
- Adjusted correspondingly by the effect from the embedded derivative, and also including the CDO valuation adjustments, consolidated pre-tax profit increased to € 40 million (previous quarter: € 6 million). Even including the effect from the embedded derivative of € -23 (+184) million attributable to the mandatory convertible bond, the Group was still profitable at € 17 (190) million, although this figure is significantly lower than the corresponding previous year figure of € 320 million.
- After taxes of € 5 million net income in the second quarter (according to IFRS) amounted to € 12 million (previous quarter: € 148 million). This amount is attributable entirely to the shareholders, because there are no minority interests. The result very much reflects the effects from the embedded derivative. After being adjusted by the post-tax effect from the embedded derivative relating to the mandatory convertible bond (€ -17 million), net income amounted to € 29 million (previous quarter: € 11 million).

Net assets and capital ratios as of 30 June 2008

- The total assets of the Hypo Real Estate Group amounted to € 395.4 billion as of 30 June 2008, compared with € 400.2 billion as of 31 December 2007.
- As of 30 June 2008, the volume of lending amounted to € 257.3 billion, compared with € 256.2 billion at the end of 2007.
- At the end of June 2008, the Group reported financial investments of € 98.8 billion, representing growth of around € 9.9 billion compared with the end of 2007 (€ 88.9 billion). Of this total figure, € 93.6

billion (31 December 2007: € 82.2 billion) was attributable to Available-for-Sale (AFS) financial investments. These consist mainly of government paper with a very low risk profile.

- The AfS reserve declined by around € 0.5 billion to € -1.8 billion in the second quarter. This decline is due to changes in the prices of AfS financial instruments which are not recognised in the income statement and which, in accordance with IFRS, have to be recognised irrespective of the risk profile of the instrument as of the reference date. Accordingly, the market-related widening of credit spreads for government paper of countries such as Italy, Greece or the USA resulted in a decline of € 560 million in the revaluation reserve in the second quarter of the year although there is no significant default risk with regard to such paper. Securities issued by sovereigns with a high credit rating account for approximately 70% of the negative AfS reserve.
- The consistent risk and business management of the Hypo Real Estate Group has been reflected in a significant improvement in the core capital ratio. As of the balance sheet date, this ratio was reported as 8.6%, considerably higher than the level of 8.3% as of 31 March 2008, and was thus also higher than the figure of 7.0% as of 31 December 2007 which was still calculated in accordance with Basel I. The own funds ratio improved to 11.3% as of 30 June 2008, compared with 10.9% as of 31 March 2008 and 9.4% at the end of 2007 (in accordance with Basel I).

New business

- New business in commercial real estate financing amounted to € 2.6 billion in the second quarter, compared with € 3.1 billion in the first quarter of the year. It was thus considerably lower than the corresponding previous year figure of € 9.4 billion. The internal rate of return (IRR) after taxes on new business was again above 15%.
- New public sector finance business was reported as € 11.3 billion in the second quarter (Q1 2008: € 15.1 billion), and thus remained at a high level in the first half of 2008 (€ 26.4 billion compared with € 29.7 billion in H1 2007). At around 40 basis points, the net margin in this low-risk business was again excellent.
- The Hypo Real Estate Group was very cautious with regard to new infrastructure financing business (€ 0.4 billion) as a result of the market conditions. In the first half of 2008, the overall level of € 2.0 billion was € 3 billion lower than the corresponding previous year figure.

Result of the operating segments

- The Commercial Real Estate segment, which comprises the German and international commercial real estate financing business, reported pre-tax profit of € 130 million in the second quarter of 2008 (previous quarter: € 164 million). The main factor behind this decline was the fact that no financial investments were sold. Such sales had resulted in income of € 23 million in the first quarter. Net interest income and net commission income as well as net trading income continued to be relatively stable, and provisions for losses on loans and advances increased slightly to € 25 (23) million.

- The Public Sector & Infrastructure Finance segment, which mainly comprises the public sector and infrastructure finance business of DEPFA, reported pre-tax profit of € 151 million, which was lower than the figure of € 172 million for the previous quarter. The strong increase in net interest income was a positive development. At € 179 million, this item was much higher than the figure reported for the previous quarter (€ 157 million) and the previous year quarter (€ 133 million). However, this positive development was opposed by the decline in net trading income, which resulted from a widening of spreads in June.
- The Capital Markets & Asset Management segment benefited from a strong increase in net trading income. Overall, pre-tax profit improved to € 36 million, compared with € -19 million in the previous quarter.

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Note for editors

An analyst call will be held today at 08:00 hours with Dr. Markus Fell, CFO of the Hypo Real Estate Group; this will also be broadcast in the internet under www.hyporealestate.com.

Hypo Real Estate Group

Following the acquisition of DEPFA Bank plc in October 2007, **Hypo Real Estate Group** has evolved into one of the leading international financial services providers for commercial real estate lending, public finance and infrastructure finance. The Group, with total assets of € 395 billion, 1,900 employees and offices across Europe, the Americas and Asia, consists of the non-operational listed Hypo Real Estate Holding AG and operational entities. Hypo Real Estate Bank International AG and Hypo Real Estate Bank AG conduct the international real estate financing business. DEPFA and DEPFA Deutsche Pfandbriefbank AG conduct the public sector and infrastructure finance business. Additional information is to be found on www.hyporealestate.com.