BayernLB
2017
Annual Report and Accounts

Separate Financial Statements

BayernLB

BayernLB's financial statements at a glance

Income statement (HGB)

EUR million	1 Jan–31 Dec 2017	1 Jan–31 Dec 2016	Change in %
Net interest income	728	1,014	–28.2
Net commission income	176	195	–9.3
Net income of the trading portfolio	116	98	18.4
Administrative expenses	–899	–873	3.0
Operating profit/loss	**405**	**417**	**–2.8**

Balance sheet (HGB)

EUR million	31 Dec 2017	31 Dec 2016	Change in %
Total assets	138,350	137,585	0.6
Business volume	170,667	168,870	1.1
Credit volume	112,392	104,880	7.2
Total deposits	78,094	75,321	3.7
Securitised liabilities	36,720	34,737	5.7
Reported own funds	10,361	12,855	–19.4

Banking supervisory capital and ratios under CRR/CRD IV (after close of year)

EUR million	31 Dec 2017	31 Dec 2016	Change in %
Common Equity Tier 1 capital (CET1 capital)	8,373	9,009	–7.1
Own funds	9,861	10,639	–7.3
Total RWA	38,873	42,157	–7.8
CET1 ratio	21.5%	21.4%	+0.1 pp[1]
CET1 ratio (fully loaded)	21.5%	18.9%	+2.6 pp[1]
Total capital ratio	25.4%	25.2%	+0.2 pp[1]

1 *Percentage points.*

Employees

	31 Dec 2017	31 Dec 2016	Change in %
Number of employees	3,216	3,196	0.6

Contents

Report by the Supervisory Board

Ladies and gentlemen,

Over the past financial year, we advised the Board of Management on the administration of the company and continually monitored its management activities.

In 2017, BayernLB's Board of Management kept the Supervisory Board and its committees informed of key developments at the Bank and within the Group at regular intervals, both promptly and comprehensively, in writing and orally. This included its supervisory duty to disclose deficiencies detected by the internal Audit division.

We held detailed discussions with the Board of Management on BayernLB's business policy and fundamental issues relating to corporate planning, especially in its financial, investment and personnel aspects. We were also briefed on business performance, focusing especially on the Group's earnings, expenses, risks, liquidity and capital status, profitability, legal and business relations, material events and business transactions.

Between meetings, as Chairman of the Supervisory Board, I remained in regular and close contact with BayernLB's Board of Management, particularly its Chairman. The Supervisory Board was also notified in writing of important matters and, where necessary, resolutions were passed.

The Supervisory Board was involved in key decisions affecting BayernLB and gave its approval where necessary.

As in previous years, meetings were once again held in financial year 2017 between the Joint Supervisory Team from the ECB and national supervisory authorities on the one hand and the Chairman of the Supervisory Board and the chairpersons of the Audit Committee and Risk Committee on the other to discuss the main issues pertaining to the respective body. These focused on strategic and regulatory matters and on BayernLB's risk situation and committee affairs.

For the banking sector as a whole, the past financial year was once again dominated by persistently low interest rates, ever tighter regulatory requirements and stiff competition. This was counterbalanced by continued very good economic performance and unusually low risk provisioning requirements. Against this backdrop, BayernLB brought the state-aid proceedings, which were initiated in 2009, to a successful early close in summer 2017. In response to the ending of restrictions on business policy, the Bank's committees agreed to a number of measures in September 2017, which included modestly expanding the foreign business.

Supervisory Board meetings

In the reporting year the Supervisory Board held a total of nine meetings which were also attended by representatives of legal supervisory authorities and, in some cases, of banking supervisory authorities.

Besides the detailed reports of the committee chairpersons on the activities of the various boards and committees, the scheduled Supervisory Board meetings dealt with the regular reports of the Board of Management on the status of BayernLB's financial position and performance and on regulatory and supervisory issues, especially the results of the on-site audits by the supervisory authorities. In connection with this, we continued to take a detailed look at IT-related issues, in particular the progress of the project set up to update and improve IT infrastructure. The Board of Management also provided us with regular updates on current business policy issues and the current status of the talks with the European Commission and the ECB within the state-aid proceedings. We subjected the Board of Management's reports to the Supervisory Board to critical scrutiny and requested additional information in some cases, which was always immediately provided in full.

In addition, the Supervisory Board spent the past financial year dealing with various "Offshore" issues related to the disposal a few years ago of the private banking business of its former Luxembourg subsidiary bank. In connection with this, the Bank's committees also approved an offshore policy.

Over several meetings, after prior consultation in the relevant committees, we discussed Board of Management and Supervisory Board affairs, including the assessment of the Board of Management and Supervisory Board, which must be conducted in accordance with statutory requirements, and matters relating to remuneration policy. In relation to the latter we also considered the revised Remuneration Ordinance for Institutions, which came into effect in August 2017. We also set the targets for the Board of Management for 2017 and agreed the feedback to the members of the Board of Management for the past financial year.

Additionally in 2017, we regularly discussed BayernLB's capital situation, especially with regards to the conditions under the EU state aid proceedings. Another regular item on the agenda was our DKB subsidiary, specifically its current financial position, performance and risk situation.

In January 2017, the Board of Management gave us its preliminary indications for the 2016 annual financial statements. The Supervisory Board also focused on the auditor reforms and next steps in relation to this matter. Besides various regulatory issues, we were also updated on the current status of the efficiency programme and a strategic project within the Savings Banks & Association division.

In our March meeting, we discussed in detail the business performance in 2016. We also looked at the internal Audit division's annual report and the annual audit plan for 2017. The Supervisory Board and the Board of Management also discussed the progress of the project portfolio.

In April 2017, the focus was on the Board of Management's Report for financial year 2016, the adoption of the annual financial statements and the approval of the consolidated financial statements. The resolution was based on the recommendations of the Audit Committee and a subsequent detailed discussion with the auditors Deloitte GmbH Wirtschaftsprüfungsgesellschaft. In accordance with a proposal by the Audit Committee, the Supervisory Board also recommended to the General Meeting that the auditing firm Deloitte GmbH be reappointed to audit the 2017 annual financial statements of BayernLB and the Group, which the General Meeting agreed to. Another key focus of the meeting was the current status of the EU state-aid proceedings and the related application for the full repayment of the silent partner contributions of the Free State of Bavaria, which we approved. We also looked at the updating of key planning parameters and their impact on the medium-term planning for 2017 – 2021. The Supervisory Board also noted both the human resources report and status report on variable remuneration for employees in financial year 2016.

The focus of our meeting in July 2017 was the ending of the EU state-aid proceedings. In this connection, we and the Board of Management discussed for the first time the launch and expansion of business activities. The Board of Management also kept us abreast of the results of the ECB's thematic review in connection with a major regulatory project. We also noted the remuneration officer's remuneration monitoring report and the investments report.

In our closed meeting in September we stepped up the strategic discussions with the Board of Management about enhancing the business model after the end of the EU state-aid proceedings and approved a modest expansion of the foreign business. We were also informed by the Board of Management about the current status of the efficiency programme.

In our regular September meeting, we devoted greater attention to issues related to DKB's retail customer business, particularly in light of current developments in digitalisation and innovation. Besides status reports on business policy matters, the Supervisory Board addressed the issue of future non-financial reporting under the German Corporate Social Responsibility-Directive Implementation Act. In addition, the Supervisory Board agreed to recommend to the General Meeting the appointment of the audit firm PricewaterhouseCoopers GmbH Wirtschaftsprüfungsgesellschaft as the new auditor for financial year 2019. This follows the recommendation of the Audit Committee, which dealt with the change of auditor in financial year 2017.

The main item on the agenda of the December meeting was the Group's medium-term planning for 2018 – 2022, which we discussed in detail with the Board of Management and then approved. Furthermore, as part of the strategy dialogue, the Supervisory Board took a look at the Business Strategy and related sub-strategies. We and the Board of Management also discussed the ECB's decision to create supervisory requirements (SREP decision) and were briefed on the current performance of our sales offices and certain regulatory requirements.

Supervisory Board committees – an overview

In a total of six meetings, the **Risk Committee** dealt with all major issues relating to the risk strategy agreed by the Board of Management and all aspects of BayernLB's risk situation at both Group and Bank level. It discussed the Group-wide risk strategies, which must be updated at least once a year, and approved individual loans requiring authorisation. It also examined reports by the Board of Management on sub-portfolio strategies, risk trends and especially risk-bearing capacity. The Risk Committee also checked whether the terms and conditions in the customer business were in line with the Bank's business model and risk structure.

The Risk Committee and the Board of Management also regularly discussed geopolitical and macroeconomic risks in connection with regulatory issues. Special topics included the impact of Brexit, the effects of a rise in interest rates and the future of the car industry.

The **Compensation Committee** carried out its legally mandated duties in a total of five meetings. It discussed in particular the Board of Management's reports on the structure of the remuneration systems for employees (focusing partly on their relationship to the Business and Risk Strategy), monitored their suitability and received regular updates on specific issues. It evaluated the impact of the remuneration systems on the Bank's and Group's risk, capital and liquidity situation and discussed the size and distribution of a total bonus pool. The Compensation Committee also discussed with the Remuneration Officer her report on the suitability of the remuneration systems for BayernLB staff. It additionally devoted much of its attention to enhancing the remuneration systems for employees and for members of the Board of Management, taking into account new regulatory requirements. Under its original area of responsibility, the Compensation Committee also provided advice on matters related to Board of Management remuneration and prepared decisions by the Supervisory Board.

The Compensation Committee and Risk Committee worked closely together and regularly exchanged information.

The **Executive and Nominating Committee** met five times in the reporting period. The discussions particularly centred on preparations for Supervisory Board meetings and business and corporate policy considerations. The Committee also prepared decisions on Board of Management matters for the plenary session. Furthermore, the Executive and Nominating Committee carried out an assessment of the Board of Management and the Supervisory Board in accordance with the German Banking Act.

In a total of seven sessions, the **Audit Committee** dealt with the monitoring of the accounting process and the effectiveness of the risk management system, particularly the internal control system and the internal Audit division. The Committee also oversaw the implementation of the audit of the annual financial statements and of the consolidated financial statements, particularly with regard to the independence of the auditors and the services they provided, including any necessary approvals of non-audit services supplied by the auditors. Another issue the Committee looked at in detail was the Board of Management's reports on BayernLB's current financial position and performance and on the status of large (regulatory) projects (including for IFRS 9). In 2017, the internal Audit division and Group Compliance reported to the Audit Committee on their work and audit findings and other matters. The Committee deliberated on the money-laundering and financial crime threat analysis and conferred with the auditors Deloitte on what the audit of the 2017 annual financial statements should focus on. Other key points on the agenda of the Audit Committee in 2017 included in particular the impact of the auditor reforms and the related matter of the choice of a new auditor for financial year 2019, as well as the progress of the project set up for improving IT.

In its two meetings, in accordance with its legal duties, the **BayernLabo Committee** dealt with all matters in respect of BayernLabo on behalf of the Supervisory Board and passed resolutions concerning BayernLabo's affairs for which the Supervisory Board is responsible. It also discussed the business and risk strategy, refinancing and HR planning with both the Board of Management and BayernLabo Management. The Committee was updated by the Board of Management and BayernLabo Management on business performance and it approved BayernLabo's own contribution to its internally funded programmes.

The Supervisory Board and respective committees carried out the tasks assigned to them by law, the Statutes and current Rules of Procedure.

Additional specialist training

The Supervisory Board attended two information events given by specialists from the Bank, external experts and representatives of the external auditors on current developments, with the focus on BayernLB. Besides macroeconomic aspects, they delved into selected areas of supervisory law and regulatory requirements, especially developments in banking regulation and various IT and digitalisation-related issues.

Corporate governance

The BayernLB Corporate Governance Principles set out the regulations on corporate management and corporate supervision that apply to BayernLB on the basis of binding and in-house regulations. The Supervisory Board discussed compliance with these Corporate Governance Principles in 2017 in its meeting on 21 March 2018. The Board of Management, Supervisory Board and General Meeting agreed that they were aware of no evidence that these principles had not been observed in financial year 2017.

Changes to the Supervisory Board

Prof. Dr Christian Rödl stepped down from the Supervisory Board on 30 April 2017 and was succeeded in the post by Stephan Winkelmeier on 1 May 2017.

Audit and approval of the 2017 annual accounts

Deloitte GmbH Wirtschaftsprüfungsgesellschaft conducted the audit of the annual financial statements and consolidated financial statements of the Bank, the management report and the Group management report and the annual financial statements and management report of BayernLabo, a legally dependent institution of the Bank. Deloitte issued an unqualified opinion. The Supervisory Board and BayernLB's BayernLabo Committee each verified the independence of the auditors of the financial statements in advance.

The financial statements documentation and audit reports were duly presented to all Supervisory Board members. The BayernLabo Committee and the Audit Committee discussed each of the documents forming part of the annual and consolidated financial statements in conjunction with the auditors' audit report and in detail with the auditors themselves. Each committee chair reported to the Supervisory Board on this matter.

In its meeting of 11 April 2018, the BayernLabo Committee adopted BayernLabo's submitted annual financial statements and approved the management report to BayernLabo's accounts.

In its meeting today, on the recommendation of the Audit Committee, and after examining the auditors' reports and the annual and consolidated financial statements documentation and discussing these in detail with the auditors, the Supervisory Board approved the findings of the audit and concluded that it had no reservations even after the final outcome of the audits.

In its meeting today, the Supervisory Board adopted the Bank's annual financial statements submitted by the Board of Management and approved the management report; it also approved the consolidated financial statements and Group management report.

Furthermore, the Supervisory Board proposed to the General Meeting that the Board of Management be discharged and that the reported net retained profits of EUR 50 million be distributed to the providers of capital. The General Meeting gave its approval to both proposals in its meeting today.

A thank you to the customers, the Board of Management and the staff

The Supervisory Board would like to thank all of BayernLB's customers and business partners for their loyalty over this past financial year. It also wishes to thank the members of the Board of Management and all of BayernLB's staff for all their hard work over the past year, and for their huge personal contribution.

Munich, 12 April 2018

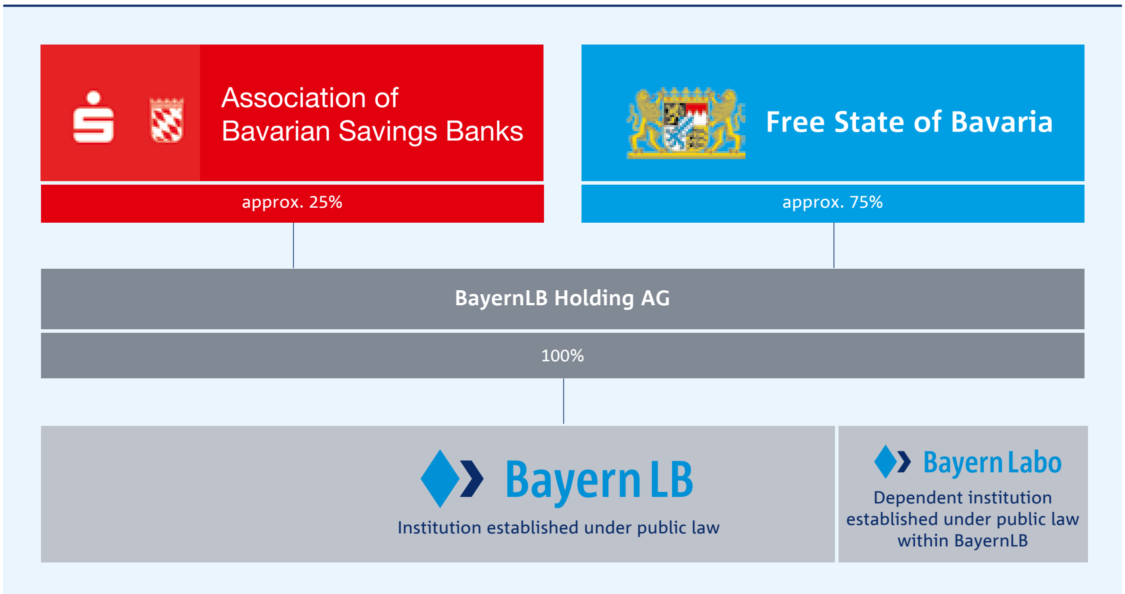
On behalf of the Supervisory Board

Gerd Haeusler
CEO

Management report of BayernLB

Overview of BayernLB

Business model and strategy



Bayerische Landesbank, Munich (BayernLB or Bank) is an institution with legal capacity established under public law with its registered office in Munich and a nominal capital of EUR 2,800,000,000. The nominal capital is due to BayernLB Holding AG, Munich as the entity that has direct ownership. The Free State of Bavaria and the Association of Bavarian Savings Banks are indirect owners through their respective stakes in BayernLB Holding AG. Bayerische Landesbodenkreditanstalt, Munich (BayernLabo) fulfils the public mandate by carrying out the state-subsidised loan business.

The rating agencies Moody's Investors Service (Moody's) and Fitch Ratings (Fitch) have assigned the following ratings to BayernLB:

	Moody's	Fitch
Long-term (unsecured)	A1	A–
Short-term (unsecured)	P-1	F1
Public Pfandbriefs	Aaa	AAA
Mortgage Pfandbriefs	Aaa	–
Financial strength/viability rating	baa3	bbb

As a commercial bank, Landesbank and central bank to the savings banks, BayernLB is a strong corporate and real estate lender focused geographically on Bavaria and Germany as well as a reliable partner to the Bavarian savings banks.

BayernLB's strategic business model is based on the following operating business segments:

- **Corporates & Mittelstand**
- **Real Estate & Savings Banks/Association** including the legally dependent institution Bayerische Landesbodenkreditanstalt, Munich (BayernLabo) and the subsidiary Real I.S. AG Gesellschaft für Immobilien Assetmanagement, Munich (Real I.S.)

- **DKB** with the core business activities of the Deutsche Kreditbank Aktiengesellschaft, Berlin (DKB) sub-group and Bayern Card-Services GmbH – S-Finanzgruppe, Munich (BCS)
- **Financial Markets**, including the subsidiary BayernInvest Kapitalverwaltungsgesellschaft mbH, Munich (BayernInvest)

Corporates & Mittelstand

The Corporates & Mittelstand business area handles business with large German and selected international companies and the Mittelstand corporate customer business in Germany, Austria and Switzerland. These large customers are mostly DAX, MDAX and family-owned companies with annual sales of at least EUR 1 billion. The focus in Mittelstand is on companies with annual sales of over EUR 50 million.

BayernLB's core competencies include traditional and structured credit financing, comprising working capital, capex and trade financing, project and export financing, lease financing and transportation finance (including rolling stock). Since the early completion of the EU proceedings, the transportation finance product range has also been complemented by asset-based aircraft financing. In addition, BayernLB helps its customers tap capital markets for their financing needs, for example through traditional bonds, German Schuldschein note loans and interest rate and currency hedging. BayernLB also has a strong market position in the state-subsidised loan business.

Real Estate & Savings Banks/Association

BayernLB's real estate business focuses on long-term commercial real estate financing and services. The regional focus here is on Germany, although it also supports customers' activities abroad to diversify the portfolio and risks. In the commercial real estate area, products include financing for existing real estate assets, project development, housing developers and real estate portfolios. In the managed real estate area, the focus is mainly on financing concepts for hotels, logistics centres, hospitals, clinics and care homes and syndicated financing with savings banks. To serve customers more comprehensively under one roof, the Bank makes extensive use of its working relationship with subsidiaries and affiliates, such as Real I.S. AG, Bayerische Landesbank Immobilien-Beteiligungs-Gesellschaft mbH & Co. KG, Munich (BayernImmo), LB Immobilienbewertungsgesellschaft mbH, Munich (LB ImmoWert) and Bayern Facility Management GmbH, Munich (BayernFM).

The Bavarian savings banks and BayernLB are linked together in a preferred partnership. For the Bank, the savings banks are both important customers and sales partners and thus they form one of the key pillars of its business model. BayernLB acts as a central service provider for the savings banks and supplies them with tailored products and services in its Association business. The focus of the relationship is on supplying the savings banks with a range of complementary products and services for both their own business and their customers, including payment services, capital market business, international business, syndicated and subsidised loans, as well as foreign notes and coins/precious metal activities. The savings banks outside Bavaria also have access to selected product segments. Liquidity management is particularly important for these customers. Funding from the savings banks is an important source of refinancing for BayernLB and for strengthening the common liquidity pool. BayernLB also acts as a lender and service provider to the public sector and institutional investors. The focus here is on intensifying sales in Germany and on expanding market share in the core market of Bavaria in close partnership with the Bavarian savings banks. It provides a wide range of customised financing and investment solutions to state governments, local authorities and public institutions. BayernLB also stands out in this segment thanks to its expertise in public-private partnership projects and the renewable energy sector. BayernLabo fulfils the public mandate by carrying out the state-subsidised loan business for BayernLB.

Financial Markets

Financial Markets offers a range of money market, forex and capital market services, funding and treasury strategies, and a broad portfolio of structured investment products. Main customers include the savings banks, banks, German and international large and Mittelstand customers, real estate customers and institutional customers, which are served in the respective business areas. Securities asset management for BayernLB is handled by the Group subsidiary BayernInvest. This investment company focuses mainly on advisory services and managing securities investment funds for institutional and private investors.

DKB

DKB, an integral part of the BayernLB Group, complements the business model. It operates in the retail segment as an online direct bank with a steadily growing customer base, and in the infrastructure and corporate customers segment as a specialist. Its expertise extends especially to financing and investment products in the environmental technology, residential, municipal, social infrastructure, health services, education & research, energy, utilities and other segments.

Implementation of the business model

BayernLB continued to rigorously implement its business model in 2017 by pursuing a clear strategy of being a customer-focused bank. The Bank’s strategic framework is formed by the current strategic goals and target structure they are based on. In this regard, BayernLB’s focus is on strengthening its sustainable operating business areas, while winding down portfolios with elevated risk.

In business with corporate customers, the positive earnings trend in the Mittelstand has been maintained since the previous year.

