



Cost Savings Potential at Aareal – Outside-in Analysis

April 2021

- Petrus Advisers have – with external help – analysed the salary, bonus and pension cost structure of Aareal’s German banking operations⁽¹⁾ – only for this part of the group we estimate cost savings potential of €20-37 million
- Key issues identified include:
 - 1 Leadership structure**
 - Too many leadership levels (especially the General Managing Director level) and too many management roles
 - Eliminating one leadership level will result in savings that we estimate at €3-5 million per year
 - 2 Oversized and overpaid Management Board**
 - Aareal’s Management Board has 6 members with individual compensation significantly above benchmark
 - We estimate savings potential of €4-6 million per year from reducing the number of members to 3-4 and aligning compensation more with benchmark levels
 - 3 Compensation levels**
 - At €149k / employee, Aareal Bank⁽¹⁾ boasts the highest average salaries of any German bank we have analysed⁽²⁾
 - A reduction by 10-20% would result in savings of an estimated €14-27 million per year or €10-21 million excluding the Management Board savings

⁽¹⁾ Defined as Aareal Group excluding Aareon AG, German part only.

⁽²⁾ 2018 data; 2017 data used for pbb.

4 Excessive pension cost

- Especially the Management Board has excessive pension rights (yearly contribution representing 15% of total fixed salary plus full target bonus (even if the bonus is not fully achieved) and a guaranteed 4% annual yield on such contributions)
- While it is difficult to analyse the total pension situation at Aareal outside-in, expert discussions suggest an estimated €3-5 million cost savings potential per year
- In addition, we believe there is a very substantial capital gain opportunity of €30-50 million from hiving off a portion of the pension liability to dedicated service providers

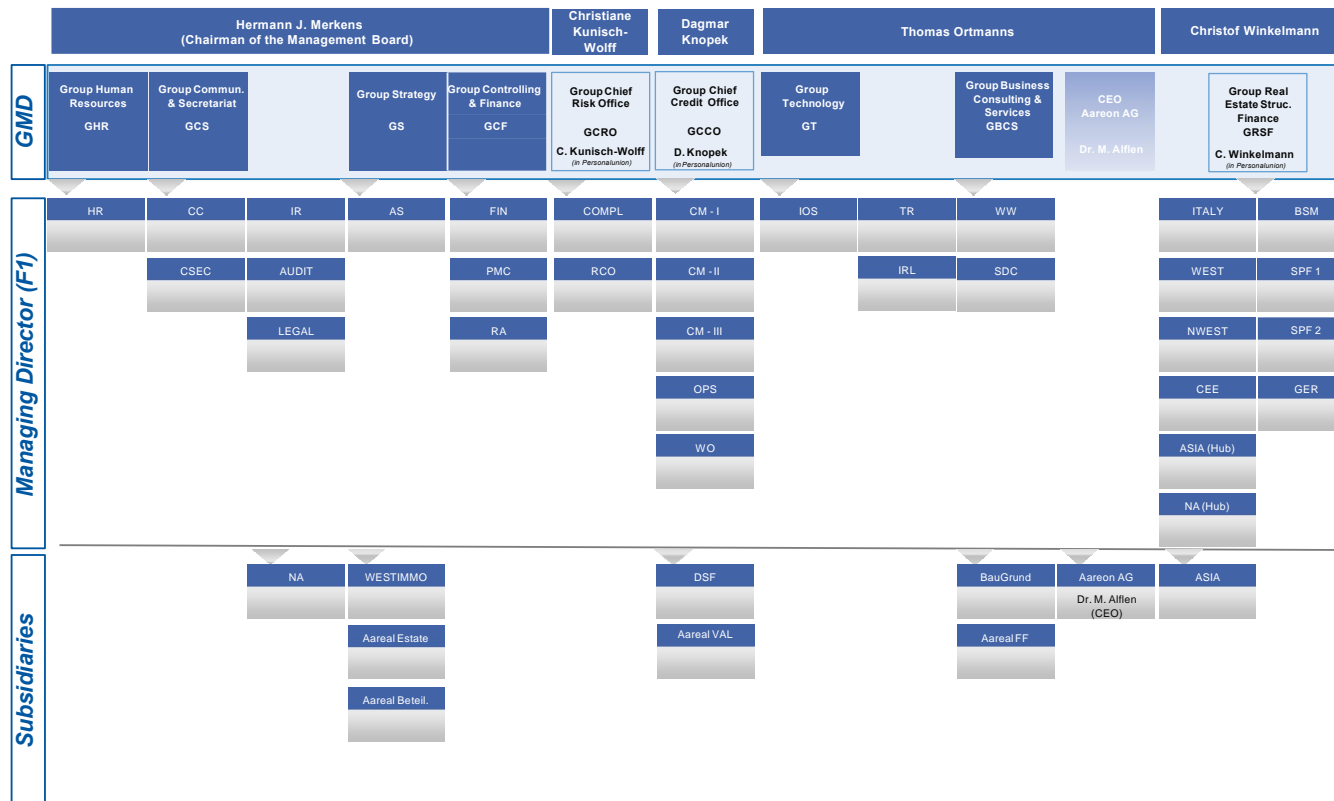
Annual Savings Potential (€m)		Low	High
1	Leadership Structure	3	5
2	Mgt Board Size & Compensation	4	6
3	Bank Compensation Level	10	21
4	Pension Cost	3	5
Total		20	37

