PETRUSADVISERS

Marija Korsch (Chairwoman of the Supervisory Board, Chairwoman of the Remuneration Control Committee)
Aareal Bank AG („**Aareal**“)
Paulinenstraße 15
65189 Wiesbaden
Cc: Christof von Dryander (Deputy Chairman of the Remuneration Control Committee), Klaus Novatius (Deputy Chairman of the Supervisory Board, member of the Remuneration Control Committee), Richard Peters (Deputy Chairman of the Supervisory Board, member of the Remuneration Control Committee), Marc Oliver Heß (Interim CEO, CFO)

London, 24 November 2020

Dear Ms. Korsch,

Following up on our letter of 6 November, we would like to clarify that we sent our ‘urgent call for work’ only to you, Mr. Merkens and Mr. Heß. The rumors in the press are therefore based on points that Aareal must have leaked to the outside. In consequence, we saw no alternative but to go public with our letter.

It has been communicated to us that you have used the press rumours about our ‘urgent call for work’ as a pretext to impose the termination of any constructive exchange with Petrus Advisers. We are by no means surprised by your reaction. Throughout the past year, we have repeatedly been lectured that in your opinion everything at Aareal is in great shape. The reality is that your contribution to Aareal and particularly the strategy of the bank has been consistently negative. When we discussed our letter with you, your only reaction was that Aareal had Euro 350-370 million in freely distributable cash which would be paid to shareholders as soon as the ECB gives the go-ahead[1]. This very logic of yours proves that you do not sufficiently appreciate the gravity of the situation. The work on Aareal Bank’s[2] RoE we have shared with you shows clearly that while a reduction of capital can be helpful to boost RoE, it will by no means be sufficient to close the performance gap towards achieving a sustainable level of 8-10% post-tax ROE.

The work of the supervisory board in respect to the existing strategy Aareal Next Level has equally been unsatisfactory: As a result of lengthy discussions, we had to initiate a review of a strategy that had been announced as recently as January 2020. The leadership at Aareal had apparently hoped that a partial sale of Aareon would solve all problems because the capital markets would learn to appreciate the enormous value of the software subsidiary. Consequently, Aareal took very expensive private-equity-capital on board in order to compensate for management shortcomings at Aareon and to develop its potential. Following many discussions, we agreed that a partial sale made sense as the Aareon business was simply too poorly managed to be a stand-alone entity in the capital markets (via an IPO or spin-off to Aareal shareholders).

The anticipated share price fireworks did not materialise. Aareal Bank does not earn its cost of capital and the capital markets do not trust its leadership. Prior to our public letter, the market even put a negative value on Aareal Bank. You as the Chairwoman have time and again denied this problem and have instead repeatedly tried to block off our arguments as well as our offer of support. Instead of involving renowned industry experts to help develop a sustainable future for Aareal Bank, your preference is to spend a lot of money on consultants – McKinsey and Bain have the mandate to sort it out for the bank and Aareon, respectively.

Particularly, when it comes to costs, Aareal – under your leadership – has consistently blocked any proper efficiency initiatives. Yet, the facts are overwhelming and simply unethical: despite ever faster plummeting results you have stuffed your evidently oversized management board of six with ever more money. For 2019, the management board was paid Euro 19 million[3] representing some 13% of Aareal’s net income of that very year! The 2019 compensation was 4-5 times higher than pbb’s and the gap is even wider in comparison to other German and Austrian banks.

[1] *Conference call of 10 November 2020 at 11.30 cet.*

[2] *Aareal Bank defined as Aareon Bank AG excluding Aareon AG.*

[3] *Paid compensation including ancillary benefits and pension benefits.*

Adding a share price decline by 44% since 2015[4] makes this carte blanche you have given to freely plunder the bank a serious case of governance misconduct. The supervisory board costs Euro 1.5 million per year and thus twice as much as for example pbb's. Since 2015, supervisory board and management board have cost us a total of nearly Euro 80 million – c. 7% of current market capitalization[5]!

Independent of the outcome of the strategic review, we therefore demand a clear signal by Aareal:

(1) 0% Bonus for 2020: in response to our question, Aareal has confirmed that provisions for 2020 bonus allocations assuming 100% target achievement have been made. Your share price has declined by 37% this year[6] and no dividend has been paid out. We demand the logical and complete forgoing of any bonus this year.

(2) Catch-up: any change of the 0% bonus regime can only happen if and when the sustainably achieved post-tax RoE of Aareal Bank is 8-10% (not considering the release of any Covid-19 related provisions).

(3) Claw-back: very high provisions made for 2020 point to excessive risk taking at Aareal Bank. We demand an independent review of the risk-taking behaviour of the management board. The fact that no dividend was paid for 2019 has to be taken into consideration. We furthermore demand a claw-back of bonuses paid out in the past should this review deliver negative results.

(4) Size of the Management Board: in light of the limited size and complexity of Aareal, a management board with 3-4 members seems appropriate and should be implemented.

(5) Cost of the Supervisory Board: we demand a significant reduction of the current cost (c. Euro 1.5 million per year plus the cost for your assistant, your office and the support of the work of the supervisory board by at least one senior Aareal manager). A reduction of the number of supervisory board seats seems logical.

Countless times have you tried to tell us that for legal and regulatory reasons there was limited room to change existing compensation structures. We are very happy to volunteer our help to find solutions with regulators as long as they enable less excessive compensation levels.

Moreover, you have publicly declared that for you there was no alternative to Hermann Merkens as CEO. We are very sorry that Mr. Merkens has fallen sick and hope he will get well soon. So far, there has not been any information for shareholders regarding the nature of his sickness. However, it has been clearly communicated to us that he is currently not in a position to fulfill his professional duties as per §84 AktG. We are worried that a long-term sick leave would certainly further increase the leadership vacuum at Aareal. We therefore demand that the supervisory board meet its duty of care and immediately consider succession alternatives for Mr. Merkens.

Ms. Korsch, we have had to conclude that under your leadership at Aareal real progress is not possible and that constructive recommendations have been blocked off. Instead, your focus has been to ensure excessive banker pay to maintain peace at home – untenable conditions, which have no place at a bank with a modern approach. We expect a clear statement by Aareal with respect to 2020 bonus payments by 26 November at the latest and reserve our rights to take further steps. In case you are not able to deliver this, we urge you to step aside and make space for fresh talent bringing a dynamic and sustainable approach to ethically acceptable leadership of a bank.

Sincerely,

Klaus Umek
Managing Partner

Till Hufnagel
Partner

[4] *Per 19 November 2020.*

[5] *Based on a market capitalization of Euro 1.134 million per 19 November 2020, per Factset.*

[6] *Bloomberg per 19 November 2020.*

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