In the commercial and residential real estate businesses, the Bank virtually achieved its growth target for new business of around EUR 5 billion. In the retail customer area, DKB grew its customer base to about 3.7 million in 2017.

BayernLB is the exclusive service provider for the Bavarian savings banks in the field of subsidised loans. BayernLB also plays a leading role across the German market in the foreign notes and coins/precious metal business.

The transformation of BayernLB's capital markets business continued in 2017. The main emphases here were on making further investments in the customer support processes to improve customer penetration and to increase earnings from customers, while continuing to steadily update and digitalise the system landscape required for the capital market business.

With the signing of the agreement for BayernLB to repay EUR 1.0 billion to the Free State of Bavaria, the EU state-aid proceedings were brought to a close in June 2017 as the Bank had complied with all major EU conditions and commitments about two and a half years ahead of the deadline. As part of the state-aid proceedings, BayernLB repaid around EUR 5.0 billion in state aid ahead of schedule.

Now that the EU state-aid proceedings have come to a close, BayernLB is pursuing a moderate growth trajectory and focusing in particular on increasing its earnings. This includes leveraging additional business potential which should gradually improve the Bank's profitability over the next few years. With a view to offsetting the higher costs in the upcoming years, further efficiency measures were identified in the business model and implemented. BayernLB maintained its favourable position relative to its peers in terms of cost structure. The long-term optimisation of the business model and transition into an agile organisation will provide a sound basis for expanding market share in the core business areas and leveraging new sources of earnings in the medium to long term.

The still challenging market environment had an impact on BayernLB's operating business in 2017. Accordingly, the main challenges it faced in securing its earnings base were the persistently low interest rates and stiff competition from established market participants and increasingly from new market entrants such as fintechs. Meanwhile, rising regulatory requirements affecting, for example, capital requirements (in terms of quantity and quality), liquidity requirements, risk management, and IT infrastructure increasingly put pressure on the fixed cost base.

In the annual strategic process, the BayernLB Group drew up and then fleshed out strategic directions and goals and specific measures for all its segments, based on the interplay between current strengths and weaknesses and future market opportunities and risks. To ensure long-term competitiveness, the Bank is targeting moderate growth in the opportunities-rich core business, increasing stability, efficiency and flexibility, and taking a very customer-focused approach. The Bank's main aim here is to increase and intensify business with existing customers while gaining new customers in the defined core segments. The Bank will work towards achieving this by making sure that products and services meet customer needs and by taking measures to step up sales and further improve customer-focused sales structures, and also by increasingly digitalising the entire value chain. This, coupled with a solid capital base and the good, long-standing customer relationships that the Bank enjoys, will lay the foundations for the successful growth of BayernLB.

Internal management system

BayernLB is included in the BayernLB Group's management process. The BayernLB Group's management system is based on managing the inter-related variables of profitability, risk, liquidity and capital. One of the main goals of the internal management system is to continuously optimise the resources employed while simultaneously ensuring the Group's capital and liquidity base is adequate.

The profitability of the BayernLB Group is managed using two key financial ratios that act as crucial indicators of performance: return on equity and cost efficiency. Return on equity (RoE) is calculated by dividing profit before taxes by shareholders' equity as calculated according to regulatory requirements. At Group level, the average Common Equity Tier 1/CET1 capital available over the financial year has been used since the start of financial year 2016. For all management levels below this, the average economic capital employed in the financial year is derived from the risk-weightings of the underlying individual transactions (RWAs) specified by regulatory authorities. Cost efficiency is monitored by means of the cost/income ratio (CIR), the ratio of administrative expenses to gross earnings[1]. In addition to measuring return on equity and cost efficiency, BayernLB also uses other ratios. These include measures of the profitability and expense of risk-weighted assets (RWAs) employed, and also economic value added (EVA). This expresses the profit of a company before deduction of the income tax components, taking account of the cost of the capital employed denominated in euro. In order to ensure integrated and consistent management, the key figures RoE and CIR are used at all levels of management. The management cycle is a continuous process of carrying out annual medium-term planning, producing intrayear detailed target vs actual comparisons and making regular projections to the year-end.

Risk-bearing capacity is monitored using the Internal Capital Adequacy Assessment Process (ICAAP). This process is used in the BayernLB Group, BayernLB and DKB. The aim of ICAAP is to ensure that there is sufficient economic capital at all times for the assumed or planned risks. For risk management, BayernLB follows a liquidation-based approach in ICAAP that is designed to protect senior creditors. The method for calculating risk-bearing capacity is assessed and refined on a regular basis to ensure it takes adequate account of external factors and internal strategic targets. The economic capital is of suitable quality to absorb any losses and is calculated, based on the liquidation approach, by deducting from the sum of equity and subordinated capital those items that are not available in the event of liquidation (e.g. intangible assets). To produce an in-depth, forward-looking analysis of economic capital adequacy, risk-bearing capacity is calculated based on the Business Strategy and supplemented by stress tests.

The strategic principles for dealing with liquidity risk within the BayernLB Group are set out in the Group Risk Strategy. The overriding priority of liquidity risk management and monitoring is to ensure that the BayernLB Group can meet its payment obligations and obtain funding at all times. In addition to stringently ensuring solvency, the primary goal of BayernLB's liquidity management is to ensure adequate access to markets. In the BayernLB Group, daily limits are placed on liquidity risks at the operating unit level based on defined scenarios.

1 Gross earnings = net interest income + net commission income + gains or losses on fair value measurement + gains or losses on hedge accounting + gains or losses on financial investments + other income and expenses.

Amongst other things, operating liquidity management is based on capital flow accounts and limit utilisation ratios. Additional information can be found in the Risk Report.

Capital is managed using the CET1 ratio and the total capital ratio in accordance with the fully loaded Capital Requirements Regulation and Directive (CRR/CRD IV) and the guidelines from the ECB's Supervisory Review and Evaluation Process (SREP). The capital required and the corresponding capital ratios are derived from the Business and Risk Strategies and the latest medium-term planning. RWAs are allocated to monitor and ensure compliance at all times with the capital ratios planned and required by the regulator as a basic condition for all business activities. As part of overall bank management, target capital amounts, risk-bearing capacity and funding are combined.

Human resources

2017 was a year in which BayernLB implemented its targeted new strategy. Human Resources was focused on helping the business areas and the central areas achieve their strategic and economic goals. The highlights were successfully concluding the HR-related changes in the cost-cutting programme while simultaneously supporting the business areas and central areas to implement organisational measures and expand and train employees in response to the stepping up of sales activities and the increasingly complex regulatory working environment.

As at 31 December 2017, 3,216 people were employed at BayernLB, of which 3,040 were based in Germany (FY 2016: 3,010 people) and 176 were based abroad (FY 2016: 186 people). The increase in headcount in 2017 was mainly due to the fact that, in parallel with reductions in the workforce at BayernLB, new employees with specific qualifications were recruited to work in the sales units and manage additional regulatory requirements.

Since financial year 2017 BayernLB has produced a report on equality and equal pay (equal pay report) pursuant to section 21 of the German Equal Pay Transparency Act (EntgTranspG). The equal pay report is attached to this management report as an appendix. The equal pay report for 2017 will be submitted to the operator of the Federal Gazette along with BayernLB's annual financial statements and the management report for financial year 2017 and published in the Federal Gazette. BayernLB's annual financial statements can also be viewed online at www.bayernlb.com.

Corporate responsibility

One of BayernLB's stated corporate goals is to achieve commercial success while meeting its social responsibilities. BayernLB therefore attaches great importance to its work in the community, the fields of education and science and the world of art and culture. It equally goes without saying that sustainability management and reporting play no less important roles in BayernLB's business activities.

Specialised, independent sustainability rating agencies regularly rate the targets and measures of the Bank's sustainability management on behalf of investors and give it very high scores compared with its peers for its commitment to dealing with the social and environmental challenges facing the public banking sector.

The BayernLB Group has held the oekom prime status distinction from rating agency oekom research since 2001 and thereby demonstrated its continual commitment to sustainable development. BayernLabo also continues to hold the prime rating.

Key changes in the participations portfolio

In the reporting year, BayernLB sold shareholdings in Fondations Capital I S.C.A., Senningerberg, Luxembourg and BayernLB Capital Partner GmbH, Munich.

Report on the economic position

Macroeconomic and sector-specific environment

Germany's economy continued to post strong growth in 2017, thereby exceeding the Bank's forecasts. Economic output was up 2.2 percent on the year before[2]. This growth was broad based, as it was fed both by public and private consumption and capital spending on buildings and equipment. The jump in capex in particular came as a surprise in light of the plethora of political risks which had raised uncertainty for companies on repeated occasions over the course of the year. The outcome of the elections in the Netherlands and France, which was positive for Europe, lightened corporate sentiment and willingness to spend. This was bolstered by easy financing conditions, driven by the European Central Bank's (ECB) expansive monetary policy. Exports also drove growth in 2017 as they rose more than imports. The global economic environment brightened as the year progressed, while the uptick in global demand boosted the economy in Germany. In the economically favourable environment, unemployment fell further over 2017, closing the period at 5.5 percent on a seasonally adjusted basis[3]. The high volume of refugees accepted into the country and coming onto the labour market in increasing numbers was, however, more than offset by an even higher pace of job creation, with some sectors already reporting shortages of qualified workers.

Inflation in Germany averaged 1.8 percent over the course of 2017. This was noticeably higher than in the previous year and BayernLB's expected figure of 1.6 percent, but it did fall short once again of the ECB's target of "below, but close to 2 percent"[4]. The ECB stuck to its generally very loose monetary policy in 2017. The interest rate spread (between the deposit facility rate and marginal lending facility rate) remained between –0.4 percent and 0.25 percent. However, the ECB took the decision in December 2016 to reduce the volume of securities it was purchasing every month. From April 2017, it cut monthly purchases from EUR 80 billion to just EUR 60 billion. Then in October 2017 it agreed to scale down the purchase volume to EUR 30 billion monthly from the start of 2018 and so take one further small step towards monetary normalisation[5]. But against this background, bank lending to companies and households in Germany hardly picked up over the year and in October was 1.4 percent higher than a year earlier. Overall demand for lending can still be characterised as subdued[6].

Contrary to BayernLB's predictions, in 2017 the euro appreciated by 14 percent to USD 1.20/EUR, breaching the sideways corridor it had been in since 2015 of about USD 1.05 – 1.15/EUR. A factor in this, besides Emmanuel Macron's electoral victory in France and the unexpectedly good state of the economy in Europe, was ECB president Mario Draghi's speech at the ECB conference in Sintra in Portugal in June, where he held out the prospect of a less heavily expansionary monetary policy. The euro also got some uplift from the general depreciation in the US dollar that began in 2017. As the Bank had predicted, the Brexit process and a cooling UK economy caused

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2 See Statistisches Bundesamt 2018, press release no. 011

3 Agentur für Arbeit, monthly report December 2017; https://statistik.arbeitsagentur.de/Statistikdaten/Detail/201712/arbeitsmarktberichte/monatsbericht-monatsbericht/monatsbericht-d-0-201712-pdf.pdf (German only)

4 See Statistisches Bundesamt 2017, press release no. 478

5 ECB press release of 26 October 2017; https://www.ecb.europa.eu/press/pr/date/2016/html/pr161208.en.html

6 See Deutsche Bundesbank 2017: "Banking Statistics – December 2017, Statistical Supplement I to the Monthly Report", Table I 6a; https://www.bundesbank.de/Redaktion/DE/Downloads/Veroeffentlichungen/Statistische_Beihefte_1/2017/2017_12_bankenstatistik.pdf?__blob=publicationFile the pound sterling to weaken further against the euro. However, this softening was less pronounced than forecast mainly because BayernLB had not expected the Bank of England to hike rates in November 2017. Also unexpected was the faltering of the Swiss franc against the euro during 2017. This was due to the boost to the euro from the buoyant state of the eurozone economy and sunnier political sentiment in Europe (resulting in lower demand for the "safe haven" franc). The Swiss National Bank is also keeping to its negative interest rate policy, despite the weaker franc.

At the start of 2017, yields on 10-year German government bonds were at 0.2 percent[7]. Growth and higher inflation expectations in particular led Bunds to advance into 0.5 percent territory twice in the first quarter[8]. The uncertainty that arose in the run-up to the French presidential election and the impact from the US did, however, result in setbacks. In mid April – shortly before the first round of the election in France – 10-year Bunds were yielding around 0.15 percent[9], their low point for the year. The positive election results and especially ECB president Draghi's speech in Sintra at the end of June drove up yields significantly. By mid July, the yield had topped out for 2017 at just over 0.6 percent[10]. After that, disappointing inflation figures in the US caused yields to steadily fall until September. There was no new pick-up from September to December, and with the result that 10-year Bund yields hovered mainly between 0.3 and 0.5 percent[11]. If one considers that inflation in 2017 was overestimated by markets and analysts and global demand for Treasuries remained high, it is hardly surprising that the position of 10-year US Treasuries at the end of the year was virtually unchanged on their position at the start of it[12]. As growth was also stronger, yields on 2-year bonds rose steeply, meaning that the Treasury curve was significantly flattened[13].

Risk premiums on Pfandbrief and covered bond markets fell across all country segments over the past year. A spur came from the ECB's widescale covered bond purchases and the outcome of the elections in the Netherlands and France. At the end of the year average risk premiums on covered bonds reached new highs; here too the volume of new issues remained lower than average. Bonds from Italy and Portugal also benefited from ratings upgrades.

7 *See Deutsche Bundesbank 2018: Daily yield of the current 10 year federal bond, time series BBK01.WT1010; https://www.bundesbank.de/Navigation/DE/Statistiken/Zeitreihen_Datenbanken/Makrooekonomische_Zeitreihen/its_details_value_node.html?tsId=BBK01.WT1010&dateSelect=2017*

8 *See Deutsche Bundesbank 2018: Daily yield of the current 10 year federal bond, time series BBK01.WT1010; https://www.bundesbank.de/Navigation/DE/Statistiken/Zeitreihen_Datenbanken/Makrooekonomische_Zeitreihen/its_details_value_node.html?tsId=BBK01.WT1010&dateSelect=2017*

9 *See Deutsche Bundesbank 2018: Daily yield of the current 10 year federal bond, time series BBK01.WT1010; https://www.bundesbank.de/Navigation/DE/Statistiken/Zeitreihen_Datenbanken/Makrooekonomische_Zeitreihen/its_details_value_node.html?tsId=BBK01.WT1010&dateSelect=2017*

10 *See Deutsche Bundesbank 2018: Daily yield of the current 10 year federal bond, time series BBK01.WT1010; https://www.bundesbank.de/Navigation/DE/Statistiken/Zeitreihen_Datenbanken/Makrooekonomische_Zeitreihen/its_details_value_node.html?tsId=BBK01.WT1010&dateSelect=2017*

11 *See Deutsche Bundesbank 2018: Daily yield of the current 10 year federal bond, time series BBK01.WT1010; https://www.bundesbank.de/Navigation/DE/Statistiken/Zeitreihen_Datenbanken/Makrooekonomische_Zeitreihen/its_details_value_node.html?tsId=BBK01.WT1010&dateSelect=2017*

12 *See U.S. Department of the Treasury 2018: Daily Treasury Yield Curve Rates; https://www.treasury.gov/resource-center/data-chart-center/interest-rates/Pages/TextView.aspx?data=yieldYear&year=2017*

13 *See U.S. Department of the Treasury 2018: Daily Treasury Yield Curve Rates; https://www.treasury.gov/resource-center/data-chart-center/interest-rates/Pages/TextView.aspx?data=yieldYear&year=2017*

On European credit markets, risk premiums on investment-grade bonds, as tracked by iBoxx Euro Corporates, tightened by around 25 basis points in 2017. Besides there being constant demand from central banks, private investors were also increasingly on the hunt for (positive) yields. This fillip, however, was not only observed on the secondary market. Primary markets posted a new record in 2017 with new issues of EUR 361 billion[14], significantly outperforming the previous record year of 2016 (EUR 321 billion).

The German stock market benefited in 2017 from an unexpectedly strong global economy, rising corporate earnings and ultra-loose monetary policy. German and European equities were reined in, however, by the appreciation of the euro against the dollar. The German stock exchange (DAX) rose 12.5 percent (including dividends) to 12,918, the biggest annual growth since 2013[15], making it the sixth year of growth in a row. In 2017 the EURO STOXX 50 (price index) trailed the DAX's performance somewhat, with a 6.5 percent rise to 3,504[16]. But, if dividends are included, it grew by +10.0 percent[17].

Course of business

The BayernLB Group is managed on the basis of IFRS indicators. As a key part of the Group, BayernLB is also managed using these metrics.

BayernLB's business performance in 2017 was marked by moderate economic growth of 2.2 percent in Germany and a market environment which remained tough for lenders. Earnings came under more pressure due to persistently low interest rates, which were even negative in some cases.

Under these challenging conditions, the Bank achieved an operating profit of EUR 405 million (FY 2016: EUR 417 million). Thanks to this, BayernLB was able to fully service the profit participation certificates in the amount of EUR 23 million and silent partner contributions in the amount of EUR 53 million. From the net profit for the year of EUR 363 million (FY 2016: EUR 332 million), the amount of EUR 313 million was paid into retained earnings, resulting in net retained profits for financial year 2017 of EUR 50 million.

As at 31 December 2017, total assets amounted to EUR 138.4 billion, about EUR 1.0 billion higher than the year before. BayernLB's financial position was once more largely driven by the credit business, where the focus of lending was on the operating business segments, especially the savings banks as association partners, in line with the customer-focus of BayernLB's business model on Germany. Amounts due from customers stood at EUR 67.3 billion (FY 2016: EUR 68.8 billion). Amounts due from banks came in at EUR 35.0 billion (FY 2016: EUR 26.2 billion), of which EUR 15.1 billion (FY 2016: EUR 14.1 billion) related to affiliated savings banks.

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14 See Bloomberg: aggregation of all issued EUR bonds of non-financial companies with a minimum size of EUR 100 million, published via Bloomberg.

15 See Deutsche Börse: DAX 30 performance, taken from Thomson Reuters Datastream 15 February 2018

16 See STOXX: EURO STOXX 50, taken from Thomson Reuters Datastream 15 February 2018

17 See STOXX: EURO STOXX 50, taken from Thomson Reuters Datastream 15 February 2018

The market environment for the refinancing business in the eurozone was positive overall throughout financial year 2017. BayernLB had unrestricted access to money and capital markets during the reporting period. The Bank obtained funding from institutional and private investors without any difficulty and at a cost-effective rate throughout the year. The Bank again had a comfortable supply of liquidity in 2017 and was solvent at all times.

After repaying state aid to the Free State of Bavaria in the amount of EUR 1.0 billion, BayernLB improved its solid capital base (CET 1 ratio fully loaded) from 18.9 percent to 21.5 percent due to the reinvestment of profits and another fall in risk assets. Common Equity Tier 1 capital (CET1) amounted to EUR 8.4 billion as at 31 December 2017 (FY 2016: EUR 9.0 billion).

Results of operations

EUR million	1 Jan – 31 Dec 2017	1 Jan – 31 Dec 2016	Change in %
Net interest income	728	1,014	–28.2
Net commission income	176	195	–9.3
Gross profit	**904**	**1,209**	**–25.2**
Personnel expenses	–500	–491	1.9
Operating expenses	–399	–382	4.5
Administrative expenses	**–899**	**–873**	**3.0**
Net income of the trading portfolio	116	98	18.4
Net of other operating expenses, income and other taxes	–12	180	–
Risk provisions	–27	–364	–92.6
Gains or losses on measurement	322	167	93.4
Operating profit/loss (operating earnings)	**405**	**417**	**–2.8**
Gains or losses from extraordinary items	–6	6	–
Income taxes	–37	–90	–59.4
Net income/loss for the financial year	**363**	**332**	**9.1**
Withdrawals from capital reserve	0	0	–
Allocations to retained earnings	–313	–332	–5.9
Replenishment of profit participation certificates	0	0	–
Replenishment of silent partner contributions	0	0	–
Net retained profits	50	0	–

Rounding differences may occur in the tables.

There was a significant drop in net interest income of EUR 286 million to EUR 728 million (FY 2016: EUR 1,014 million). This was almost exclusively due to the fall of EUR 259 million in income from profit transfer agreements. The main reason was the strategic decision to reinvest DKB's net profit for 2017 to strengthen its capital base. Net interest income from credit and money market transactions and securities after allowing for interest expenses declined slightly by EUR 21 million.

Net commission income fell by about 9 percent to EUR 176 million (FY 2016: EUR 195 million). Commission income fell by EUR 20 million to EUR 229 million (FY 2016: EUR 249 million), while commission expenses were slightly below the previous year at EUR 53 million (FY 2016: EUR 54 million). On the earnings side, there was a drop of EUR 19 million in income from the credit and securities business.

Administrative expenses were virtually stable, rising by only a modest 3 percent or EUR 26 million to EUR 899 million (FY 2016: EUR 873 million). Of this rise, EUR 9 million was attributable to staff costs and EUR 17 million to operating expenses, with the latter line item pushed up by rising IT costs (EUR +24 million) and legal and advisory costs (EUR +16 million). The scale of the expenditure shows that BayernLB is continuously investing in updating and improving its IT structure and improving its business processes, primarily to meet the growth in regulatory requirements. Expenses for the bank levy and deposit guarantee scheme comprised a total charge to administrative expenses of EUR 64 million (FY 2016: EUR 60 million).

All realised and unrealised contributions to earnings from trading are shown in the net income of the trading portfolio item. Net income from the trading portfolio improved by 18.4 percent to EUR 116 million in financial year 2017 (FY 2016: EUR 98 million). This trend was driven by gains on currency-related transactions of EUR 56 million (FY 2016: EUR 20 million) and measurement effects from counterparty-specific default risks in the derivatives business of EUR 55 million (FY 2016: EUR 48 million). Due to the increase in net profit from the trading portfolio, EUR 13 million (FY 2016: EUR 11 million) was allocated to the fund for general bank risks pursuant to section 340e para. 4 HGB.