- While we appreciate that our work had to be performed outside-in, the results point to significant remuneration issues also below the Management Board level
 - We therefore recommend an independent review of Aareal Bank’s leadership structure, compensation structure and level as well as in particular the pension system for German employees be undertaken

1 Leadership Structure: Too Many Chiefs...

- Aareal Bank has too many leadership levels (F3 – GMD and E3 – E1) and too many very senior roles – especially the GMD and F1 level add complexity and high cost
- Organisations of Aareal's size do typically not have a GMD level
- Eliminating one leadership level would in our view save some €3-5 million

Leadership Structure of Aareal Bank AG (2018 Organizational Chart)

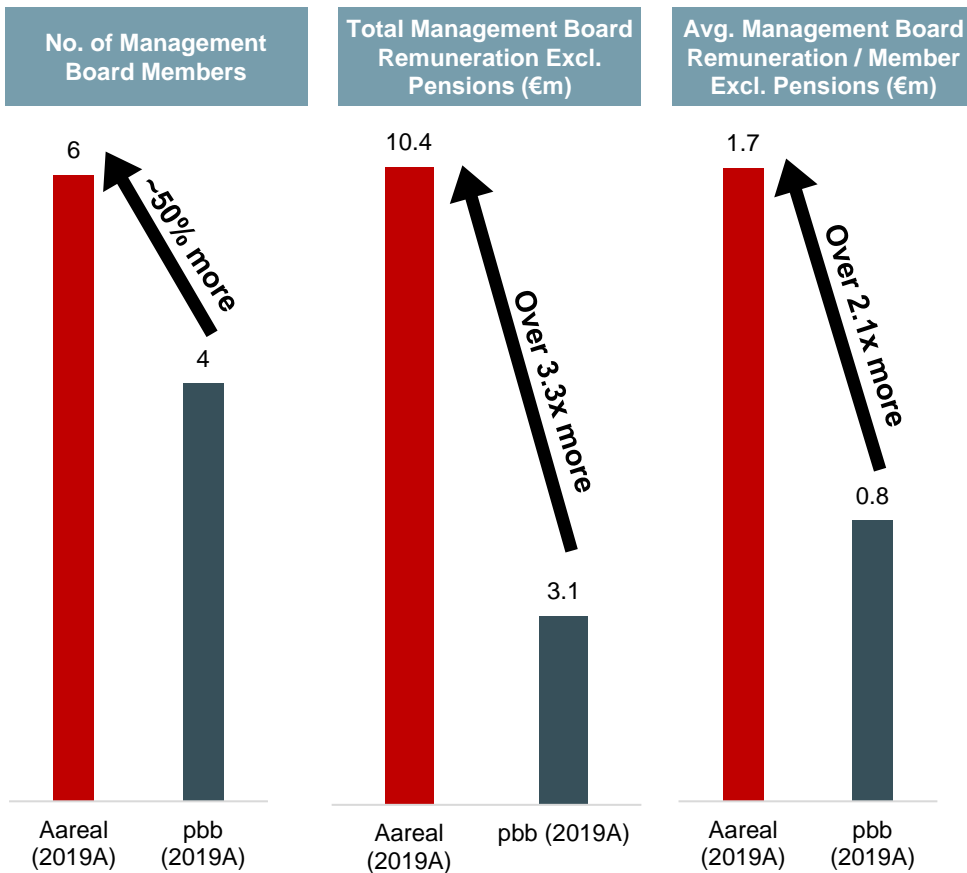


Sources: Aareal Bank AG (2018); zeb-Research; Die Bank 07/2019; V. Ashiagbor et al.: Business Effectiveness Benchmarking Survey (...), PWC 2016; B. Davison: Management Span of Control (...), Journal of Business Strategy 24/2003 (4), S. 22-29; J. Dörich et al.: Die "richtige" Führungsspanne (...), Betriebspraxis & Arbeitsforschung 227/2016, S. 30-36; G. Neilson et al.: Management Spans and Layers (...), Booz Allen Hamilton 2003