After netting other operating expenses, income and other taxes, the Bank posted other operating income of EUR –12 million (FY 2016: other operating income of EUR +180 million). The previous year's net item was boosted mainly by the first-time application of the new rules for discounting provisions for pensions and similar obligations in accordance with section 253 para. 2 HGB. BayernLB realised a gain of EUR 133 million on this.

The cost/income ratio (CIR)[18] rose to 82.8 percent (FY 2016: 54.6 percent) as a result of the reinvestment of DKB's earnings, following the significant drop in net interest income and other operating income (FY 2016: 54.6 percent).

Risk provisions, comprising risk provisions in the credit business and gains or losses on securities in the liquidity reserve stood at EUR –27 million, a significant drop on the previous year's figure (FY 2016: EUR –364 million) which mainly comprised a large allocation to the contingency reserves pursuant to section 340f HGB. As a result, expenses for provisions for risks in the credit business plunged from EUR –367 million to EUR –65 million. At the same time, the earnings contribution from securities in the liquidity reserve improved from EUR 6 million to EUR 38 million. In financial year 2017, an allocation of EUR 47 million was made to the fund for general bank risks under section 340g HGB (FY 2016: allocation of EUR 42 million).

18 CIR = (administrative expenses + expenses for the bank levy and deposit guarantee scheme + amortisation, depreciation and writedowns on intangible assets and tangible assets)/(gross profit + net income/losses from the trading portfolio + net of other operating expenses, income and other taxes).

Gains or losses on measurement of fixed asset securities increased by EUR 155 million to EUR 322 million (FY 2016: EUR 167 million). The change in earnings was mainly due to the repurchase of all securities held or issued by BayernLB Capital Trust I and BayernLB Capital LLC I, both in Wilmington, Delaware, in the US, which contributed EUR 314 million to earnings.

Due in part to the factors described above, the Bank reported an operating profit of EUR 405 million in the reporting year (FY 2016: EUR 417 million). Thanks to this, BayernLB was able to fully service the profit participation certificates in the amount of EUR 23 million and silent partner contributions in the amount of EUR 53 million.

BayernLB's net profit for the year resulted in a return on equity (RoE)[19] of 4.8 percent for financial year 2017 (FY 2015: 4.8 percent).

Gains or losses from extraordinary items came in at EUR –6 million and were EUR 12 million lower than the previous year's figure (FY 2016: EUR 6 million). Both extraordinary income of EUR 2 million (FY 2016: EUR 15 million) and extraordinary expenses of EUR 8 million (FY 2016: EUR 10 million) were related to the restructuring measures under the KSP cost-cutting programme. The changes arose in the year under review from measurement effects.

Income taxes amounted to a negative EUR 37 million (FY 2016: EUR –90 million). This item includes tax refunds and releases of tax provisions.

The Bank posted a net profit of EUR 363 million (FY 2016: EUR 332 million). Part of this amount (EUR 313 million) was booked to the retained earnings, leaving net retained profits of EUR 50 million, which will be distributed to the providers of capital.

Financial position

Both total assets and business volume were higher in financial year 2017:

EUR billion	31 Dec 2017	31 Dec 2016	Change in %
Total assets	138.4	137.6	0.6
Business volume*	170.7	168.9	1.1

** Total assets plus contingent liabilities and loan commitments.*

The business volume, which includes both total assets and off-balance-sheet transactions, rose by EUR 1.8 billion to EUR 170.7 billion. Total assets rose by EUR 0.8 billion to EUR 138.4 billion, largely due to the increase in the due from banks line item. The increase in business volume was due to the increase in contingent liabilities and credit commitments of 3.2 percent to EUR 32.3 billion (FY 2016: EUR 31.3 billion). The main reason for the increase in contingent liabilities to EUR 10.1 billion (FY 2016: EUR 9.9 billion) was higher liabilities from guarantees and indemnity agreements. The increase in other liabilities was due solely to the increase in irrevocable loan commitments.

19 RoE = the ratio of gains or losses on ordinary activities to the average of regulatory capital available over the financial year (CET1). The comparison figure for the previous year was adjusted.

Assets

EUR billion	31 Dec 2017	31 Dec 2016	Change in %
Credit volume*	112.4	104.9	7.2
Due from banks	35.0	26.2	33.7
Due from customers	67.3	68.8	−2.1
Securities	16.6	20.7	−19.7
Trading portfolio	7.1	11.1	−36.1
Participations/shares in affiliated companies	2.5	2.5	0.2

** Due from banks and customers plus contingent liabilities from guarantees and indemnity agreements*

Amounts due from banks increased by EUR 8.8 billion to EUR 35.0 billion (FY 2016: EUR 26.2 billion). This was due to a significant rise in overnight lending to domestic banks of EUR 9.6 billion.

Amounts due from customers dropped by EUR 1.5 billion to EUR 67.3 billion (FY 2016: EUR 68.8 billion). Amounts due from domestic customers rose slightly to EUR 46.1 billion (FY 2016: EUR 45.9 billion). However, amounts due from foreign borrowers contracted markedly to EUR 21.2 billion (FY 2016: EUR 22.9 billion).

The securities portfolio shrank to EUR 16.6 billion (FY 2016: EUR 20.7 billion). The volume of bonds and other fixed-income securities dropped by EUR 4.1 billion to EUR 16.5 billion. The main cause of the fall was the reduction in the holdings of bonds and fixed-income securities in the investment portfolio due to sales (EUR –3.4 billion).

The volume of the trading portfolio (assets held for trading) sank to EUR 7.1 billion (FY 2016: EUR 11.1 billion). The item largely comprises bonds and other fixed-income securities in the amount of EUR 1.5 billion (FY 2016: EUR 2.5 billion) and positive market values of derivatives in the amount of EUR 3.5 billion (FY 2016: EUR 6.5 billion).

There were no major changes in the participations portfolio and shares in affiliated companies in the financial year. The increase in the holding of shares in affiliated companies was primarily the result of value-based changes.

Liabilities

The main items on the liabilities side are as follows:

EUR billion	31 Dec 2017	31 Dec 2016	Change in %
Due to banks	41.2	43.3	−4.9
Due to customers	36.9	32.0	15.3
Securitised liabilities	36.7	34.7	5.7
Trading portfolio	3.5	4.9	−28.6
Equity	7.6	8.2	−7.7

Amounts due to banks fell by EUR 2.1 billion to EUR 41.2 billion (FY 2016: EUR 43.3 billion), mainly in short and medium-dated maturities. However, amounts due to customers increased by EUR 4.9 billion to EUR 36.9 billion (FY 2016: EUR 32.0 billion).

Securitised liabilities rose overall, by around EUR 2.0 billion to EUR 36.7 billion (FY 2016: EUR 34.7 billion). The portfolio grew by EUR 3.2 billion to EUR 6.7 billion due a programme for issuing short-term money market instruments, whereas the portfolio of issued bonds shrank by EUR 1.2 billion to EUR 30.0 billion. This mostly related to the portfolio of mortgage Pfandbriefs, which reduced from EUR 2.5 billion to EUR 1.5 billion, due to maturing instruments.

The volume of the trading portfolio (liabilities held for trading) sank by EUR 1.4 billion to EUR 3.5 billion (FY 2016: EUR 4.9 billion). A significant component was derivatives with negative market values, which fell year on year from EUR 4.3 billion to EUR 2.9 billion. This trend was in line with trading assets.

BayernLB's reported equity (after payment into retained earnings) totalled EUR 7.6 billion as at 31 December 2017, a decrease on the previous year's EUR 8.2 billion. The fall was primarily due to the repayment of the silent partner contributions to the Free State of Bavaria in the amount of EUR 1.0 billion, which took place in June 2017.

Banking supervisory capital and ratios under CRR/CRD IV and KWG

Capital for banking supervisory purposes is calculated in accordance with CRR/CRD IV.

Common Equity Tier 1 capital (CET1) amounted to EUR 8.0 billion as at 31 December 2017 (FY 2016: EUR 8.6 billion). The decline was largely the result of repaying a silent partner contribution of EUR 1.0 billion to the Free State of Bavaria in June 2017. The CET1 ratio was a solid 20.6 percent (31 December 2016: 20.4 percent). Total own funds as at 31 December 2017 amounted to EUR 9.5 billion (31 December 2016: EUR 10.2 billion) and the total capital ratio came to 24.4 percent (31 December 2016: 24.3 percent).

The following figures are based on the report to supervisory authorities as at 31 December 2017:

EUR billion	31 Dec 2017	31 Dec 2016
Total RWAs	38.9	42.2
Own funds	9.5	10.2
• Tier 1 capital	8.0	8.6
• Common Equity Tier 1 capital (CET1 capital)	8.0	8.6
Total capital ratio	24.4%	24.3%
Tier 1 capital ratio	20.6%	20.4%
CET1 ratio	20.6%	20.4%

Based on the adopted annual financial statements as at 31 December 2017, the Bank had CET1 capital of EUR 8.4 billion and a CET1 ratio of 24.5 percent (fully loaded: 21.5 percent). Based on own funds of EUR 9.9 billion, the total capital ratio was 25.4 percent. As at 31 December 2017, the return on capital employed as defined in section 26a para. 1 sentence 4 of the German Banking Act (KWG) was 0.3 percent (FY 2016: 0.2 percent).

General overview of financial performance

BayernLB's results of operations in financial year 2017 were solid taking into account the still challenging economic environment.

On the whole, a look at the earnings performance in 2017 shows that the Bank is well on track in terms of growth and its business model has proven effective even in the difficult market environment.

Moreover, risks were reduced further and appropriate measures taken for the future in the reporting year. Proper account has been taken of the risks.

BayernLB's net assets and financial position were stable in financial year 2017. The Bank's liquidity was good throughout the reporting period. Further information on refinancing and the liquidity situation is provided in the risk report.

For information on events of major significance after the close of the financial year, please refer to the notes to the annual financial statements.

Report on expected developments and on opportunities and risks

Report on expected developments including opportunities and risks

Economic environment

Growth momentum is likely to remain high in 2018, even if the (in some cases) very high quarterly growth rates from 2017 will probably not be matched entirely. For Germany BayernLB is therefore forecasting a slight slowdown in growth on the previous year to 2.1 percent. The country's economy will continue to benefit from the strong economic picture around the world. The approved programme of tax reforms in the US will play a role, as it should temporarily bulk up the economy there and probably crank up demand in Germany too. There is, however, still a great degree of uncertainty surrounding the Brexit process, which is likely to cause some of the euphoria on the part of companies in Europe to evaporate over the whole of 2018. All in all, Germany's upturn will remain on track, driven by strong domestic demand and external economic activity. Consumption will, once again, play a leading role, even if the increase in consumer spending power will in all likelihood be tempered slightly by a small increase in inflation. In addition, public spending will probably increase again in 2018. High tax receipts and the currently low interest burden on public-sector budgets suggest that this can again be achieved while maintaining a budgetary surplus. But investment should also nudge up gross domestic product because the need to expand is gaining traction where production capacity is fully utilised and the steady influx into metropolitan areas is resulting in higher spending on construction. Real estate prices should climb further in this environment, especially in conurbations with high migration rates.

With capacity utilised and wages growing slightly more strongly, inflation should move towards the ECB's target of less than but close to 2 percent. BayernLB expects it to average 1.9 percent over the course of the year. The ECB should thus continue to slowly exit from its expansive monetary policy. However, the interest rate spread should remain unchanged in 2018, while securities purchases will probably be extended until the end of the year, but at an even smaller volume from October. The biggest economic risks to Germany are (global) inflation rising by a much greater extent than expected and therefore accompanied by a marked tightening of monetary policy (above all in the US economy where capacity is more fully utilised). This could lead to markets overreacting, putting the brakes on global growth momentum. Despite there being many unresolved political problems in Europe (from Brexit right through to the creation of a sustainable architecture for the currency union), BayernLB is not expecting a new crisis in 2018 in its baseline scenario. It cannot, however, rule out fresh uncertainty triggered by specific events, such as the outcome of the new elections held in Italy. The protectionist measures recently initiated in the USA are unlikely to lead to any major countermeasures from its trading partners and it should therefore be possible to avert a serious trade war. There is, however, the risk in the short term of market turmoil from trade disputes.

Regarding exchange rates, BayernLB is expecting the US dollar to increase in value against the euro during 2018, to close the year at USD 1.13/EUR. The US Federal Reserve is likely to hike key rates by 25 basis points every quarter (i.e. much faster than markets expect) if the economy is doing well, there is full employment on the labour market and wage and inflationary pressure builds up. However, if core inflation rises only slowly, the ECB will probably not end its securities purchases for good until the end of the year, initially disappointing market expectations that an interest rate pivot is fast approaching. In the case of the pound sterling, BayernLB is expecting the currency to depreciate to GBP 0.95/EUR in 2018. The Bank believes it should become increasingly apparent when the negotiations on the future EU-UK relationship open, that the UK will only have very restricted access to the EU Single Market after the transition period, on par with the existing free trade agreement with Canada. BayernLB also expects the UK economy to cool further over the course of the year, snuffing out market expectations of another rate hike by the Bank of England. The Bank believes that the Swiss franc will tread water at its now weaker level in 2018. There is no prospect of a sustained appreciation in the franc so long as the Swiss National Bank clings to its negative interest rate policy and there is no major rise in risk aversion on the markets.

In the eurozone, the biggest risk to the bond markets in the first quarter is the tapering of security purchases by the ECB. That is because, aside from the significant reduction in net purchases to EUR 30 billion by the ECB, there will also be little reinvestment during this period, whereas high volumes are likely to be issued simultaneously at the beginning of the year. In the first quarter, persistently low inflation will, however, probably limit yield rises to 0.6 percent due to a drop in demand. The pace of growth should quicken slightly thereafter, given the higher deficit in the US that the expected tax reforms will generate, the Fed's shrinking of its balance sheet, expectations that the ECB will become less expansionary, and most importantly that inflation will rise from the second quarter. By year-end the Bank is expecting 10-year Bunds to be yielding around 1.0 percent.

In respect of the covered bond market, the Bank is anticipating spreads widening moderately in the market as a whole due to the withdrawal of ECB purchases. Covered bonds from the euro periphery will probably underperform their EU core counterparts.

Even if the ECB bond purchase programme is likely to remain a significant factor in 2018, the impact of support purchases will continue to fade over the course of the year. This means the fundamental trend for the corporate bond market should increasingly come under the spotlight. The combination of a constructive economic environment, solid earnings growth and still low rates of default can be viewed as positives, but they are unlikely in the medium term to hold spreads at the current cyclical low. Although BayernLB is forecasting moderate widening of 10 – 15 basis points in the investment grade segment (iBoxx Euro Non-Financials), this is likely to be exceeded in the high-yield bracket (BofA Merrill Lynch Euro High Yield), which should see a stretching out of around 60 basis points.

The upward trend on stock markets will probably continue in 2018, carried by the continuing strength of the world economy. Greater price volatility is, however, expected. Stock markets in 2018 will be boosted in particular by further increases in corporate earnings. The exchange rate trend of a moderate depreciation of the euro against the dollar that has been forecast by the Bank should fuel European equities further, in contrast to 2017. However, with the potential for positive surprises about economic growth not being so strong, the tailwind from monetary policy ebbing and capital market interest rates rising, share prices will probably enjoy slower growth globally compared with 2017. Potential triggers for rising volatility and temporary price corrections are the increase in fears about stronger monetary tightening by central banks, uncertainty surrounding global economic growth and (geo) political conflicts.

BayernLB's future performance

The successful implementation of the Business Strategy requires the capital base to be solid and the core business to remain stable. In 2017, as one of the key cornerstones of BayernLB's future strategic direction, the Bank defined an overarching strategic course and drew up the specific measures for achieving it. The focus of the strategic goals will be on prudent internationalisation to achieve a sustained increase in returns and regional diversification of risks, selective digitalisation of sales channels, targeted volume growth within the existing risk guidelines to increase the ability to cover fixed-costs, and strengthening of sources of earnings not dependent on interest. BayernLB's market presence will continue to be shaped by its universal bank-like business model with a geographical focus on Bavaria and Germany.

In 2018 the strategic direction set in the previous years will continue to be pursued and the potential opened up by the premature ending of the EU proceedings will also be used. Key factors in the Bank's success here will be expanding the Mittelstand business to the neighbouring regions of Austria and Switzerland, selectively extending the customer portfolio in the large international companies segment and expanding transportation finance to include asset-based aircraft financing. In doing so, BayernLB will be able to build on a strong customer and product portfolio. The intensively competitive interest rate environment, irritations posed by protectionist developments, political uncertainties and, in particular, potentially stronger inflation growth in the US with concomitant significant increases in interest rates harbour risks and will create a tough decision-making and investment environment for international companies, project developers, sponsors and investors.

With regard to commercial and residential real estate customers, the focus and core aspects of the strategic goals will be to boost sales activities and increase market penetration by offering comprehensive customer relationship management across the whole product range. In addition, the foreign portfolio share will also be increased by 25 percent to around 35 percent (especially via the Paris, London and Milan branches, with the US business re-established via the New York office) to achieve better portfolio and risk diversification. BayernLB expects to achieve steady portfolio growth between now and 2022 by implementing the planned increases in business with existing customers in Germany and abroad, and expanding the customer base, for example by opening new sales offices. BayernLB believes portfolio quality will remain good and stable for financial institutions in developed markets, while ongoing (geo)political tensions and macroeconomic risks could lead to a deterioration in the previously good portfolio quality in certain emerging markets. The quality of the Countries/Public-Sector/Non-Profit Organisations sub-portfolio should continue to be very good and stable. The Corporates sub-portfolio should also remain stable overall in 2018. Furthermore, BayernLB believes the portfolio quality of the real estate business will stay stable as well.

Given the strategic focus of the business areas and the London branch on international companies, it is predicted that any negative impact of Brexit on the Bank's target customers will be moderate and bearable and that business activities with these clients could be continued. BayernLB's Business and Risk strategies are regularly assessed in relation to Brexit; no notable adjustments have yet been made. From a current perspective, there is no negative impact on earnings forecasts and the Bank is assuming that planned business can be realised as soon as there is adequate political and economic certainty.

The successful, trust-based collaboration with savings banks and municipalities is based on the sales and customer-orientated support model, with a holistic approach and range of needs-based products and services.

DKB's strategic focus is on ensuring stable and profitable customer relationship management by achieving a good balance in its lending and deposit business. In the retail customers business, online bank DKB will aim for more customer growth and higher wallet share through a comprehensive range of products and services. In the corporate and infrastructure customer segments it operates with a broad-based network and sector-specific expertise for the defined core customer groups.

The Bank assumes that interest rates will remain low. Institutional investors will therefore continue to turn to longer-dated instruments and credit risk (senior unsecured and subordinated capital) to generate returns. For BayernLB's part, this interest rate environment calls for more focus to be placed on managing funding costs. Thanks to the expected presence of central banks as both bond buyers and suppliers of liquidity (e.g. ECB – TLTRO II), the Bank is forecasting a plentiful supply of market liquidity in 2018. BayernLB will, however, continue to work on its funding portfolio so it can call on a comfortable funding base even when central bank activity starts to ebb.

Increasing importance will be attached to managing loss absorption capacity, which is determined by the supervisory minimum requirement for own funds and eligible liabilities (MREL) and, as an additional aspect, has a significant impact on BayernLB's capital market rating.

BayernLB sees opportunities, especially if the economic data turns out better than expected. A rapid increase in interest rates in particular would help net interest income. On the other hand, further falls in interest rates would weigh on the Bank as, for example, it would need to inject more funds into pension provisions. Furthermore, the greater strategic freedom of action offered by the premature ending of the EU state aid proceedings offers the chance to realise additional earnings potential. Earnings and cost-cutting potential could also be generated by targeted efficiency and digitalisation measures.

For 2018 the Bank is expecting profit before taxes to be significantly lower than in the previous year. In a still difficult market environment with increasing regulation, persistently low interest rates and tough competition, BayernLB will be investing further in forward-looking projects to, for example, upgrade its IT architecture, while at the same time boosting efficiency and cutting costs. It cannot be ruled out that any change in the assumptions underlying our forecasts may affect BayernLB and its net assets, financial position and results of operations.

Risk report

Principles

This risk report is prepared in accordance with the requirements of the German Commercial Code (Handelsgesetzbuch (HGB)) on risk reporting. The following information relates to the provision in section 289 para. 4 HGB, which requires corporations within the meaning of section 264d HGB in conjunction with section 340a HGB to describe the key features of the internal monitoring and risk management system they use for the accounting process.

Key developments in 2017

- Risk profile remains stable
- Core business expanded in line with strategy
- Risk-bearing capacity maintained at all times
- Liquidity position continues to be healthy

The risk profile at BayernLB remained stable in financial year 2017.

Gross credit volume rose by EUR 3.2 billion to EUR 171.8 billion.

The Bank's high portfolio quality improved again and benefited from new business with good quality assets and the positive financial and economic environment in Germany, BayernLB's core market.

Thanks to strict risk discipline, the key metrics of portfolio quality remained stable, with a high investment grade share of 87.1 percent (FY 2016: 85.8 percent) and a further fall in the non-performing loan ratio to 1.8 percent (FY 2016: 1.9 percent). In the core business, the non-performing loan ratio was 0.3 percent (FY 2016: 0.3 percent).

Risk-bearing capacity was maintained throughout financial year 2017 as the provision of risk capital was solid. In addition, BayernLB had a good supply of liquidity on hand.

Internal control and risk management system

Tasks and objectives

BayernLB has established an internal control system (ICS) to ensure that its accounts are properly prepared and reliable. This includes principles, procedures and measures for ensuring the accounts are produced in an efficient and cost-effective manner. Consequently, the internal control system helps to limit risks in the accounting process and plays a key role in providing a true and fair view of BayernLB's net assets, financial position and results of operations.

One key aim of the internal control system is to ensure that all transactions are fully and properly entered, processed and documented in accordance with legal requirements and standards, the Bank's statutes and other internal directives. This also ensures that risks are disclosed in line with supervisory requirements. The IT systems used by the central areas participating in the process are suitable for this purpose and the staff have been given adequate training in the legal and internal standards and in how to use the IT systems.

Management structure

The organisation of the committees and boards below the Board of Management reflects a new European regulatory structure led by the ECB, involving the Single Supervisory Mechanism (SSM) and Supervisory Review and Evaluation Process (SREP), and with the objective of making corporate management more consistent and transparent within the BayernLB Group.

Management structure

Supervisory Board and committees

The Supervisory Board monitors and advises BayernLB's Board of Management. It is assisted in its work by the committees described below:

The Audit Committee monitors the accounting process, the effectiveness of the risk management system, particularly the internal control system and internal audit division, and the correction of open findings from audits and the annual accounts.

The Risk Committee mainly deals with issues relating to the risk strategies approved by the Board of Management and the risk situation at BayernLB, and decides on loans requiring approval by the Supervisory Board under the German Banking Act and BayernLB's Competence Regulations.

In addition to the above-mentioned committees, the Supervisory Board is supported by the Executive and Nominating Committee, the Compensation Committee and the BayernLabo Committee.

Board of Management and committees (committees and boards)

In managing the business and the company the Board of Management is supported by committees and boards.

Each committee is headed by a member of the Board of Management. The Board of Management has transferred responsibilities and, to an extent, decision-making powers to the committees. The committees have a largely advisory function. The individual Board of Management member's responsibility for his/her segment and the overall responsibility of the Board of Management pursuant to the Rules of Procedure and the allocation of tasks of the Board of Management continue to apply.

The Performance & Capital Committee, chaired by the CFO, monitors the performance/earnings situation and (regulatory) capital base. It also prepares decisions on BayernLB's performance and capital management for the Board of Management.

The Risk Committee, chaired by the CRO, supports and advises the Board of Management in discussing changes in the Group risk profile that include BayernLB, assesses potential recovery situations, discusses the main quantitative procedures and methods for managing and monitoring all types of risk (apart from liquidity risk), reviews new regulatory requirements and initiates implementation in terms of Pillar 2.

The Liquidity Committee, chaired by the member of the Board of Management responsible for Financial Markets, is essentially concerned with ensuring the ongoing liquidity of BayernLB and advises and takes decisions within the parameters of the guidelines set out by the Board of Management.

In addition, the Board of Management is supported in its activities by the Management Committee.

Senior management

At senior management level the boards generally act across the segments, without any direct involvement by the Board of Management.

The RWA Board, chaired by the head of the Controlling division, monitors and manages changes in risk-weighted assets (RWAs) at BayernLB.

The Credit Risk Board, chaired by the head of the Risk Office Credit Analysis division, is the highest competence holder on credit matters below the Board of Management and deals with sector portfolio, country and product reports and policy issues regarding credit risk management for the core business.

The Product Board, chaired by the Group Risk Control division, is responsible for complying with MaRisk requirements for the launch of business activities in new products. It is mainly responsible for the approval of new products and regularly approving the valuation models used and changes to these models.

The Corporates & Mittelstand Investment Board and the Real Estate Investment Board are the highest decision-making bodies below the Board of Management with authority to allocate capital and resources for their business area and are responsible for the business area-specific management carried out on the basis of central rules and ratios and the strategic targets of the area.

Other boards set up by the Board of Management include the Remuneration Board, the Project and Investment Board, the CFO/COO Board, the Regulatory Board and the Ad Hoc Board.

Organisation

Besides segregating the functions of the Sales and Risk Office units and the Trading and Back Office units, a business organisation must have adequate internal control procedures and mechanisms to manage and monitor key risks.

The Board of Management is chiefly supported in this task by the Risk Office, Financial Office, and Operating Office central areas as well as the Corporate Center.

Risk Office

The Risk Office of BayernLB comprises the Group Risk Control, RO Credit Analysis, Mid Office, Group Compliance and Research divisions.

The Group Risk Control division independently identifies, values, analyses, communicates, documents and monitors all risk types at aggregated level. For the purposes of operational management of risk types and risk-bearing capacity, Group Risk Control provides the Board of Management and other committees of the Supervisory Board with independent and risk-relevant reports.

In addition to periodic and ad-hoc reporting on BayernLB's risk situation to internal decision-makers, communication also comprises external risk reports filed in accordance with legal and supervisory requirements.

Decisions regarding risk management are made in accordance with the Business Strategy and Risk Strategy, which are harmonised with each other. Credit risk management is a joint responsibility of the Sales units and Risk Office units, with segregation of duties being ensured at all times. In this management process, the RO Credit Analysis division is responsible for analysing, assessing and managing the risk-relevant exposures in the core business (the Risk Office role). It takes the lead in setting the Credit Risk Strategy for individual customers, sectors, countries and special products such as leasing, project finance and acquisition finance, is responsible for ongoing credit and transaction analysis and votes on behalf of the Risk Office in the credit approval process.

The Mid Office division pools the credit-related tasks and frees up the sales and credit analysis units to concentrate on their primary tasks and, with its standardised, lean processes, makes a key contribution to boosting customer business and achieving the planned business growth.

The Group Compliance division was allocated to the Risk Office central area in 2017. The division monitors and ensures compliance with legal and supervisory requirements. It also coordinates the compliance activities of the subsidiaries.

The Research division is responsible for risk assessment of countries and sectors, and issues economic analyses and forecasts, as well as capital market studies and recommendations (including on bonds and Schuldschein note loans from individual issuers). The division contributes to risk management at BayernLB and provides analyses and forecasts for BayernLB customers and for the securities and currency business of the Financial Markets business area and the Bavarian savings banks.

A new Functional Data Management department was set up in 2017, reporting directly to the Chief Risk Officer. This is mainly responsible for managing data quality and requirements, the data quality report and data governance. The head of the department acts as Chief Data Officer.

The Group Regulatory Office department reports directly to the Chief Risk Officer and acts as the central point of contact at the working level for BayernLB Group with banking supervisory authorities such as the ECB, BaFin and the Deutsche Bundesbank.

Credit Consulting

The Credit Consulting division looks after the restructuring and liquidation exposures. The division performs the roles of both the Sales units and the Risk Office for the exposures assigned to it.

Financial Office

Operational implementation of Group-wide accounting standards is the responsibility of the Financial Office central area, in particular the Finance division, which ensures that the accounts are properly prepared. It is also responsible for establishing the accounting process and making sure it is effective.

Its key tasks include preparing the separate financial statements, consolidated financial statements and the Group management report, establishing accounting policies, initiating accounting-related projects, and providing guidance on national and international developments in accounting.

The Financial Office central area also implements the relevant accounting standards and legal requirements on accounting, which are detailed in the directives for preparing the accounts. These directives, which are an important component of the accounting-related internal control system, are summarised and documented in the Accounting Manual, and in the instructions for Group companies for preparing the financial statements.

The separate financial statements and management report are compiled in accordance with the directives for preparing the accounts, produced by directive of the Board of Management, checked by the auditors and approved by the Supervisory Board. The Supervisory Board has set up an Audit Committee whose duties include discussing the audit reports and preparing the resolutions for the Supervisory Board's approval of the separate financial statements and management report. Upon request, the auditor takes part in the discussions of the Audit Committee and Supervisory Board on the separate and consolidated financial statements and reports on the key findings of its audit.

The Controlling division is also assigned to the Financial Office central area. This unit is responsible for supervisory reporting and the operational implementation of consistent rules across the Group as part of management controlling, and lays down standard methods and procedures.

Operating Office

The Operating Office central area is responsible for BayernLB's operating processes and supporting these in the Group IT, Operations & Services and Organisation divisions.

Corporate Center

The Audit division audits BayernLB's business operations and reports directly to the CEO. Taking a risk-oriented auditing approach, its auditing activities extend to all activities and processes within BayernLB. In particular, its activities also include important processes and activities outsourced to third parties. Pursuant to MaRisk BT 2.1 sub-section 3, the Company can forego its own auditing activities in cases of material outsourcing arrangements, insofar as the other internal audit activities performed – i.e. the external service provider's internal auditing – satisfy the MaRisk AT 4.4 and BT 2 provisions. Where companies performing material outsourced activities have no internal audit service of their own, BayernLB's internal Audit division undertakes its own auditing activities. The internal audit units of companies performing material outsourced activities are regularly reviewed to ensure they are capable of satisfactorily performing their duties. As Group internal auditor, it also supplements the internal auditing units of subordinate companies.

The CEO is directly in charge of the Legal & BoM Support, Group Strategy & Group Communications and Human Resources divisions.

Scope of monitoring and monitoring procedures

The internal control and risk management system is governed by the internal written organisational rules (schriftlich fixierte Ordnung (SFO)).

The rules governing the accounting-related internal control system are set out in the directives for preparing the accounts. The main component of these directives is the Accounting Manual (FACT manual), which contains key requirements for ensuring the uniform application of accounting policies and measurement methods. This is supplemented by instructions on preparing the separate financial statements. These instructions on preparing the annual accounts include information on reconciling and eliminating intra-Group transactions, the debt consolidation process, expenses and earnings consolidation, as well as on tasks, contacts and deadlines relating to the preparation of the separate financial statements. In addition, changes in accounting standards, IT systems and control procedures for ensuring high quality reporting and data are also explained.

Instructions on risk management are prepared within BayernLB on the basis of the Group Risk Guidelines. These rules govern the risk management and monitoring processes used for the timely identification, full documentation and appropriate disclosure of major risks.

As with the Accounting Manual (FACT manual) and instructions for preparing the annual accounts, these rules are regularly reviewed, updated and published internally.

To ensure transactions are fully and correctly processed, and that bookings, data entry and documentation are in compliance, a number of internal control procedures have been implemented within BayernLB. Measures include the segregation of duties, a differentiated access authorisation system to prevent unauthorised intruders, ongoing checks within the workflow process applying the dual-control principle, and checks programmed into the IT systems. The internal control system reconciles ledgers and sub-ledgers, monitors manual bookings in the main ledgers and conducts posting runs. Additional checks and reconciliations are also conducted to ensure data is correctly transferred between IT systems.

When preparing the separate financial statements, checks are carried out to determine if the underlying data is properly presented, and the quality of the data in the accounts is assessed (e.g. applying the dual control principle, conducting plausibility checks). BayernLB uses server-based consolidation software, in particular to take account of the branches and BayernLabo, for which separate editing and reading rights have been assigned. This software has a number of checks built into the program to ensure entries are properly made and correctly documented.

The accounting process is checked regularly for inherent risks, so that measures can be taken when necessary to refine the internal control system.

BayernLB has outsourced some of its services to external companies. This mainly relates to IT services, infrastructure services, rating services and securities processing.

Both central and decentralised units within BayernLB ensure that these outsourced services are subject to the internal control system:

The Central Outsourcing Management office in the Organisation division sets the rules for the outsourcing process in BayernLB and provides centralised status reports on outsourcing to the Board of Management. The ongoing monitoring and managing of external service providers as required by section 25b of the German Banking Act (KWG) and MaRisk AT 9 is performed decentrally by outsourcing managers in the business units responsible for accepting the services. Assessment of outsourcing risks forms part of the regular risk reporting to the Board of Management.

Risk-oriented management

Risk Strategy

Decisions regarding risk management are made in accordance with the Business Strategy and Risk Strategy, which are harmonised with each other.

The Risk Strategy, which is based on the Business Strategy and reviewed regularly, is set by the Board of Management and discussed with the Risk Committee of the Supervisory Board. The general objectives and guidelines of the Risk Strategy and the strategic requirements for the different types of risk are drawn up based on the Business Strategy.

The Risk Strategy sets the following main objectives and guidelines for 2017:

Objectives:
- Ensure on a sustainable basis that the amount and quality of capital is appropriate from both a regulatory and economic perspective
- Ensure BayernLB is solvent at all times
- Achieve sustainable earnings using value-based management of RWAs

Guidelines:
- BayernLB only takes on risks it is able to assess and manage
- In those areas where the strategy allows for portfolio growth, quality takes priority over quantity
- Sales and Risk units are jointly responsible for earnings after risk provisions
- BayernLB applies high ethical principles in its business activities.

The economic capital available for allocation is based on the long-term capital available, and was allocated within BayernLB by risk type in line with the Risk Strategy in force for 2017.

The basis for setting the Risk Strategy is the annual risk inventory carried out in accordance with MaRisk and the risk-bearing capacity calculation. The risk inventory examines not only BayernLB but also the participations and special purpose entities in BayernLB, regardless of whether they are consolidated under German commercial law or supervisory requirements. BayernLB's risk profile is then shown in the risk map within the risk inventory and presented to the Board of Management for information purposes. The major risks at BayernLB are credit risk, market risk, including risk from pension obligations, operational risk, participation risk, risk of a rise in the cost of liquidity, and business and strategic risk, including reputational risk. The individual risk types are described in greater detail further on in this report.

Capital management

Capital management is based on a planning process that incorporates strategic, risk-based and regulatory factors into a multi-year operational plan. The Business Strategy is an essential element for preparing the capital planning and the risk strategy.

Integrated risk and earnings reporting

Trends in the four key areas of performance, capital, liquidity and risk are integrated into a monthly Group management report presented to the Board of Management. As a component of the integrated reporting, the Group management report provides a brief impression of the current situation with key figures and ratios. Additional detailed information focused on the four key areas is then presented and commented on.

The instruments used to manage and monitor the achievement of Business and Risk Strategy goals are constantly refined.

The processes involved in managing regulatory capital adequacy and internal capital adequacy are described in the sections below.

Regulatory capital adequacy (solvency)

To ensure BayernLB has the proper amount of regulatory capital, the objectives, methods and processes below have been defined: the starting point for the allocation of regulatory capital is BayernLB's own funds planning. Own funds are defined as Common Equity Tier 1 capital (CET1), additional Tier 1 capital and Tier 2 capital. Common Equity Tier 1 capital comprises subscribed capital plus reserves and various supervisory adjustments and deductions. Tier 2 comprises profit participation certificates and long-term subordinated liabilities.

Own funds planning is based largely on the internal target Common Equity Tier 1 ratio (ratio of Common Equity Tier 1 capital to RWAs) and an internally set target total capital ratio (ratio of capital to RWAs) for the BayernLB Group. It establishes upper limits for credit, market and operational risks arising from business activities in the planning period.

Regulatory capital is distributed in the planning process to each planning unit through RWAs. The planning units (Group units) are the defined business areas/central areas within BayernLB, BayernLabo and DKB.

Risk-weighted assets (RWAs) are allocated to the Group units through a top-down distribution approved by the Board of Management for credit, market and operational risks, combined with an internally assumed capital ratio of 12.5 percent (FY 2016: 11.5 percent). Compliance with the RWA limits available to each Group unit is constantly monitored by the Performance & Capital Committee. The Board of Management receives monthly reports on current RWA utilisations.

Information on the changes in the BayernLB Group's supervisory ratios can be found in this management report under "Banking supervisory ratios under CRR/CRD IV for the BayernLB Group". BayernLB publishes additional information in the disclosure report in accordance with section 26a KWG. The disclosure report can be found on BayernLB's website under "Disclosure Report".

Economic capital adequacy (risk-bearing capacity)

As part of the Internal Capital Adequacy Assessment Process (ICAAP), the economic capital adequacy (risk-bearing capacity) is ensured and monitored so that sufficient economic capital is available at all times to cover the risks assumed or planned.

For risk management, BayernLB follows a liquidation-based approach in ICAAP that is designed to protect senior creditors. This is computed using internal targets for the accuracy of risk measurement, which correspond to a confidence level of 99.95 percent. The method for calculating risk-bearing capacity is assessed and refined on a regular basis to ensure it takes adequate account of external factors and internal strategic targets.

The economic capital is of suitable quality to absorb any losses and is calculated in accordance with the liquidation approach by deducting those items that are not available in the event of the liquidation of BayernLB (e.g. intangible assets) from the sum of equity and subordinated capital.

The Risk Strategy, in tandem with the Business Strategy, sets the risk appetite and the framework for risk planning. The Risk Strategy allows only a proportion of the available economic capital to be allocated to risk types in the course of business activities.

The planning of economic risks for the risk-bearing capacity calculation and the planning of the economic capital are integral parts of the planning process described under the "Regulatory capital adequacy" section. For an in-depth, forward-looking analysis of economic capital adequacy, the calculation of risk-bearing capacity is based on the Business Strategy and is supplemented by stress tests. Both scenario and sensitivity analyses are carried out for this purpose. In addition to historical scenarios, the impact of adverse changes in risk factors both on specific risk types and across all risk types is also analysed using hypothetical scenarios. The latter in particular have a major role in the analysis of situational scenarios.

The liquidation-based analysis of risk-bearing capacity is supplemented by a going concern perspective. This analyses capital adequacy with respect to the sustainability of the business model in the event of a loss that is statistically probable only once over a rolling five-year planning horizon.

Sensitivity analysis also plays a part in the comprehensive analysis of risk-bearing capacity by increasing transparency of the impact of potential changes in individual risk factors (such as the impact of changes in interest rates).

Risk-bearing capacity is quantified routinely and as required from a liquidation perspective and based on the going concern scenario and is reported monthly to the Board of Management as part of the regular ongoing internal risk reporting, together with the results and key assumptions of the stress tests performed.

Current situation

The graphic below shows year-on-year changes in risk capital requirements at BayernLB.

Risk capital requirements

EUR million	31 Dec 2017	31 Dec 2016
Credit risk	1,017	773
Market risk	1,339	1,644
• of which actual price risk	386	669
• of which pension risk	953	975
Operational risk	356	445
Participation risk	130	119
Business and strategic risk (includes reputational risk)	466	412
Liquidity cost risk	151	180
from capital provided to institutions of the BayernLB Group	342	355
• credit and participation risks	342	355
Total	**3,802**	**3,928**

BayernLB had adequate risk-bearing capacity, as the provision of risk capital was solid.

The fall in the risk capital requirement mainly related to market risk. As market volatility fell and positions were changed market risk, which includes the risk from pension liabilities, declined. No risk capital is required for real estate risk because of the high level of hidden reserves and higher market values for BayernLB’s own real estate.

As part of BayernLB’s stress testing programme, the possibility of a severe economic downturn (ICAAP stress scenario) is routinely calculated. Since September 2017 the ICAAP stress test has been based on the downside case used in the 2017–2021 medium-term planning. As specified in AT 4.3.3. MaRisk, this reflects the impact of a “severe economic downturn”. The update to the medium-term planning has resulted in an adjustment to the macro-economic basis used to derive the changes in the risk factors for the material risk types examined under the ICAAP stress test. Linking the ICAAP stress test to the latest downside case ensures that the stress parameters will always be up to date, forward looking, economically sound and therefore plausible, and that the stress scenario is consistent within the Bank and across the Group.

Under the severe recession scenario, the risk capital requirement for the individual risks rises to a total of EUR 5.2 billion (restated FY 2016: EUR 5.8 billion).

A severe economic downturn (the ICAAP stress scenario) would see 51.4 percent utilisation of available economic capital (restated FY 2016: 53.3 percent). The regulatory minimum capital ratios were also met in the going concern scenario.

Inverse stress testing

Inverse stress tests were conducted at the BayernLB level as an integral element of the stress testing programme. Contrary to the logic of conventional stress tests, scenarios that could potentially jeopardise the existence of the Bank's current business model are identified using a retrograde procedure. Inverse stress tests are conducted for both individual risk types and across all risk types. The integration of different divisions in the scenario parameters makes it possible to analyse varying perspectives of BayernLB's risk and earnings situation simultaneously and integrate them into the stress testing in a consistent manner. Both qualitative and quantitative analyses are carried out, based in particular on the effects of current developments in external and internal risk factors on BayernLB.

Recovery plan

The BayernLB Group has had a recovery plan in place since 2013, in accordance with the German Recovery and Resolution Directive (Sanierungs- und Abwicklungsgesetz (SAG)), Minimum Requirements for the Design of Recovery Plans (Mindestanforderungen an die Ausgestaltung von Sanierungsplänen (MaSan)) and the supervisory requirement. This sets out the options open to the BayernLB Group to ensure it has sufficient capital and liquidity even in situations of financial stress. Thresholds for one and two-stage indicators are continuously monitored so that early action can be taken to ensure solvency. The status of these indicators is reported to the Risk Committee and the Board of Management monthly and to the Risk Committee of the Supervisory Board quarterly in the risk reporting.

The recovery plan is updated annually and was amended in 2017, in particular by changes in the system of indicators. The thresholds for the one and two-stage indicators in the recovery plan, which are set mainly at Group level and are based on SAG and MaSan, were complied with by comfortable margins. Against this background, no recommendations for action needed to be sent to the Board of Management.

Resolution plan

As part of the reaction to the 2008 financial crisis, lawmakers established the EU regulation on a uniform Single Resolution Mechanism (SRM Regulation) and SAG. These direct resolution authorities at the European and national level to maintain resolution plans for banks that can be activated in an emergency to avert threats to the financial system, where possible without the need for taxpayers' money.

BayernLB complied with its legal responsibilities by assisting the responsible resolution authorities (the Single Resolution Board (SRB)) and the German Financial Markets Stabilisation Institution (Finanzmarktstabilisierungsanstalt (FMSA)) to develop a resolution plan for the BayernLB Group.

Credit risk

In accordance with its business model as a corporate and real estate lender and partner to the savings banks with a regional focus on Bavaria and Germany, the largest risk for BayernLB is credit risk.

Definition

Counterparty risks arise if a transaction results in a claim against a borrower, issuer of securities or counterparty. If these fail to meet their obligations, the Bank suffers a loss equal to the unpaid amount less the value of any realised collateral plus the related settlement costs. This definition covers both lending and guarantee risks from the credit business, and issuer and counterparty risks from trading activities.

Risks from changes in the credit rating of securities are managed primarily through the management of interest rate risks. When managing interest rate risks, a distinction is made between market-related and credit rating-related interest rate risks; this is also reflected in the separate presentation of the risk capital requirements for counterparty risks and market risks.