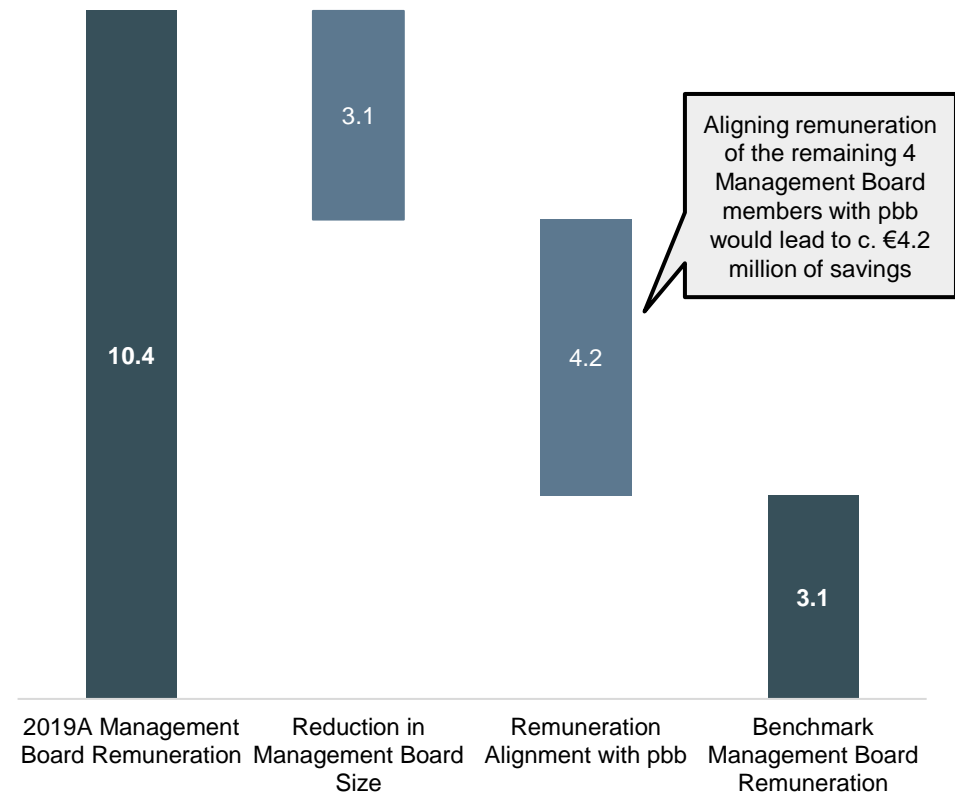
2 Oversized and Overpaid Management Board

By reducing the number of Management Board members to 3-4 and aligning its compensation closer to peers, we estimate a savings potential of €4-6 million per year

Management Board Compensation: Aareal vs pbb



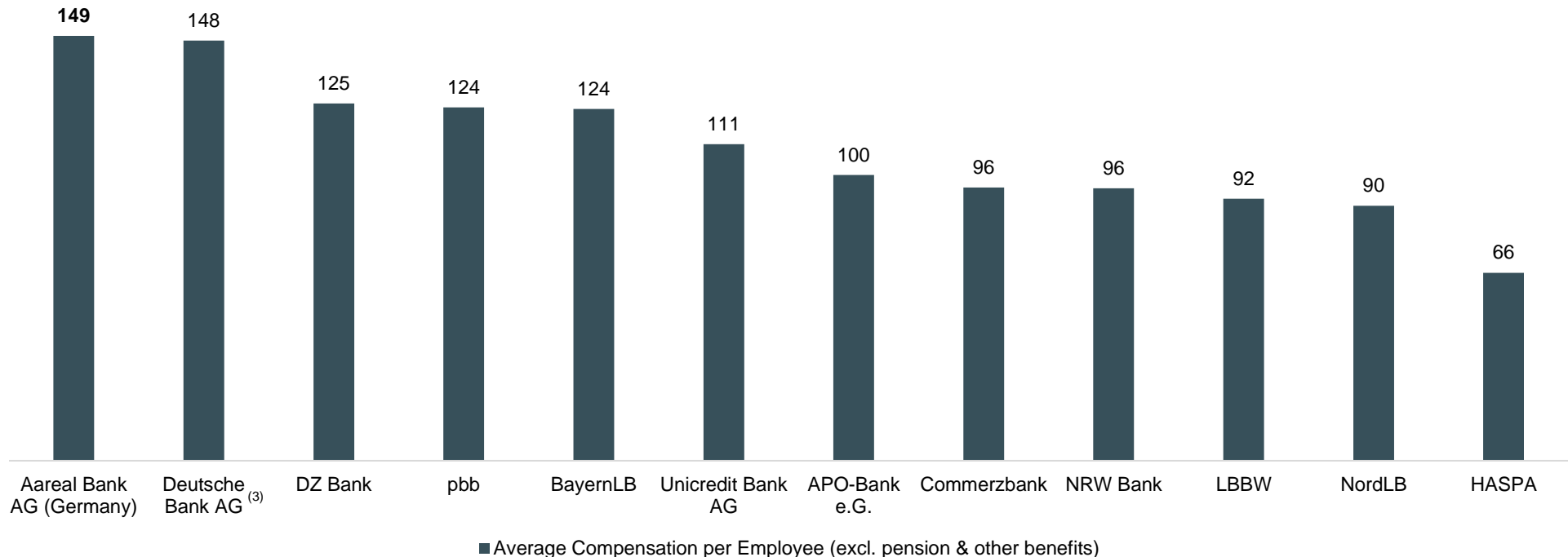
There Is a ~€7 million Cost Saving Potential on Alignment of Remuneration and Size of Management Board (€m)