Country risks, which are another type of counterparty risk, are also measured, managed and monitored. Country risk is defined in the narrow sense as the risk of a country or a business partner whose registered office is located in another country failing to meet its obligations on time or at all due to sovereign acts or economic or political problems (transfer and conversion risks). Country ratings are a key tool for measuring individual country risk. At BayernLB, both country risk in the narrow sense and the sum of the assumed counterparty risks of individual customers in the respective countries (domicile principle) with the exception of Germany are considered when measuring and limiting risks.

Credit Risk Strategy and approval process

The Credit Risk Strategy – which is part of the comprehensive Risk Strategy – is set for BayernLB by BayernLB's Board of Management, taking account of risk-bearing capacity considerations.

While the EU proceedings were still ongoing, the Investment Boards checked compliance with the conditions imposed by the EU that customers and/or transactions had to have a connection with Germany before concluding any transactions.

The credit approval process at BayernLB consists of several stages. The Competence Regulations define the authority of the different competence holders based on the loan volume to be approved, the business area it is allocated to and the rating classification. Credit decisions that ultimately require approval by the Board of Management or Risk Committee of the Supervisory Board must first go through the Credit Risk Board, which itself is a competence holder. The Supervisory Board's Risk Committee decides on all loans that require the approval of the Supervisory Board under the German Banking Act or the Competence Regulations.

New products and products for new markets are subjected to the new product process.

Risk measurement

Risk classification procedure

In accordance with the Internal Ratings Based Approach (IRBA), BayernLB uses rating procedures that are approved by the supervisory authorities. To maintain and refine the rating procedures, BayernLB works mainly with RSU Rating Service Unit GmbH & Co. KG and Sparkassen Rating und Risikosysteme GmbH. All rating procedures are subject to a regular validation process to ensure they are able to correctly determine the default probabilities in each customer and financing segment. Validation includes both quantitative and qualitative analyses of the rating factors and the overall model. The accuracy and calibration of the procedure, the data quality and the design of the model using statistical and qualitative analyses, and users' feedback are examined.

The procedures are regularly modified where necessary. For instance, market-induced factors have been incorporated into various rating procedures in recent years in order to further improve their accuracy.

Exposure at default

Exposure at default is the expected claim amount taking account of a potential (partial) draw-down of open lines and contingent liabilities that would negatively impact risk-bearing capacity in the event of a default. For trading transactions, the current market value is taken as the basis. Any replacement risks are taken account of by means of an add-on.

Collateral valuations and loss ratios

The market value is taken as the starting point for collateral valuation. It is reviewed on both a scheduled and ad-hoc basis and adjusted whenever there is a change in valuation-relevant parameters. Based on these individual collateral valuations, the Bank estimates the size of the loss upon default, which is principally calculated using differentiated models for realisation ratios (average expected proceeds from the realisation of collateral) and for recovery rates (share of proceeds from the unsecured portion of a claim). The unsecured loss given default (LGD) is determined using the recovery rate. It shows the expected loss from the unsecured exposure of a loan. The different resolution scenarios (resolution, restructuring and recovery) are considered. These models are likewise updated and refined in partnership with RSU Rating Service Unit GmbH & Co. KG using pooled data and internal loss data. All models are regularly validated and checked for their representativeness.

Expected loss

Expected loss per transaction/per borrower is a (risk) ratio which not only takes account of the expected claim amount at the time of default but also the customer's credit rating/assigned probability of default and the estimate of losses upon default. This ratio can be used as an indicator of a portfolio's expected risk level.

Expected losses are also relevant for the calculation of standard risk costs, which are used to calculate the risk-adjusted credit terms in the preliminary calculation of the individual transaction (credit pricing). Expected loss allowances are also incorporated into the calculation of flat-rate risk provisions.

Unexpected loss

BayernLB calculates unexpected loss at portfolio level using a simulated credit portfolio model, which estimates default risks on a one-year horizon with a confidence level of 99.95 percent. Dependencies among borrowers in the portfolio are estimated using a country and sector-specific model. In addition, the effects of rating migrations and uncertainties in calculating loss ratios are also taken into account. The impact of an unexpected loss by an individual business partner on the whole portfolio is also calculated for risk analysis purposes.

Risk monitoring

The following instruments are used for monitoring and limiting credit risks in BayernLB:

Early warning

All relevant borrowers and exposures are monitored daily using the Bank's internal early warning system. The goal is to identify negative changes in the risk profile early on by means of suitable early risk warning indicators (e.g. based on market price information such as CDSs or share prices and internal information, in particular information about business partners and transactions) so there is still sufficient scope for action to avoid or minimise risk.

Risk capital requirements

BayernLB manages unexpected losses/risk capital requirements using appropriate limits at Bank and business-area levels. In addition, the sensitivity of key risk input parameters (mainly probabilities of default, loss ratios and correlations) is calculated regularly and supplemented by various stress tests, which in different forms (hypothetical, based on historical data) are used to assess risk-bearing capacity.

Counterparty default risk limits for borrowers/borrower units

In keeping with MaRisk, counterparty risks at borrower and borrower unit level are monitored daily using a limit system. The monitoring takes account of various transaction features using different credit limit types (e.g. issuer risk limit). Where the limits within the BayernLB Group add up to at least EUR 400 million per economic borrower unit, a Group-wide (Group) limit is required. BayernLB's Group Risk Control division monitors the Group limit centrally. To limit risk concentrations, the maximum gross credit volume for each economic borrower unit is limited to EUR 500 million Group-wide. The Board of Management or the Risk Committee of BayernLB's Supervisory Board may approve exceptions to this limit in well-founded individual cases (e.g. good credit rating, profitability and strategy). These customers are individually listed in the quarterly Group Risk Report with their Group limit and gross credit volume.

Sector and country limits

To manage risk concentrations, limits are set for sectors and countries. Sector and country limits apply Group-wide. Limits are set on gross credit volumes and, in some cases, also on the net credit volume for specific countries. Limits are set by BayernLB's Board of Management or can be delegated by it, based in part on an analysis of the sector, country and portfolio structure and a vote taken under the lead of the RO Credit Analysis division. In addition to sector and country limits, the Board of Management also sets or approves as delegated additional specific portfolio guidelines and individual transaction conditions to safeguard portfolio quality. Sector and country limits and portfolio guidelines are monitored centrally by BayernLB's Group Risk Control division. Compliance with the individual transaction conditions is reviewed in the course of the approval process. Sector and country strategies are reviewed annually. Irrespective of this, strategies can be changed as events arise.

Collateral

Another key way in which risks are limited is by accepting the usual types of bank collateral and valuing them on an ongoing basis. When deciding what collateral is needed, particular account is taken of the type of financing, the borrower's available assets, their value and liquidity and whether the relative costs are reasonable (costs of acceptance and ongoing valuation).

Collateral is processed and valued in accordance with the relevant directives, which set out the procedures for valuing the collateral, any discounts to be applied, and how often the valuation must be reviewed. Net risk positions are calculated on the basis of the liquidation value of the collateral.

As part of its IRBA approval, the supervisory authority has granted BayernLB approval to lower its regulatory capital requirements through the use of real estate liens, ship mortgages, registered liens on aircraft, guarantees, financial collateral in the form of securities, cash deposits and credit derivatives.

BayernLB employs derivative instruments to reduce market and counterparty risks. In derivatives trading, the usual practice is to conclude master agreements for the purposes of close-out netting. Collateral agreements exist with certain business partners restricting the default risk associated with certain trading partners to an agreed maximum and authorising a call for additional collateral should this limit be exceeded. Banks and public-sector customers are the main counterparties in the derivatives business. Limits are imposed as part of the generally applicable limitation process for counterparty risk. Furthermore large credit risks are subject to both regulatory and internal management methods.

In credit default swaps (CDSs), BayernLB takes positions as both protection seller and protection buyer, but its focus is not on actively trading credit derivatives. CDS positions are valued and monitored daily at individual transaction level. Gains and losses on these positions are calculated daily on the basis of these valuations.

Problem loan handling and forbearance

Problem exposures are classified in accordance with the standard international categories ("special mention", "substandard", "doubtful" and "loss") in terms of their level of risk, and a special restructuring and risk monitoring process is implemented if warranted.

By initiating suitable measures at an early stage as part of an intensive support or problem loan-handling process, BayernLB aims to minimise or completely prevent losses from occurring.

BayernLB defines problem loans in the substandard and doubtful categories as forbearance exposures.

Exposures which have been restructured in order to minimise the risk of losses are defined as forbearance exposures. An exposure has been restructured if concessions have been granted to a counterparty in financial difficulties. Concessions are defined as the modification of the terms and conditions of the loan agreement (e.g. a deferral, waiver or standstill agreement) or its refinancing.

Exposures cease to be reported as in forbearance if all of the following criteria apply:
- They have not been classified as non-performing (master rating 22 to 24) for more than two years (probationary period).
- Principal and interest payments have been duly made during the probationary period on a material portion of payments due.
- None of the borrower's exposure is more than 30 days overdue at the end of the probationary period.

Please see the accounting policies in the Notes for details of how risk provisions are calculated and assets written down.

Risk provisions

Where necessary, due account has been taken of the risks in the credit business through loan loss provisions. The principles governing loan loss provisioning and writedowns for problem loans establish how loans at risk of default are to be handled, valued and reported (see the note on accounting policies).

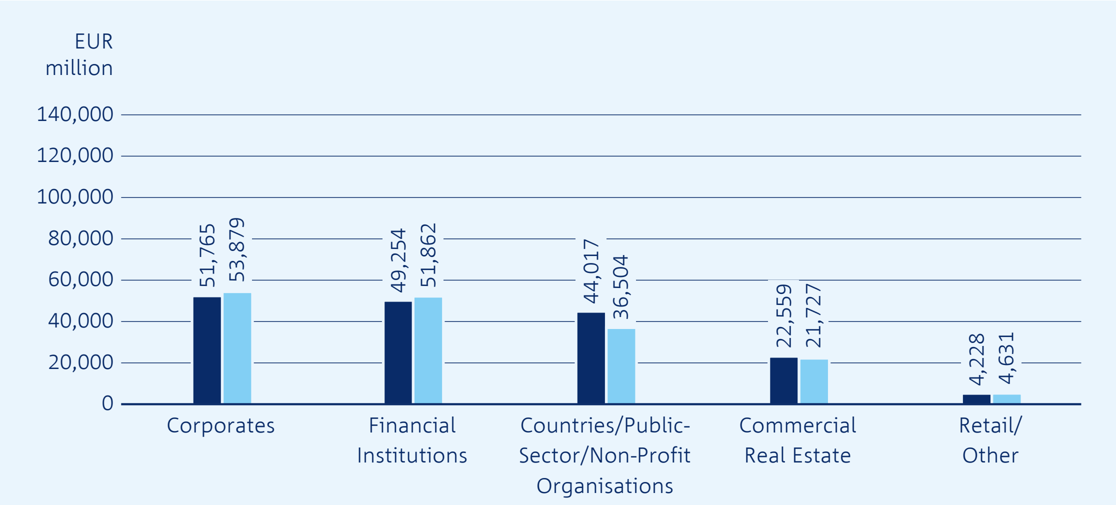
Current situation

The following presentation of credit risk is based on the figures used for internal reporting to the Board of Management and the Risk Committee of the Supervisory Board.

The gross credit volume for credit transactions comprises the gross lending volume – drawdowns plus unutilised commitments – and undrawn internal current account limits. For trading transactions it is calculated from market value, for derivatives transactions from credit equivalent amounts.

Gross credit volume at BayernLB is broken down below by sub-portfolio, rating category, region, issuer risks, replacement risks and net credit volume by size.

Gross credit volume by sub-portfolio



■ 31 Dec 2017 Total: EUR 171,822 million
■ 31 Dec 2016 Total: EUR 168,604 million

In the past financial year the gross credit volume of BayernLB including Bayerische Landesboden-kreditanstalt (BayernLabo) rose from EUR 168.6 billion to EUR 171.8 billion, an increase of 1.9 percent (EUR 3.2 billion).

Most of the growth came in the Countries/Public-Sector/Non-Profit Organisations sub-portfolio, driven by the higher cash holdings at the Deutsche Bundesbank. The Commercial Real Estate sub-portfolio also increased slightly, whereas Financial Institutions and Corporates both saw a fall in lending.

Corporates sub-portfolio

The strategically important Corporates sub-portfolio retained its position as the largest sub-portfolio at BayernLB in the current very challenging market environment. Gross credit volumes were up in three sectors, despite the difficult market. Overall, exposure in the sub-portfolio fell by a total of EUR 2.1 billion to EUR 51.8 billion. This is equivalent to a decline of 3.9 percent.

Exposure was up by EUR 0.7 billion in the consumer goods, tourism, wholesale & retail sector to EUR 6.4 billion. The expansion mainly relates to the financing of cruise ships with export credit insurance and retailers in the United Kingdom.

The car industry also put in a positive performance, with business volumes up by EUR 0.3 billion to EUR 5.5 billion. The increase was mostly among leading auto suppliers and financing subsidiaries with a strong credit rating.

The construction industry also performed well, with lending up by EUR 0.2 billion to EUR 3.4 billion. This was largely caused by an expansion of business with two leading firms in this segment.

Major parts of the logistics & aviation, manufacturing & engineering and utilities sectors saw declines.

Exposure in logistics & aviation fell by EUR 1.1 billion to EUR 5.7 billion, principally driven by lower volumes of aircraft financing.

Gross credit volume in manufacturing & engineering fell by EUR 0.7 billion to EUR 5.8 billion. Much of this decline was due to lower financing volumes in aerospace and defence.

The largest sector in terms of scale, utilities, saw gross credit volume decline by EUR 0.7 billion to EUR 8.4 billion. The focus remains on Western Europe (63.9 percent) and North America (16 percent). Just under two thirds of the sector volume is in structured financing. Project financing in electricity generation from renewable energy is a particular focus, making up 43.7 percent of the sector portfolio. Along with structured financing, traditional corporate loans to utilities account for roughly one third of the sector. These are spread all along the value chain, from generation to supplying the end customer. The market opportunities from the dynamic change under way in the German energy market have been used to grow volume with multi-utilities and in the regulated grid business, whereas the financing of conventional power generation has been cut back.

The position in the strategically important home market was further strengthened. The share of Germany in the Corporates sub-portfolio rose to 63.2 percent (FY 2016: 60.0 percent).

The already high investment grade share in the Corporates sub-portfolio improved once again, to 76.6 percent (FY 2016: 74.9 percent).

The granularity of the sub-portfolio also improved. Customers with a gross credit volume of less than EUR 50 million accounted for 40.0 percent (FY 2016: 38.6 percent) of the portfolio.

Transactions that are no longer part of the core business decreased further: the share of non-core business belonging to this sub-portfolio shrank by another EUR 0.6 billion to EUR 0.6 billion.

Financial Institutions sub-portfolio

Gross credit volume in the Financial Institutions sub-portfolio fell by EUR 2.6 billion to EUR 49.3 billion (FY 2016: EUR 51.9 billion), a decrease of 5.0 percent. As with the previous year, the year under review also saw a decline.

Most of the decrease in volume in the sub-portfolio occurred in the bank sector, where gross credit volumes were down, mainly to global commercial banks. This was predominantly driven by shifts in liquidity at various institutions. Contrary to the decline at global commercial banks, business volumes in the strategically important Savings Banks area rose slightly.

The already very high quality of the sub-portfolio increased again marginally, with the investment grade share rising slightly to 96.6 percent (FY 2016: 96.5 percent). The share in Germany also edged up, to 63.2 percent (FY 2016: 62.5 percent).

Countries/Public-Sector/Non-Profit Organisations sub-portfolio

Gross credit volume in the Countries/Public-Sector/Non-Profit Organisations sub-portfolio rose considerably by EUR 7.5 billion or 20.6 percent to EUR 44.0 billion (FY 2016: EUR 36.5 billion). This was due in particular to an increase in funds held with the Deutsche Bundesbank and was primarily related to fine tuning of the increased excess liquidity.

Excluding the balance held with central banks, the credit volume in the sub-portfolio fell by around EUR 2.6 billion. This was largely to do with reduced lending to German states and foreign sovereigns.

The already very high investment grade share in the Countries/Public-Sector/Non-Profit Organisations sub-portfolio again improved slightly, to 97.7 percent (FY 2016: 97.4 percent).

Commercial Real Estate sub-portfolio

As at the reporting date, gross credit volume in the Commercial Real Estate sub-portfolio amounted to EUR 22.6 billion (FY 2016: EUR 21.7 billion).

In line with strategy, gross credit volume in the reporting period grew by around EUR 0.8 billion or about 3.8 percent. These figures already include the planned reduction of non-core business in the sub-portfolio. Accordingly, gross credit volume in the non-core business shrank by EUR 0.8 billion to EUR 1.0 billion.

The expansion in the business volume was largely in commercial real-estate management in logistics (EUR 0.3 billion), property developers' commercial construction (EUR 0.3 billion) and housing associations (EUR 0.1 billion).

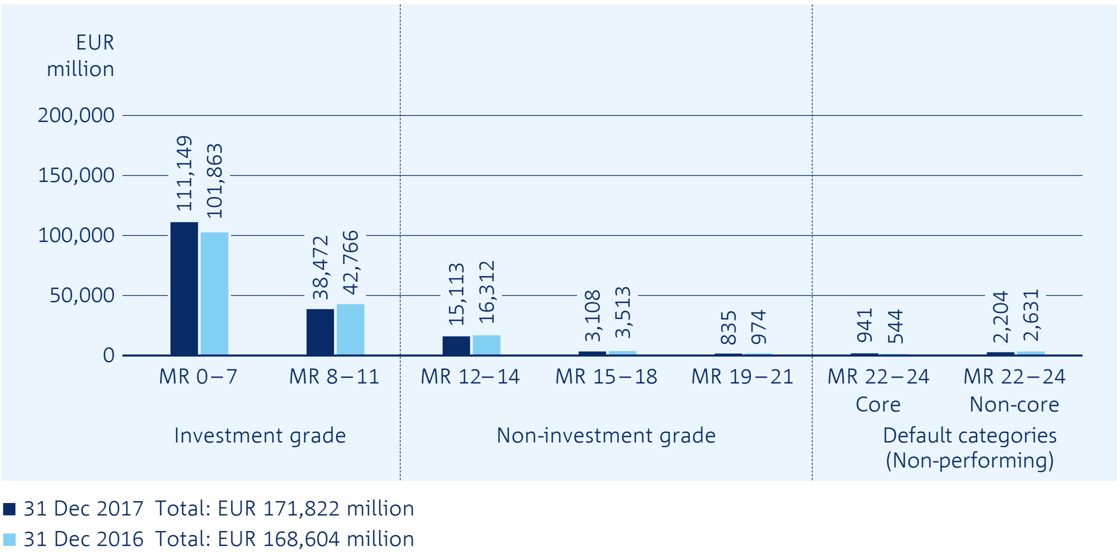
The quality of the Commercial Real Estate sub-portfolio remained high, with the investment grade share rising to 83.0 percent (FY 2016: 81.8 percent). This means that the investment grade share has risen by around 10 percentage points in ten years. The share in Germany increased to 79.1 percent (FY 2016: 75.3 percent). Granularity and collateralisation rates in the sub-portfolio continued to be high for the most part. As at the reporting date, customers with a gross credit volume of less than EUR 50 million accounted for 45.8 percent (FY 2016: 46.6 percent) of the portfolio. The collateralisation ratio was 67.5 percent (FY 2016: 68.8 percent), still close to the three-year average of around 70 percent.

Retail/Other sub-portfolio

In Retail/Other, the smallest sub-portfolio, gross credit volume fell in line with strategy by EUR 0.4 billion to EUR 4.2 billion (FY 2016: EUR 4.6 billion).

The decline was mainly a result of the planned reduction in retail customer business, which has not been a core activity of BayernLB for some years and is being gradually run down.

Gross credit volume by rating category



Gross credit volume at BayernLB in the investment grade master rating (MR) categories 0–11 rose by EUR 5.0 billion in the reporting period. The investment grade share rose accordingly from 85.8 percent to 87.1 percent. The volume in rating category 0–7 rose by EUR 9.3 billion. Most of the increase occurred in the Countries/Public-Sector/Non-Profit Organisations sub-portfolio as a result of the aforementioned higher balances held at the Deutsche Bundesbank. The volume in rating category 8–11 fell by EUR 4.3 billion. This was mainly caused by declines in business volume in the Corporates and Financial Institutions sub-portfolios, which were primarily in this rating category.

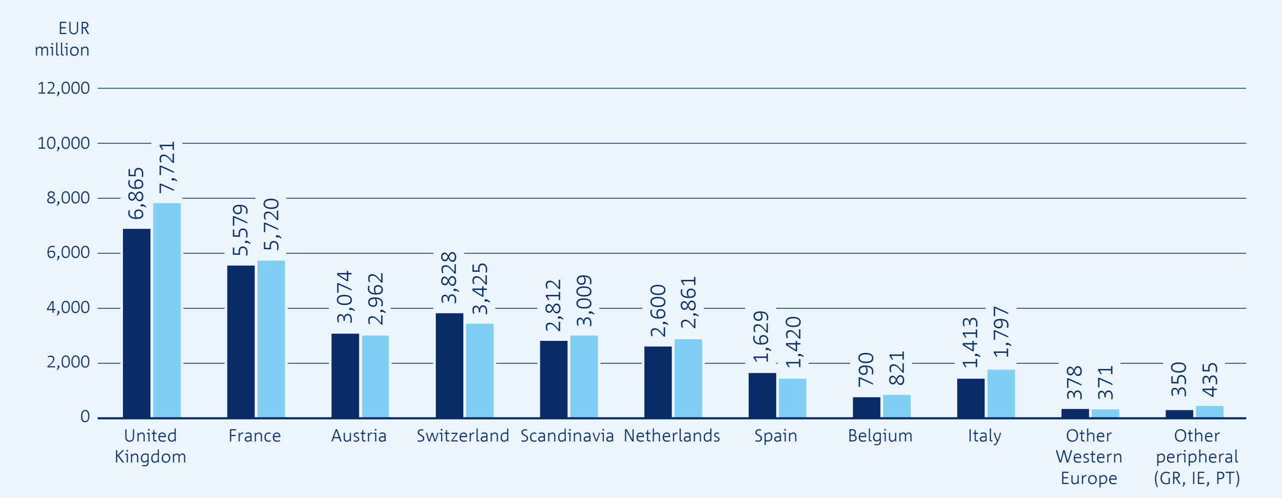
The volume in rating category 12–14 fell by EUR 1.2 billion. In line with this, the proportion of gross credit volume in these rating categories declined from 9.7 percent to 8.8 percent. Gross credit volume in rating categories MR 15–18 and MR 19–21 also fell by a total of EUR 0.5 billion over the reporting period. The proportion of the gross credit volume in these rating categories fell accordingly from 2.7 percent to 2.3 percent.

The already high portfolio quality improved again slightly. The non-performing loan ratio improved during the reporting period to 1.8 percent (FY 2016: 1.9 percent).

Adequate risk provisions were set aside to cover loans added to the default categories.

The following table shows gross credit volume in western European countries (excluding Germany).

Gross credit volume in western European countries



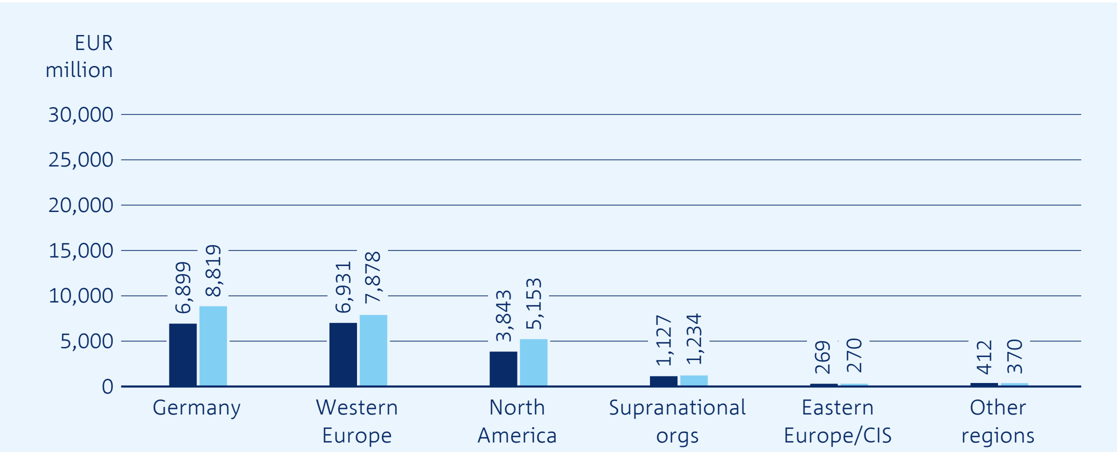
■ 31 Dec 2017 Total: EUR 29,319 million
■ 31 Dec 2016 Total: EUR 30,543 million

In Western Europe (excluding Germany), business volume fell by approximately EUR 1.2 billion to EUR 29.3 billion (FY 2016: EUR 30.5 billion). The fall of EUR 0.9 billion mainly related to the United Kingdom, where business volumes declined in the Corporates and Commercial Real Estate sub-portfolios in particular.

In addition, gross credit volume also decreased markedly in Italy, Finland and the Netherlands. Increases in volume occurred mainly in Switzerland, Spain and Denmark.

The following table shows gross issuer risk by region.

Gross issuer risk by region

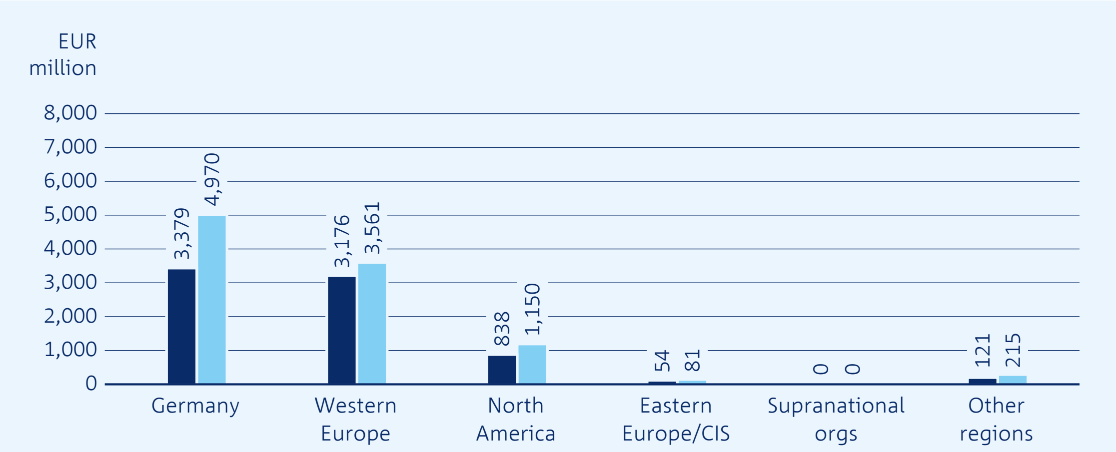


■ 31 Dec 2017 Total: EUR 19,481 million
■ 31 Dec 2016 Total: EUR 23,723 million

Gross issuer risk fell again in the reporting period. It declined in total by around EUR 4.2 billion to EUR 19.5 billion (FY 2016: EUR 23.7 billion). Most of the reduction took place in Western Europe and North America. Gross issuer risk in Germany fell by EUR 1.9 billion to EUR 6.9 billion (FY 2016: EUR 8.8 billion), with reductions largely coming from public-sector borrowers.

The following table shows gross replacement risk by region.

Gross replacement risk by region



■ 31 Dec 2017 Total: EUR 7,568 million
■ 31 Dec 2016 Total: EUR 9,978 million

Gross replacement risk also fell in the reporting period, declining by EUR 2.4 billion to EUR 7.6 billion (FY 2016: EUR 10.0 billion). The reduction occurred mainly in Germany, where gross replacement risk fell by EUR 1.6 billion to EUR 3.4 billion (FY 2016: EUR 5.0 billion). Most of the decrease in Germany was spread evenly across the Corporates, Financial Institutions and Countries/Public-Sector/Non-Profit Organisations sub-portfolios.

Summary

The overall market environment in 2017 remained very challenging, with persistent pressure on margins and high liquidity. Despite this difficult market environment, the core business with target customers was further expanded. The increase in business in the Commercial Real Estate sub-portfolio is particularly worthy of mention.

The quality of the credit portfolio remains very good. This is reflected in the high investment grade share, which also continued to grow, improving significantly from 85.8 percent to 87.1 percent. There was also further growth in the percentage of German customers. Portfolio granularity went down slightly in the reporting period.

Participation risk

Definition

Participation risk (shareholding risk) comprises BayernLB's counterparty (default) risk arising from its shareholdings.

This risk entails a potential loss in value arising from the following:
- The provision of equity or equity-like financing (e.g. silent partner contributions), such as suspension of dividends, partial writedowns, losses on disposal, or reductions in hidden reserves
- Liability risks (e.g. letters of comfort) and/or profit and loss transfer agreements (e.g. assumption of losses)
- Capital contribution commitments

Group Risk Control is responsible for setting standards and reporting at portfolio level. BayernLB has an independent central unit with the authority to issue guidelines for all methods and processes relating to participation risk monitoring. Operational implementation of the risk management instruments is the responsibility of the business units concerned.

Risk Strategy

The goal is to hold a core portfolio of participations that support the BayernLB Group's business activities. The integral components of the BayernLB Group remain Deutsche Kreditbank AG and the other Group strategic subsidiaries: BayernInvest Kapitalverwaltungsgesellschaft mbH and Real I.S. AG Gesellschaft für Immobilien Assetmanagement. The BayernLB Group would like to dispose of its non-core participations.

Participation risks are handled in accordance with the participation risk policy and the participation risk strategy, which is derived from the overarching risk strategy. These are the investment process, the capital base and controlling and reporting. All participations are approved by BayernLB's Board of Management. Other issues to be decided and mandatory consent for investments are governed in detail by the Bayerische Landesbank Act, the Statutes and the Rules of Procedure of the Board of Management of BayernLB.

Measuring and monitoring risk

A classification procedure for identifying and measuring risk with clear guidelines on the early detection of risks has been implemented for all participations held by BayernLB. Key factors in this regard are risk-based early warning indicators and the assessment of the maximum potential loss.

Where BayernLB provides both equity and debt capital, it examines any additional risks, particularly those arising from its status as a lender.

For CRR/CRD IV reporting purposes, participation risks are measured using the simple risk-weighted method unless they fall under the grandfathering method under article 495 para. 1 CRR.

Risk capital requirements for participation risk are measured in ICAAP using the PD/LGD method in accordance with CRR/CRD IV.

Risks from direct participations are reported to the Board of Management in the regular risk reporting process as well as in an annual investment report using the relevant procedures (classification, early warning). Major participations with difficulties are monitored in the intensive support or problem loan processes and reported to the Board of Management on a quarterly basis. The participations report sets out in particular recommendations for action and the implementation status of measures already executed for participations in intensive support or problem loan process with a potential loss in excess of EUR 10 million.

Summary

The participation portfolio moved in line with strategy during the year under review.

Market risk

Definition

Market risk is the risk of potential losses in value from changes in market prices (interest rates, credit spreads, exchange rates, equity and commodity prices) and other factors (correlations, volatility) that affect prices. Accordingly, BayernLB breaks down its market risks into general and specific interest rate risk, currency risk, equity price risk, commodity risk and volatility risk. Risks from pension liabilities are also included under market risks.

Risk Strategy

The Risk Strategy sets out the strategic principles for handling market risks and prescribes the amount of economic capital to be made available for them. Market risks may only be taken on within approved limits and are regularly measured and monitored. The risk capital requirement for pension risk is also limited and monitored separately.

The amount of economic capital provided for market risks is broken down by risk unit and, if necessary, by individual market risk type and, with the exception of pension risks, implemented in the form of value-at-risk (VaR) limits.

In accordance with the current Business and Risk Strategy, market risks are normally only assumed as a result of transactions on behalf of customers and related hedge transactions. Moreover, market risks may also result from transactions for liquidity management, asset/liability management or the non-core businesses.

Risk measurement

BayernLB uses historical simulation as the main VaR method, which is able to take account of correlations between the various types of market risk. Calculations for daily management and monitoring are based on a one-day holding period and a confidence level of 99 percent. The same methods are used for both the trading book and the banking book. Market risks that are not covered by the daily VaR limit calculation are taken into account by alternative risk assessment methods (e.g. stress test estimates). Since 30 June 2017, BayernLB has included a risk premium to estimate the interest rate risk on external credit margins.

Pension risks (risks from BayernLB's pension liabilities) are calculated using a scenario-based approach. The model refinements applied in 2016 remained unchanged in 2017. As a result of the declining volatility in the discount rate, the risk model worked with the intended minimum fluctuation approach in the second half of the year.

Market risk measurement methods are constantly checked for the quality of their forecasting. In the backtesting process, the risk forecasts are compared with actual outcomes (gains or losses). As at 31 December 2017, based on the Basel traffic light approach, the forecasting quality of the procedure for measuring market risk was good.

The outcomes of VaR or scenario-based risk measurement must always be looked at in the context of the assumptions used in the model (mainly the confidence level selected, a one-day holding period, and the use of historical data over a period of around one year to forecast future events). For this reason, risk positions are subjected to regular stress tests based on historical crises and hypothetical changes in market prices, following which the potential risks are analysed. Stress tests take into account all relevant types of market risk and are regularly reviewed to assess the suitability of the parameters used, with parameter changes being made where required.

For risk-bearing capacity one-day VaR is scaled to a one-year horizon, i.e. it is assumed risk positions are closed or hedged over a one-year time horizon. This takes particular account of market liquidity risk – the risk of having to close out risk positions on financial terms that are less favourable than had been expected. Valuation discounts for market liquidity-relevant factors (e.g. bid-ask spreads), which are relevant for accounting and reporting, are also modelled.

The standard approach is used at BayernLB to calculate the regulatory capital backing for trading transactions.

Risk monitoring

In BayernLB, several tools are used to monitor and limit market risks, including VaR and related VaR limits, risk capital limits for market and pension risks, and risk sensitivity and related sensitivity limits, and stress tests, all of which constitute part of the mix in the assessment of risk-bearing capacity in various forms.

Pension risks are monitored monthly. The actual market risks are monitored daily by the market risk controlling units independently of trading units and forwarded as part of the daily reporting to the responsible members of the Board of Management. In addition to complying with these regulatory requirements, this ensures risks are reconciled daily and reported to those responsible for positions. If limits are breached, appropriate measures are taken as part of an escalation procedure.

Interest rate risk in the banking books, excluding pension risks, forms part of the daily risk calculation and monitoring processes of the market risk controlling units. Both contractual and legal termination rights on loan transactions are modelled as options and incorporated into the risk calculation.

Alongside the regulatory interest rate shock scenario of +/−200 basis points calculated for the interest rate risk including pension risk in the banking book, additional interest rate shock scenarios are also calculated and limited. As at 31 December 2017, the change in the present value relative to BayernLB's eligible capital in the interest rate shock scenario of +/−200 basis points was well below the 20 percent limit set in BaFin's criterion for institutions with elevated interest rate risk.

As part of risk reporting the Board of Management is informed monthly and the Risk Committee of the Supervisory Board is informed quarterly about the market risk situation.

Current situation

At BayernLB the main factor affecting the VaR for the actual market risks is general and specific interest rate risk. All other types of risk play a much less significant role by comparison. The current situation for pension risks is presented in the chapter on "Economic capital adequacy".

VaR contribution of actual market risks by risk type (confidence level 99 percent, holding period 1 day)

			1 Jan 2017 to 31 Dec 2017		
EUR million	**31 Dec 2017**	**31 Dec 2016**	**Average**	**Maximum**	**Minimum**
General interest rate VaR	11.7	27.9	16.6	28.4	8.5
Specific interest rate VaR (credit spreads)	4.7	10.3	7.5	11.7	4.7
Currency VaR	1.5	1.9	2.1	3.8	1.4
Equities VaR	0.8	0.7	0.8	0.9	0.6
Commodities VaR	1.7	1.7	1.7	3.4	1.0
Volatility VaR	1.0	5.2	3.0	5.0	0.9
Total VaR*	**14.3**	**26.2**	**17.8**	**26.8**	**11.5**

* *When calculating the risk capital requirement, risk-bearing capacity takes into account VaR, premiums for credit risks on money market transactions, risk on CVA fluctuations and risk on external credit margins.*

Summary

Total VaR fell by around EUR 12 million compared with 31 December 2016. The decrease in general interest rate risk due to a smaller interest rate long position was strengthened further by lower market volatility. Specific interest rate risk declined due to lower market volatility and a reduction in positions, while volatility risk was additionally impacted by changed market data shifts for loan termination rights, which also contributed to the fall in risk.

Liquidity risk

Definition

BayernLB defines liquidity risk as the risk of not being able to meet payment obligations in full or as and when they fall due (insolvency risk or liquidity risk in the narrow sense). It also considers it to be the risk – for example, in a liquidity crunch – that funding cannot be obtained at all or only at above-market rates (securing liquidity or refinancing risk) or that assets can only be sold at a discount to their market prices. This section looks first at liquidity risk in the narrow sense before moving on to refinancing risk, by means of changes in the funding mix.

Risk Strategy

The strategic principles for dealing with liquidity risk in BayernLB are set out in the Risk Strategy. The overriding priority of liquidity risk management and monitoring is to ensure that BayernLB and the BayernLB Group can meet their payment obligations and obtain funding at all times. In addition to stringently ensuring solvency, the primary goal of BayernLB's liquidity management is to ensure long-term access to the market.

These strategic goals are detailed in the Group Guidelines for daily management. There is an emergency plan to safeguard liquidity in the event of emergencies. This defines the processes, management tools and hedging instruments needed to avert potential or address real acute crises. They also contain an escalation mechanism which comes into operation when early warning signals are triggered.

At BayernLB, daily limits are placed on liquidity risks at the operating unit level based on defined scenarios. This ensures that liquidity risks taken are managed and escalated in a consistent and effective manner at all times.

During the reporting year, responsibility for strategic and operational liquidity management at BayernLB belonged to the Group Treasury and the Structuring & Trading divisions of the Financial Markets business area. This ensures adequate liquidity reserves at all times and the management of operational liquidity on the market. Group-wide risk controlling of liquidity risks is conducted by the Group Risk Control division in the Risk Office central area. This area also prepares liquidity overviews, such as capital flow accounts and limit utilisation ratios as the basis for controlling and monitoring liquidity risks. The Liquidity Committee consults with the Group Treasury, Group Risk Control and the Controlling divisions on issues such as liquidity and refinancing strategies and acts as a driving force by preparing courses of action for the Board of Management.

BayernLB actively manages its liquidity reserves in accordance with the regulatory requirements of pillars 1 and 2. The active management of liquidity reserves also includes complying with the Net Stable Funding Ratio (NSFR) and the Liquidity Coverage Ratio (LCR) requirements contained in CRR and its subsequent regulations pursuant to the Delegated Regulation (DelReg). In line with regulatory requirements BayernLB's figures for ratios are regularly reported.

The Additional Liquidity Monitoring Metrics (ALMM) for BayernLB were also reported regularly to the supervisor in 2017. Changes to regulatory requirements that have an impact on liquidity risk, such as the new version of MaRisk, the new version of CRR or new implementing technical standards are constantly monitored in order to identify additional requirements and ensure they are implemented as scheduled in close cooperation with all units affected. This ensures reporting requirements can be met and liquidity can be efficiently managed in the future.

Risk measurement

BayernLB produces daily liquidity overviews to measure, analyse, monitor and report on liquidity risk. These project and compare the liquidity gaps, i.e. the net deterministic and non-deterministic future payment inflows and outflows, and the realisable liquidity counterbalancing capacity to an accuracy of one day.

In terms of volumes and timing, the liquidity counterbalancing capacity quantifies the ability of BayernLB to obtain cash at the earliest opportunity at market rates and in accordance with supervisory restrictions. It indicates the ability to cover liquidity gaps and therefore all cash flow-based liquidity risks. The most important components of liquidity counterbalancing capacity are the holdings of highly liquid securities eligible as collateral at the central bank and other collateral eligible for discounting at the central bank.

Liquidity risks from an off-balance sheet conduit are fully incorporated. Model assumptions are regularly validated using backtesting and adjusted.

To be adequately prepared for various risk situations, BayernLB also calculates and limits its liquidity on the basis of its management scenario and several stress scenarios (systematic and idiosyncratic stress scenarios, and a combination of both).

BayernLB regularly analyses the sensitivity of the liquidity risk profile to a series of extreme hypothetical stress scenarios. A check is also carried out to identify conditions that represent inverse scenarios which could jeopardise normal operations at BayernLB.

Potential concentrations in the liquidity situation and refinancing structure are constantly analysed and monitored. There were no significant concentrations during the year under review.

A net cash flow figure for the next 180 days is calculated daily for the public Pfandbrief register and the mortgage register. In accordance with section 27 of the Pfandbrief Act (Pfandbriefgesetz), the results and other indicators with respect to the register of cover are reported quarterly to the Board of Management. The balance of cumulative cash flows and available liquidity indicated there was surplus liquidity throughout 2017.

Risk management

To safeguard solvency even in times of crisis, BayernLB has a suitable portfolio of liquidity reserves comprising highly liquid securities, central bank facilities and available economic capital in the registers of cover. The liquid funds that these can generate serve to cover unplanned cash outflows, even in a stress scenario.

The medium to long-term structure of the liquidity is managed over all maturities, while limits are placed only on terms of up to five years. To safeguard BayernLB's solvency and its ability to refinance, suitable instruments are used to create a funding structure that is balanced in terms of maturity, instruments and currencies. The key management tool is the Group-wide refinancing planning, which is regularly adjusted in line with the current liquidity situation.

The liquidity transfer price system set up in BayernLB is another instrument to efficiently manage liquidity risks. This ensures that all relevant liquidity risks, costs and benefits are matched up internally to avoid misallocations in liquidity management.

The quality of assets in the register of cover for Pfandbriefs is set by law. This, combined with matching currencies and maturities, ensures that Pfandbriefs issued by BayernLB meet high standards on the market. BayernLB's Collateral Management makes sure that standards are maintained. This ensures that BayernLB has an ongoing ability to issue bonds in the Pfandbrief segment.

Operational liquidity management (observation period of up to one year) also ensures compliance with the supervisory requirements of the Regulation on the Liquidity of Institutions (Liquiditätsverordnung (LiqV)). In the year under review, BayernLB had a liquidity ratio of between 1.35 and 1.61 (FY 2016: between 1.41 and 2.1). The supervisory requirement that there always be sufficient available cash to cover callable payment obligations over the same period (ratio always in excess of 1.0) was therefore observed at all times.

The Bank also met the minimum regulatory Liquidity Coverage Ratio (LCR) at all times in the reporting year through its integrated management of operational liquidity. BayernLB's LCR amounted to 155 percent as at 31 December 2017. The LCR is calculated by comparing highly liquid assets with the net cash outflows for the following 30 days. In the reporting year there was a regulatory requirement that highly liquid assets cover at least 80 percent of the net cash outflow. In 2018, the minimum regulatory ratio will increase to 100 percent.

As a result of the Second Regulation on Amending LiqV issued by BaFin, LiqV no longer applies to institutions supervised by the ECB with effect from the start of 2018. It is therefore no longer monitored by BayernLB and has been fully replaced by the LCR.

Risk monitoring

Group Risk Control monitors liquidity risks independently of trading units and calculates and limits ratios derived from the daily scenario-based liquidity overview.