3 Oversized Average Compensation Levels at Aareal Bank

- At €149k / employee, Aareal Bank AG's⁽¹⁾ average compensation (Germany organisation excluding pension benefits and other benefits) is the highest amongst all German banks in our ranking
- A 10-20% reduction (to be achieved over time) – which would take Aareal closer to benchmark – suggests a cost savings potential of some €14-27 million⁽²⁾ or €10-21 million considering the Management Board savings potential

Benchmarking of Average Cost Per Employee Across Peers (Wages and Salaries Only, in €k, 2018A)



(1) Aareal Bank defined as the German employees of Aareal group excluding Aareon AG.

(2) Assuming c. 880 relevant employees in the German banking operation of Aareal Bank and c. 20% part-time workers.

(3) Excluding Postbank.

Source: Annual reports; Aareal Bank AG (2018); BdB; BVR; DSGVO; VÖB / Total annual compensation = fixed and variable compensation excluding pension and other benefits (e.g. company cars, etc.)

4 Aareal Bank's Overly Generous Pension Plans Offer Savings Potential of at Least €3-5m

- Aareal has a legacy of numerous defined benefit and define contribution plans
- While from outside-in, transparency on Aareal's pension cost situation is limited, it appears that a significant cost savings potential exists
- An overview of the pension cost / provisions of the Management Board demonstrates that the total cost is not only related to annual pension cost / contribution but to a large extent to the valuation of the underlying pension claims:

(€m)	2020				2019			
Name	Pension Cost	Change in Pension Provision	Delta	Delta as % of Pension Cost	Pension Cost	Change in Pension Provision	Delta	Delta as % of Pension Cost
H. Merkens	0.9	1.9	1.0	115%	0.8	2.3	1.5	191%
M. Heß	0.6	0.9	0.2	37%	0.5	0.8	0.2	45%
D. Knopek	0.4	0.7	0.3	63%	0.4	0.8	0.4	97%
C. Kunisch-Wolff	0.6	0.8	0.2	38%	0.5	0.8	0.4	80%
T. Ortmanns	0.4	1.3	0.8	194%	0.6	1.6	1.0	180%
C. Winkelmann	0.7	1.6	0.9	129%	0.5	1.4	0.9	182%
Total	3.6	7.1	3.5	96%	3.2	7.7	4.5	137%

- The total defined benefit scheme alone cost shareholders €82 million in 2019 and €61 million in 2020 (service cost + net interest cost + revaluation) and that over the last 5 years has accumulated to €219 million
- Two additional factors stand out at Aareal's pension offering to its Management Board members:
 - (1) Annual claim represents 15% x (total fixed salary + full target bonus) – even if such bonus target is not fully achieved
 - (2) Guaranteed 4% yield per year on such contributions
- Following discussions with pension experts / actuaries, we believe a savings potential of at least €3-5 million per year exists for Aareal Bank's⁽¹⁾ German operations
- In addition, a significant capital gain of €30-50 million could be achieved by hiving off selected parts of the pension obligations to dedicated service providers

(1) Aareal Group excluding Aareon AG.
Source: Aareal annual report

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