The risk appetite set by BayernLB limits operational and structural liquidity surpluses separately by currency and across all currencies combined. The available liquidity thus calculated is a key parameter for the amount the managing units can use each day. To support the limiting of liquidity risks, BayernLB has established uniform escalation thresholds which are likewise monitored daily.

In addition to observing the maximum utilisation of available liquidity, ensuring that the time-to-wall figures in the defined stress scenarios are sufficient is key to complying with the liquidity risk limits. Time-to-wall shows the earliest point at which the forecast liquidity requirement ceases to be met by the liquidity counterbalancing capacity. The time-to-wall figures to be observed every day and the scenario-dependent minimum liquidity surplus limits to be observed at BayernLB are set in the Bank's Risk Strategy.

In 2017 the limitation of liquidity risks once again ensured BayernLB was solvent and able to fund itself at all times and made a valuable contribution to optimising the management of short-term and structural liquidity.

BayernLB will continue to adapt the monitoring of liquidity risk as market circumstances and regulatory requirements change so as to optimise liquidity management. To this end, BayernLB has set up an early warning system for risks and regularly conducts backtesting and validation processes.

The liquidity overviews, minimum available unutilised limit and other relevant ratios are included in the risk reports submitted regularly to the Board of Management, the Liquidity Committee" and the responsible managing units.

Current situation

Liquidity overviews are compiled for the purpose of managing and monitoring liquidity risks. This involves calculating the liquidity surplus by subtracting the cumulative liquidity gaps from the realisable liquidity counterbalancing capacity in each maturity band. Expected economic cash flows from non-deterministic products are based partly on modelling assumptions.

The BayernLB management scenario yielded the following results as at 31 December 2017 compared to 31 December 2016:

31 Dec 2017 Cumulative figures in EUR million	**Up to 1 month**	**Up to 3 months**	**Up to 1 year**	**Up to 5 years**
Liquidity surplus	**13,313**	**11,039**	**5,962**	**7,869**
arising from				
• liquidity counterbalancing capacity	23,980	23,600	20,719	6,254
less				
• liquidity gap	10,667	12,561	14,758	−1,616

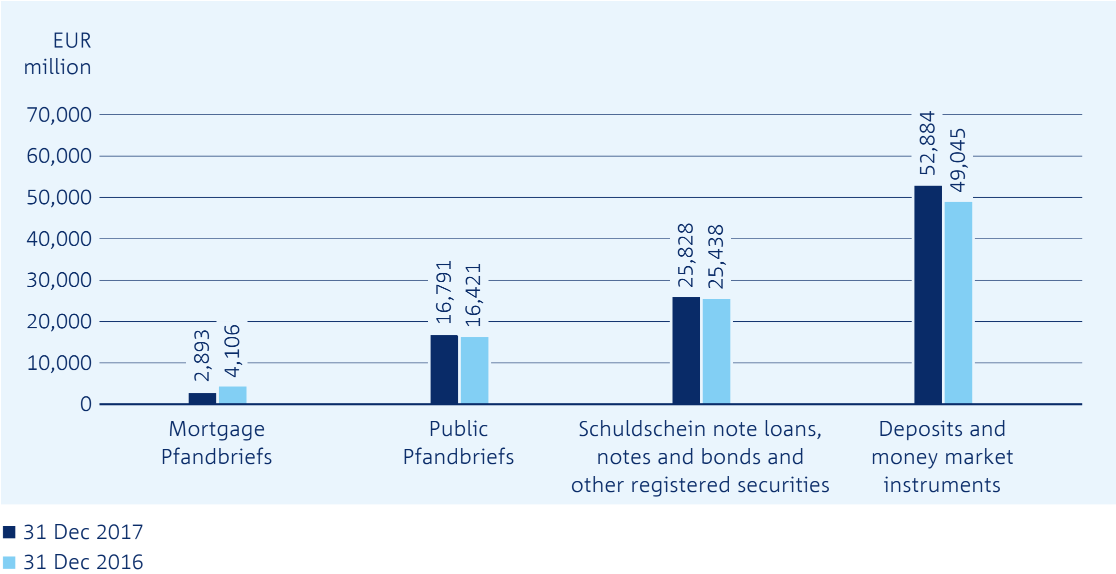
31 Dec 2016 Cumulative figures in EUR million	**Up to 1 month**	**Up to 3 months**	**Up to 1 year**	**Up to 5 years**
Liquidity surplus	**9,725**	**8,523**	**4,304**	**8,410**
arising from				
• liquidity counterbalancing capacity	29,794	27,926	24,500	8,384
less				
• liquidity gap	20,070	19,403	20,195	−26

The changes in liquidity overviews between 31 December 2016 and 31 December 2017 continued to be marked by the focus on core business areas. By using excess liquidity available on the market BayernLB was able to increase its liquidity surplus, especially in maturity bands up to one year.

The liquidity surplus as at 31 December 2017 indicates that BayernLB's liquidity is good.

The change in the refinancing structure of BayernLB for financial year 2017 compared to the previous year was as follows:

Funding structure



The entire year 2017 was marked by the excess liquidity created by the ECB's monetary policy and the associated pressure to invest, which was accentuated by the record low deposit rate at the ECB: minus 0.4 percent. The rise in uncertainty was reflected in the uptrend in volatility triggered by the prevailing political, geopolitical and monetary risks.

Supervisory requirements to monitor and manage liquidity and funding risk continued to be introduced into banks' treasury management in 2017:

- qualitative management metrics to measure short and medium-term minimum liquidity, such as the liquidity coverage ratio (LCR) and the net stable funding ratio (NSFR) and
- qualitative requirements for treasury under the ongoing supervisory review and evaluation process (SREP).

After years spent expanding and extending the funding mix, funding policy in 2017 sought to strike a balance between meeting minimum regulatory requirements and maximising the economic efficiency of liabilities.

In line with the sector trend, BayernLB also decided to link the interest rate on short-term deposits of institutional customers with the interest rate on the ECB's deposit facility.

The funding strategy also focused on maintaining and expanding the bail-in eligible liabilities in accordance with the new minimum TLAC and MREL requirements. BayernLB has benefited too from Moody's upgrading of long-term deposits to Aa3 (outlook stable) and short-term deposit rates to P-1 through the inflow of new short-term liquidity. Money market liabilities reflect the low level of holdings standard for the industry at year-end, e.g. in repos and time deposits.

Restrained capital market funding at BayernLB helped reduce excess liquidity in 2017, but even so the low rates on the capital market were used opportunistically to raise strategic (reserve) financing. Unsecured funding was slightly ahead of plan at EUR 3.5 billion, but secured funding was cut to EUR 2.2 billion. This was around EUR 1.3 billion less than planned, not least because of the restrained performance on the asset side of the business and moves in interest rates and currencies which were favourable for margins. Cross-funding within the BayernLB Group was further reduced, as planned, but was on occasion a source of considerable inflows of liquidity.

BayernLB's funding spreads in 2017 were at the lower end of its peer group and reflect not just its good rating but also low demand. The savings bank sector was a key purchaser of unsecured bearer bonds. Huge demand for securities, including corporate issues, due to the ECB's purchasing programme saw supply tighten further across the whole market. No unit of the BayernLB Group drew any funds under the ECB's Targeted Long-Term Refinancing Operations II (TLTRO II).

This trend meant that maturing capital market issues did not have to be replaced in full, resulting in a slight decline in capital market financing outstanding. The rating upgrade and the early end to the state-aid proceedings led to a positive change in how BayernLB is perceived as a market participant, resulting in a marked increase in inflows of money market deposits, including from abroad.

Higher tax receipts meant that the demand for credit from the public sector (one of BayernLabo's target groups) was limited.

BayernLB's sustainable business model and stable earnings with a strong awareness of risks (factors which had led to three ratings upgrades since 2014) allowed the Bank to bring the EU state-aid proceedings to an early close and repay EUR 1 billion to the Free State of Bavaria at the end of the first half of 2017.

2018 will see the legal basis laid for a new class in the seniority ranking of bank liabilities in Germany: senior unsecured bonds. Until that point, any unsecured issues will be subordinate to the new class in the event of liability. Moody's saw the structural subordination of unsecured bank bonds in the liability waterfall as a reason to assume less government support for this class of debt in future crises and placed senior unsecured bonds on the watchlist with a negative outlook (BayernLB has a senior unsecured rating of A1, outlook negative). This legal development at EU level results in existing unsecured bonds ceasing to be eligible at the ECB. This drawback compared to the new category of senior unsecured bonds is offset by the fact that they qualify for inclusion in regulatory ratios (e.g. they can be bailed in).

In the coming financial years liquidity management and monitoring at BayernLB will continue to revolve around the funding options available. The focus will continue to be on ensuring liquidity reserves at BayernLB are always adequate, even in stress situations.

As well as actively managing liquidity reserves, the management of supervisory and economic liquidity risk will continue to be built around a broadly-diversified funding structure. This is supported by a reliable base of domestic investors and retail customer deposits at subsidiary DKB.

Summary

Thanks to its forward-looking liquidity management, BayernLB had good liquidity throughout the period under review.

Operational risk

Definition

In line with the regulatory definition in CRR, BayernLB defines operational risk as the risk of loss resulting from inadequate or failed internal processes, people and systems, or from external events. This includes legal risks.

The main sub-risks below the level of operational risk identified in 2017 as part of the MaRisk risk inventory were legal risk, compliance risk, information security risk (including cyber risk), outsourcing risk, model risk and process risk.

Risk Strategy

The treatment of operational risks is set out in the Risk Strategy and related sub-risk strategies and guidelines for non-financial risks. The strategic objective is to minimise or avoid risk in such a way that the costs do not exceed the risk of loss. This requires operational risks to be identified and assessed as completely as possible.

Moreover, as part of ensuring risk-bearing capacity, the risk appetite and limits are set for operational risks, and compliance with these is monitored on an ongoing basis.

Risk measurement

Operational risks for the calculation of risk-bearing capacity are quantified using the operational value at risk (OpVaR) calculation. The calculation is based on the losses incurred at BayernLB, the external losses collected via a data consortium, potential operational risks collected as part of the Operational Risk Self Assessment and the BayernLB scenario analyses (potential losses). The calculation is based on a loss distribution approach, using a confidence level of 99.95 percent. The key model assumptions and parameters used in the model are validated once a year. The risk capital requirement for BayernLB as at 31 December 2017 was EUR 356 million (FY 2016: EUR 445 million).

The newly designed OpRisk Self Assessment (OSA) was completed in 2017, resulting in a considerable improvement in the quality of ex ante data. The results will be used as a database for future OpRisk management activities (e.g. managing measures, developing early warning indicators) and for quantifying operational risks.

The standard regulatory approach is used to calculate the regulatory capital backing for operational risks.

Risk management and monitoring

Operational risks are managed and monitored both centrally in the Group Risk Control division and decentrally in the responsible divisions (e.g. the Legal Services division for legal risks).

The Group Risk Control division has the authority to establish guidelines for all methods, processes and systems to quantify operational risks. The relevant subsidiaries (participations) are included in the BayernLB Group's loss event reporting procedure.

Management of operational risk is complemented by an efficient system to monitor the execution of measures, which was further enhanced in 2017.

Operational risks at BayernLB are reported to the Board of Management every quarter as part of the regular reporting on risk and on an ad hoc basis if material losses occur. The operational risk loss situation and trends and the resulting capital charges form a major part of the regular reporting.

Operational risks are included in stress analyses and the monitoring of risk-bearing capacity across all types of risk, and integrated into the overall management of risk and the Risk Strategy.

Business continuity management

Business Continuity Management (BCM) is used at BayernLB to manage risks to the continuation of business operations and deal with crisis situations. BCM establishes a core procedure for continuing/restoring operations and has an integrated emergency/crisis management procedure for handling events that could have a sustained impact on the Bank's activities and resources.

BCM requirements are laid out in BayernLB's BCM Strategy, taking account of the Risk Strategy. BCM is also embedded in the data security policy.

BCM identifies time-critical activities and processes and lays down specific business continuity and restart procedures to protect these. Regular tests ensure that the emergency measures and crisis control procedures are effective and appropriate and are continually improved.

The roles and responsibilities and where these intersect are clearly defined and set out in the Bank-wide BCM standards.

The emergency officer monitors compliance with these standards and reports to the member of the Board of Management responsible for BCM on a regular basis. Central BCM information is also used to manage operational risks.

The Chief Operating Officer has overall responsibility for BCM.

Current situation

Losses from operational risks amounted to EUR 51.8 million as at 31 December 2017 (FY 2016: EUR 65.5 million). BayernLB accounted for the largest share, BayernLabo accounting for EUR 0.02 million (FY 2016: EUR 0.02 million).

The loss profile at BayernLB in 2017 was affected by provisions for legal change risk. A major factor in this was the ruling by the Federal Court of Justice that processing fees in corporate banking are invalid. The 2017 loss profile was positive in the context of BayernLB's continuing business activities. The total loss overall, and the risk capital requirement, fell substantially.

Summary

The amount of operational risk losses in 2017 was in line with expectations.

Summary and outlook

All in all, BayernLB's risk profile in financial year 2017 was stable.

BayernLB had adequate risk-bearing capacity at all times in the financial year and as at 31 December 2017. The stress scenarios conducted also confirm that adequate capital is held. In addition, BayernLB had a comfortable supply of liquidity on hand. Risk provisions take appropriate account of known risks. Regulatory solvency requirements were met. Equity capital for the purpose of risk coverage amounted to EUR 9.5 billion (further details are reported in the management report under the banking supervisory ratios under CRR/CRD IV).

The risk management and controlling system at BayernLB has appropriate processes to ensure compliance with regulatory requirements and manage risks from an economic viewpoint.

Non-financial declaration

BayernLB's non-financial declaration and the BayernLB Group's non-financial declaration are combined in accordance with Section 315b para. 3 HGB in conjunction with Section 289b para. 2 sentence 2 HGB and are published in the 2017 annual report of the BayernLB Group.

The combined non-financial report for 2017 will be submitted to the operator of the Federal Gazette along with the consolidated financial statements and the Group management report of the BayernLB Group for financial year 2017 and published in the Federal Gazette.

BayernLB's annual financial statements and the BayernLB Group's annual report can also be viewed online at www.bayernlb.de.

Appendix to the management report of BayernLB for 2017

Equal pay report pursuant to section 21 of the German Remuneration Transparency Act for the period from 1 January to 31 December 2016

The German Remuneration Transparency Act (EntgTranspG) requires an appendix to be attached to the management report for 2017; this report relates, however, to calendar year 2016 (section 25 para. 2 EntgTranspG).

Measures to promote equality between men and women and their impact

BayernLB attaches great importance to equality between men and women. Accordingly it set multi-year targets to promote equality between men and women back in 2012, long before the German Remuneration Transparency Act was promulgated. In 2017, BayernLB evaluated the progress towards achieving the targets set for the period up to the middle of 2017. Progress was made in all target areas, including the following:

The proportion of women in management positions rose, both in the second level of management, which reports directly to the Board of Management, and the management levels below this. Besides this, a working group developed and implemented concrete measures to promote women in the following action areas: raising the awareness of all managers, increasing the numbers of female applicants for managerial positions at all levels of the hierarchy, creating women's networks, and optimising processes. Women are also co-opted into the talent programme, which fosters top performers and employees with potential at BayernLB, in line with the gender balance among employees.

Special priority is given to the promotion of female junior staff. BayernLB also increased the proportion of women in trainee programmes. The proportion of applications from women is already higher than the proportion of women at universities offering a degree in business administration, specialising in finance. Efforts to promote women are bearing fruit not only in terms of applications, but also recruitment. The proportion of women selected was even significantly higher than the gender balance among applicants.

A good work-life balance also has a high priority. BayernLB has been offering flexible working hours for a long time now. Employees can choose themselves when to begin and finish work, in line with operational requirements. In addition, many now work from (mobile) remote workstations on some days of the week. Both options give employees the flexibility to harmonise their working and family lives. In a further move, the Bank has set up its own website on the intranet to raise awareness of what BayernLB offers in this area and of equality issues.

BayernLB offers special seminars for women as well and the role of equality officer was also strengthened. BayernLB set up a working group to support the equality officer in her work.

Measures to achieve equal pay for men and women

At BayernLB equal pay for people with the same qualifications and level of performance is a given. Pay scales are based on the collective wage agreements in the private banking industry and in public banks. Remuneration for non-pay scale employees is governed by agreements with staff representatives. BayernLB ensures the remuneration structure for collective wage agreements and agreements with staff representatives is transparent and gender neutral. Both HR and staff representatives adhere to the principle of equal treatment in equal measure.

Headcount and level of employment

In financial year 2016, BayernLB employed an average of 3,184 people. Of this figure, 1,475 were women and 1,709 were men.

The breakdown by level of employment is as follows:

Level of employment	Average headcount in 2016
Full-time	**2,270**
• Female	765
• Male	1,505
Part-time	**914**
• Female	710
• Male	204
Total	**3,184**

Financial statements of BayernLB

Balance sheet and income statement

Balance sheet – Bayerische Landesbank
as at 31 December 2017

Assets				2017	2016
	EUR ’000	EUR ’000	EUR ’000	EUR ’000	EUR ’000
Cash reserves					
a) Cash			116,597		167,970
b) Deposits with central banks			1,696,161		499,261
of which:					
at Deutsche Bundesbank	*196,260*				*216,841*
				1,812,758	**667,231**
Due from banks					
a) Payable on demand			11,996,156		2,300,081
b) Other receivables			23,007,485		23,877,793
of which:					
• *mortgage loans*	–				*14,582*
• *municipal loans*	*159,518*				*179,149*
				35,003,641	**26,177,874**
Due from customers				**67,336,509**	**68,810,758**
of which:					
• *mortgage loans*	*13,732,853*				*14,349,468*
• *municipal loans*	*29,276,290*				*28,523,525*
Bonds and other fixed-income securities					
a) Money market instruments					
aa) issued by public-sector borrowers		*2,119*			—
of which:					
eligible as collateral at Deutsche Bundesbank	—				—
ab) issued by other borrowers		21,769			216,622
of which:					
eligible as collateral at Deutsche Bundesbank	—				—
			23,888		216,622
b) Bonds and notes					
ba) issued by public-sector borrowers		9,109,153			10,739,739
of which:					
eligible as collateral at Deutsche Bundesbank	*6,011,359*				*6,902,269*
bb) issued by other borrowers		7,324,758			9,456,270
of which:					
eligible as collateral at Deutsche Bundesbank	*6,770,925*				*8,386,722*
			16,433,911		20,196,009
c) Own debt securities			68,627		248,558
Nominal value	*62,891*				*240,641*
				16,526,426	**20,661,189**
Equities and other non-fixed income securities				**95,218**	**40,412**
Trading portfolio				**7,087,708**	**11,096,611**
Carried forward				127,862,260	127,454,075

				2017	2016
Liabilities	*EUR ’000*	EUR ’000	EUR ’000	EUR ’000	EUR ’000
Due to banks					
a) Payable on demand			6,329,684		6,280,035
b) With agreed maturity or period of notice			34,842,610		37,011,974
of which:					
• *registered mortgage Pfandbriefs*	*431,583*				*465,473*
• *registered public Pfandbriefs*	*754,952*				*679,009*
• *issued to the lender to secure loans raised:*					
• *registered mortgage Pfandbriefs*	—				—
• *registered public Pfandbriefs*	—				—
				41,172,294	**43,292,009**
Due to customers					
a) Savings deposits					
aa) with agreed period of notice of three months		—			—
ab) with agreed period of notice of more than three months		—			—
			—		—
b) Other liabilities					
ba) payable on demand		9,997,576			6,782,760
bb) with agreed maturity or period of notice		26,924,150			25,245,795
of which:					
• *registered mortgage Pfandbriefs*	*934,514*				*1,181,725*
• *registered public Pfandbriefs*	*6,155,488*				*5,608,122*
• *issued to the lender to secure loans raised:*					
• *registered mortgage Pfandbriefs*	—				—
• *registered public Pfandbriefs*	—				—
			36,921,726		32,028,555
				36,921,726	**32,028,555**
Securitised liabilities					
a) Bonds issued					
aa) mortgage Pfandbriefs		1,526,961			2,458,497
ab) public Pfandbriefs		9,880,827			10,134,181
ac) other bonds		18,522,835			18,576,359
			29,930,623		31,169,037
b) Other securitised liabilities			6,789,755		3,568,090
of which:					
• *money market instruments*	*6,729,720*				*3,568,090*
• *own acceptances and promissory notes outstanding*	—				—
				36,720,378	**34,737,127**
Trading portfolio				**3,516,501**	**4,923,473**
Liabilities held in trust				**4,878,560**	**4,946,157**
of which: *loans on a trust basis*	*4,878,560*				*4,945,766*
Other liabilities				**648,842**	**608,891**
Carried forward				123,858,301	120,536,212

Balance sheet – Bayerische Landesbank
as at 31 December 2017 (continued)

				2017	2016
Assets	*EUR '000*	EUR '000	EUR '000	EUR '000	EUR '000
Carried forward				127,862,260	127,454,075
Participations				**245,220**	**233,094**
of which:					
• *in banks*	*19,616*				*18,213*
• *in financial service providers*	*—*				*—*
Shares in affiliated companies				**2,288,885**	**2,295,497**
of which:					
• *in banks*	*2,140,553*				*2,140,553*
• *in financial service providers*	*—*				*—*
Assets held in trust				**4,878,560**	**4,946,157**
of which:					
loans on a trust basis	*4,878,560*				*4,945,766*
Intangible assets					
a) Internally generated industrial property rights and similar rights and assets			51,953		55,718
b) Purchased licences, industrial property rights and similar rights and assets as well as licences to such rights and assets			20,861		21,847
c) Goodwill			—		—
d) Down payments effected			—		—
				72,814	**77,565**
Tangible assets				**324,156**	**334,033**
Other assets				**2,013,115**	**1,561,861**
Pre-paid expenses					
a) From the new issues and loans business			252,193		237,418
b) Others			413,017		445,238
				665,210	**682,656**
Total assets				**138,350,220**	**137,584,938**

Rounding differences may occur in the tables.

Liabilities	EUR '000	EUR '000	EUR '000	2017 EUR '000	2016 EUR '000
Carried forward				123,858,301	120,536,212
Deferred income					
a) From the new issues and loans business			112,060		90,773
b) Others			590,330		718,160
				702,390	**808,933**
Provisions					
a) For pensions and similar obligations			2,505,510		2,364,042
b) For taxes			286,027		227,234
c) Other provisions			637,006		793,314
				3,428,543	**3,384,590**
Subordinated liabilities				**1,346,670**	**3,263,994**
Profit participation certificates				**434,550**	**434,550**
of which:					
due in less than two years	*434,550*				*50,000*
Fund for general bank risks				**975,727**	**915,441**
of which:					
special items pursuant to section 340e para. 4 HGB	*55,680*				*42,746*
Equity					
a) Subscribed capital					
aa) statutory nominal capital	2,800,000				2,800,000
uncalled nominal capital	—				—
called nominal capital		2,800,000			2,800,000
ab) capital contribution		612,016			612,016
ac) silent partner contributions		47,580			1,047,580
			3,459,596		4,459,596
b) Capital reserve			2,181,643		2,181,643
c) Retained earnings					
ca) statutory reserves		1,267,508			1,267,508
cb) other retained earnings		645,292			332,471
			1,912,800		1,599,979
d) Net retained profits			50,000		—
				7,604,039	**8,241,218**
Total liabilities				**138,350,220**	**137,584,938**
Contingent liabilities					
a) Contingent liabilities from the endorsement of bills rediscounted			—		—
b) Liabilities from guarantees and indemnity agreements (see also the notes)			10,051,902		9,891,286
c) Liabilities from collateral furnished for third-party obligations			—		—
				10,051,902	**9,891,286**
Other liabilities					
a) Repurchase obligations from non-genuine sale and repurchase agreements			—		—
b) Placement and underwriting commitments			—		—
c) Irrevocable loan commitments			22,264,696		21,393,284
				22,264,696	**21,393,284**

Rounding differences may occur in the tables.

Income statement – Bayerische Landesbank
for the period from 1 January to 31 December 2017

				2017	2016
	EUR '000	EUR '000	EUR '000	EUR '000	EUR '000
Interest income from					
a) Credit and money market transactions	1,845,720				1,930,563
less negative interest	−49,026				−26,853
		1,796,694			1,903,710
b) Fixed-income securities and debt-register claims		207,800			291,406
			2,004,494		**2,195,116**
Interest expenses					
Interest expenses from bank business		−1,391,256			−1,523,687
less positive interest		87,769			46,046
			−1,303,487		**−1,477,641**
				701,006	**717,475**
Current income from					
a) Equities and other non-fixed income securities			565		226
b) Participations			4,722		4,798
c) Shares in affiliated companies			7,214		17,553
				12,501	**22,577**
Income from profit-pooling agreements, profit transfer agreements and partial profit transfer agreements				**14,419**	**273,969**
Commission income			**229,116**		**248,850**
Commission expenses			**−52,656**		**−54,298**
				176,460	**194,552**
Net income or net expenses of the trading portfolio				**116,407**	**98,350**
of which: allocation to/releases from the fund for general bank risks pursuant to section 340e para. 4 HGB	*−12,934*				*−10,976*
Other operating income				**338,295**	**419,859**
General administrative expenses					
a) Personnel expenses					
aa) salaries and wages		−314,495			−336,579
ab) social security contributions, pensions and other employee benefits		−185,387			−154,214
			−499,882		−490,793
of which: for pensions	*−80,604*				*−18,066*
b) Other administrative expenses			−372,258		−334,548
				−872,139	**−825,341**
Amortisation, depreciation and writedowns on intangible assets and tangible assets				**−26,726**	**−47,223**
Other operating expenses				**−359,021**	**−241,858**
Carried forward				101,202	612,360

				2017	2016
	EUR ’000	EUR ’000	EUR ’000	EUR ’000	EUR ’000
Carried forward				101,202	612,360
Amortisation, depreciation and writedowns on receivables and certain securities and additions to provisions in the credit business			**−26,842**		**−364,086**
of which:					
• *withdrawal from the fund for general bank risks*	*—*				*—*
• *allocation to the fund for general bank risks*	*−47,352*				*−41,826*
Income from reversals of writedowns on receivables and certain securities as well as from the release of provisions in the credit business			**—**		**—**
of which:					
• *withdrawal from the fund for general bank risks*	*—*				*—*
• *allocation to the fund for general bank risks*	*—*				*—*
				−26,842	**−364,086**
Amortisation, depreciation and writedowns on participations, shares in affiliated companies and securities classified as fixed assets			**—**		**—**
Income from reversals of writedowns on participations, shares in affiliated companies and securities classified as fixed assets			**324,011**		**169,543**
				324,011	**169,543**
Expenses from loss transfers				**−1,696**	**−2,916**
Gains or losses on ordinary activities				**396,675**	**414,901**
Extraordinary income			**2,243**		**15,297**
Extraordinary expenses			**−8,270**		**−9,736**
Net extraordinary income/loss				**−6,026**	**5,561**
Taxes on income and earnings			**−36,578**		**−90,190**
of which: deferred taxes	*—*				*—*
Other taxes, unless disclosed under “Other operating expenses”			**8,750**		**2,199**
				−27,828	**−87,991**
Net income/loss for the financial year				**362,820**	**332,471**
Withdrawals from capital reserve				—	—
Allocations to retained earnings					
a) To the statutory reserves			—		—
b) To other retained earnings			−312,820		−332,471
				−312,820	**−332,471**
Replenishment of profit participation certificates				—	—
Replenishment of silent partner contributions				—	—
Net retained profits				50,000	—

Rounding differences may occur in the tables.

Notes

The annual financial statements of Bayerische Landesbank, an institution established under public law, Munich, Germany (BayernLB), entered in the Commercial Register at Munich District Court (HRA 76030), have been prepared in accordance with the provisions of the German Commercial Code (HGB), the Ordinance Regulating Accounting for Financial Institutions and Financial Service Providers (RechKredV), the provisions of the Pfandbrief Act (PfandBG) and the supplementing regulations of the Bayerische Landesbank Act and the Bank's Statutes.

The layout of the balance sheet and income statement complies with the forms of RechKredV and includes items required for Pfandbrief banks.

Figures are given in millions of euros. Rounding differences may occur in the tables.

Accounting policies

Assets and liabilities are measured in accordance with the general measurement provisions of sections 252 et seqq. HGB, taking account of the special provisions applicable to banks (sections 340 et seqq. HGB).

The accounting policies used for the annual financial statements as at 31 December 2017 were the same as those used for the annual financial statements as at 31 December 2016. Any changes on the previous year are noted below.

Receivables and liabilities (non-trading portfolio)

Receivables in the non-trading portfolio are reported at nominal amount or at cost and decreased by any required impairments. Where there is no further reason for impairment, a reversal is made. Low-interest or non-interest bearing receivables are discounted if necessary.

Risk provisions in the credit business comprise impairments and provisions for all identifiable credit and country risks, for latent default risks and the provisions for general banking risks.

Risk provisions are calculated in accordance with the methods used in the International Financial Reporting Standards (IFRS). On indications of impairment, specific loan loss provisions are calculated by deducting from the carrying amount of the receivable the present value of future expected cash flows calculated using the original effective interest rate. Additions to or releases of risk provisions are made if expected cash flows change.

To show latent credit risks, the method for calculating portfolio loan loss provisions under IFRS, which takes into account historical probabilities of default, loss ratios and the latest ratings, is also used to calculate HGB general loan loss provisions. General loan loss provisions are made for receivables due from banks, from customers and off-balance sheet transactions for which no specific loan loss provisions have been made.

General loan loss provisions for country risks not already taken into account in specific loan loss provisions are calculated based on the probabilities of default and loss rates specific to each country.

Reserves have been established to meet general bank risks in accordance with sections 340f and 340g HGB. The reserves in accordance with section 340f HGB were deducted from the underlying asset items on the assets side.

Liabilities in the non-trading portfolio are recognised at their settlement value. Discounted bonds and similar liabilities are reported at their net present value.

Differences between the purchase price and the nominal value with interest characteristics are reported under the pre-paid expenses and deferred income items and amortised on a pro-rata temporis basis.

Securities (non-trading portfolio)

The securities portfolios in the liquidity reserve are measured according to the strict principle of lower of cost or market value observing the requirement to reverse writedowns. Securities in the "securities measured as participations" portfolio (participations portfolio) are measured according to the less strict principle of lower of cost or market value; any premiums and discounts arising are amortised on a pro-rata temporis basis.

Securities allocated to the investment portfolio are regularly tested for indications of permanent impairment. The latent risks of default are recognised through the creation of general loan loss provisions.

Trading portfolio

All financial instruments in the trading portfolio, including executory contracts concluded for trading, are measured at fair value less a risk discount.

The methodology used to calculate the risk discount is based on the supervisory regulations of the Minimum Requirements for Risk Management (Mindestanforderungen an das Risikomanagement (MaRisk)) and the requirements of article 365 of the Capital Requirements Regulation (CRR). The risk discount is calculated in the form of value-at-risk (VaR) with a confidence level of 99 percent, a holding period of 10 days and an observation period of one year. The risk discount for the whole trading portfolio is recognised under the trading portfolio item.

All income and expenses from the trading portfolios, including their refinancing costs, are recognised under the net income or net expenses of the trading portfolio item. In accordance with section 340e para. 4 HGB, allocations to the fund for general bank risks required by section 340g HGB are made from the net income of the trading portfolio.

The Bank's own criteria for including financial instruments in the trading portfolio were left unchanged in the reporting year.

Fair value

The fair value is the amount for which a financial instrument could be exchanged between knowledgeable, willing parties in an arm's length transaction.

The fair value is calculated where possible by referring to a quoted price on an active market (e.g. stock market price). A market is considered active for a financial instrument if quoted prices are readily and regularly available from an exchange, dealer or similar, and these prices represent actual and regularly occurring market transactions between knowledgeable, willing parties in an arm's length transaction.

If no active market exists, the fair value is calculated using a range of valuation methods including valuation models based on the net present value method and indicative valuation prices. The goal is to establish what the transaction price would have been in an arm's length exchange between knowledgeable, willing parties on the valuation date. An inactive market is characterised by very limited trading volumes, very wide bid/ask spreads and wide swings in indicative prices.

Valuation models

Fair values are calculated using recognised valuation models based largely on observable market data. The net present value method and option price models are among the valuation models used.

When a market price is not available, the net present value method is used for interest-bearing financial instruments. This method calculates the instruments' value based on their cash flow structures, taking account of their nominal values, residual maturities and the agreed day-count convention. If the financial instrument has a contractually agreed fixed cash flow, the cash flow structure is calculated using the agreed cash flows. In the case of variable rate instruments, cash flows are determined using forward curves. Discounting uses matching currency and maturity and secured and unsecured yield curves, and a risk-adjusted spread. Market data is used where spreads are publicly available. In the case of OTC derivatives, discounting takes account of the collateral status and currency. In addition, counterparty risk and own default risk are taken into account by considering any netting agreements (credit valuation adjustment/debit valuation adjustment). In the case of uncollateralised OTC derivatives, account is taken of bank-specific financing conditions using a funding valuation adjustment.

Options and other derivative financial instruments with option characteristics are valued largely using the Black-Scholes option pricing model. The displaced diffusion model was used to calculate valuations when interest rates were negative. The Black-Scholes model was used here again, after parallel shifting of the strike price and forward price parameters (depending on the product type and currency). The following valuation parameters are used when measuring options and other derivatives: cumulative probability distribution function for standard normal distribution, option strike prices, continuously compounding risk-free interest rates (for different currencies and maturities), price volatility, time to option expiry, estimated dividends, interest rate and pricing barriers, discounts, increments and probability of occurrence.

If an option has several possible exercise dates, it is valued using the binomial model and publicly accessible market data.

Credit derivatives are valued using the hazard rate model based on the latest credit spread.

Summary of principal valuation models by derivative product group:

Product group	Principal valuation model
Interest rate swaps	Present value method
Forward rate agreements	Present value method
Interest rate options	Black 76, displaced diffusion
Forward exchange transactions	Present value method
Currency swaps/cross-currency swaps	Present value method
Foreign exchange options	Black 76, Trinomial tree (Cox-Ross-Rubinstein)
Equity/index options	Black-Scholes, Roll-Geske-Whaley
Commodity caps/floors	Vorst
Credit derivatives	Hazard Rate Modell

Securities lending transactions

Secured securities lending transactions are treated on the balance sheet as genuine repurchase agreements. Loaned securities remain part of the securities portfolio and are recognised and measured according to whether they have been allocated to the investment portfolio, trading portfolio or liquidity reserve. Borrowed securities are not recognised. Cash pledged as collateral for securities lending transactions is recognised as a receivable (depending on the counterparty, either as due from banks or due from customers) and received collateral as a liability (depending on the counterparty, either as due to banks or due to customers). Precious metal lending transactions (except for gold) are recognised and measured in the same way.

Derivative financial instruments

Derivative financial instruments (mainly forward transactions, swaps, options, credit derivatives) are allocated to a non-trading or trading portfolio depending on their intended use. As executory contracts, they are not disclosed in the balance sheet if their intended use is as a hedging transaction. Option premiums paid or received, premiums that are not yet due for credit derivatives, and offsetting payments for price changes from total return swaps over the term are reported under the other assets or other liabilities items.

Upfront payments for interest rate and (cross) currency swaps (non-trading portfolio) are recognised under the pre-paid expenses and deferred income items. In accordance with the IDW opinion on accounting standards IDW RS BFA 1, IDW RS BFA 5 and IDW RS BFA 6, realised income and gains or losses on derivatives in the non-trading portfolio are recognised under the items other operating income and other operating expenses in the income statement. Realised losses on interest rate derivatives in the non-trading portfolio are recognised under the interest expenses item.

Derivative financial instruments in the trading portfolio are measured at fair value less a risk discount and recognised in the respective trading portfolio item (under assets if the fair value is positive and under liabilities if the fair value is negative). If the requirements for netting are met, derivative financial instruments in the trading portfolio are recognised at the net value of their market price and any variation margin paid or received. If the valuation results in a negative figure for stand-alone derivative financial instruments in the non-trading portfolio that are not part of a valuation unit, then provisions are made for expected losses from executory contracts.

If interest rate and currency risks from the non-trading book are transferred to the trading book, internal deals are recognised in the same way as external deals in accordance with the arm's length principle.

Structured products

Structured products in the trading portfolio and the liquidity reserve are treated as financial instruments which are not composed of separate parts as they are measured at fair value less a risk discount (trading portfolio) or at the strict principle of lower of cost or market value (liquidity reserve). Structured liabilities are recognised at the settlement value.

Valuation units

BayernLB utilises valuation units (underlying transactions and their related hedges) in accordance with section 254 HGB. Micro fair-value valuation units are predominantly used. They are therefore reported in accordance with the risk management approach of the corresponding non-trading books. Interest rate risk is normally hedged. If the product is structured, other market risks (equity, currency and commodity risks) may also be hedged. In a few exceptional cases, credit risk may also be hedged. Fair value valuation units are also created on portfolios for emission rights.

In accordance with the Risk Strategy, micro valuation units are normally created on inception and end when the underlying and hedging transactions mature. The total volumes of the transactions are hedged in each case. Underlying transactions in a valuation unit may be assets, liabilities or derivative financial instruments. The critical term match method is used to test prospective and retrospective effectiveness in perfect 1:1 hedges. Their level of ineffectiveness is calculated using the cumulative changes in the value of the underlying and hedging transactions. If the net value is negative, a provision for expected losses is recognised. For imperfect hedges, effectiveness is tested using the dollar-offset method and variance reduction analysis. As with perfect hedges, net negative amounts are shown as provisions for expected losses. The effective portions of the valuation units shown are recognised in accordance with the freeze method. These are recognised in the income statement in the same way as the gains or losses on measurement of the underlying transactions.

In line with the Risk Strategy, portfolio valuation units on emission rights are created on inception. The total volumes of the transactions are hedged in each case. Underlying transactions in a valuation unit may be assets or derivative financial instruments. Their prospective effectiveness is verified using correlation analysis. Their level of ineffectiveness is calculated using the cumulative changes in the value of the underlying and hedging transactions. The effective portions of the valuation units shown are recognised in accordance with the book-through method. Consequently assets and derivative financial instruments are recognised under other the other assets and other liabilities items. Reporting in the income statement is under the items other operating income or other operating expenses.

Loss-free measurement of the banking book

IDW RS BFA 3 governs specific issues relating to the loss-free measurement of the banking book under HGB. Due to the nature of banks' business in the banking book, it is not possible to directly match individual financial instruments with each other on a regular basis. The banking book is managed as a whole. For all interest-bearing on- and off-balance sheet financial instruments in the banking book, the principle of prudence is observed by making a provision for any surplus of liabilities in accordance with section 249 HGB (provision for expected losses). BayernLB calculates potential surpluses of liabilities using the net present value method. Besides the net present values and carrying amounts of interest-bearing financial instruments in the non-trading portfolio, the calculation to determine whether a provision for expected losses must be made under section 249 HGB takes account of administrative and standard risk costs. Administrative costs are calculated based on internal cost controlling. This takes into account the process costs for transactions in the portfolio as at the reporting date plus a surcharge for overheads and inflation. Standard risk costs are calculated using the same method as for risk costs. It is based on the expected losses over several years. BayernLB had no surplus liabilities as at the reporting date. No provision for expected losses from loss-free measurement was required.

Participations and shares in affiliated companies

Participations and shares in affiliated companies are valued at cost in accordance with the rules for investment assets or – if an impairment is expected to be permanent – at the lower of cost or market value as at the reporting date, taking account of the IDW's position on accounting standard IDW RS HFA 10. Where there is no further reason for impairment, a reversal is made.

Intangible assets and tangible assets

Acquired intangible assets are measured at cost, less amortisation and, if required, impairments.

Internally generated intangible assets are capitalised in accordance with the option under section 248 para. 2 HGB and valued at cost, less amortisation and, if required, impairments.

The tangible assets are measured at cost, less depreciation and, if required, impairments. After large-scale renovation work, buildings are measured using the component method. Separate wear and tear of individual components is recognised as a partial disposal and their replacement as a partial addition. They are depreciated separately over their useful life. Low-value items are fully written off in the year acquired. Interest costs are not capitalised.

The period of depreciation is equivalent to their economic life.

Deferred taxes

In accordance with section 274 HGB, deferred taxes are calculated on the temporary differences between the accounting value and the tax value of assets, liabilities and pre-paid and deferred items that give rise to a future tax liability or benefit, and on tax loss carryforwards. BayernLB, the parent company of the tax group, also recognises the temporary differences of its subsidiaries. Deferred taxes are computed in Germany (for the tax group) at the combined corporation tax and municipal trade tax rate (including the solidarity surcharge) of 31.95 percent, except for deferred taxes on participations in partnerships, which are computed at the corporation tax rate (including the solidarity surcharge) of 15.83 percent. Deferred taxes on municipal trade tax loss carryforwards are computed at an average municipal trade tax rate of 16.12 percent. For BayernLB’s foreign branches, deferred taxes are measured on the basis of the local tax rates applicable in the country concerned; the range is between 17.00 percent and 31.95 percent.

A deferred tax liability is recognised if a tax liability remains after netting. As permitted under section 274 para. 1 sentence 2 HGB, BayernLB has elected not to recognise any deferred taxes if a tax benefit is left after netting.

Provisions

Provisions for pensions and similar obligations for direct retirement benefits to employees are valued using the projected unit credit method. The method uses actuarial input based on biometric assumptions (Richttafeln 2005 G (actuarial tables) by Klaus Heubeck) and expected future salary and pension increases.

The interest rate for calculating the present value of pensions and similar obligations is the average market interest rate published by the Deutsche Bundesbank resulting from an assumed residual term of 15 years (section 253 para. 2 sentence 2 HGB). The fiscal net present value as calculated in accordance with section 6a EStG is exceeded.

Pursuant to section 253 para. 2 sentence 1 HGB, pension provisions were discounted using the respective average market rate for the past ten financial years. The discounting gave rise as at 31 December 2017 to a difference of EUR 292 million (FY 2016: EUR 250 million) on the amount that would have been calculated if the seven-year discount rate (2.80 percent) had been used for discounting; in accordance with section 253 para. 6 sentence 2 HGB this amount is potentially not available for distribution. Provisions for medical obligations and death benefit obligations arising on existing retirement benefits were discounted using the average market rates of the past seven financial years.

in %	2017	2016
Actuarial interest rate for pension obligations	3.68	4.01
Actuarial interest rate for medical obligations and death benefit obligations[1]	2.80	3.23
Changes in salary	2.25	2.50
Adjustments to pensions[2]	2.00	2.00
Changes in medical costs	5.25	5.00

1 Provisions for death benefit obligations were reported for the first time in the 2017 annual financial statements. The previous year was not adjusted.

2 In addition, eligible social insurance pensions were calculated to have increased by 2.25 percent.

Besides the pension system, for which provisions for pensions and similar obligations are made, BayernLB has two legally independent support funds for indirect retirement benefits payable to employees within Germany. Where pension benefits are provided through an indirect financing structure, BayernLB still has subordinate liability under the German Act to Improve Occupational Pensions (Gesetz zur Verbesserung der betrieblichen Altersversorgung (BetrAVG)). The Bank regularly contributes to the fund assets of these support funds where permitted under tax law. In accordance with Art. 28 para. 1 sentence 2 EGHGB, pension provisions are not made for indirect retirement benefits. As at 31 December 2017, there was a shortfall of EUR 255 million (FY 2016: EUR 247 million). Reinsurance concluded by BayernLB to fund these retirement benefit obligations offset this amount by EUR 222 million (FY 2016: EUR 219 million).

Other provisions are measured at the settlement amount dictated by prudent business judgement. The provisions are calculated on the basis of future price and cost increases. Other provisions are determined on a full-cost basis. Risks for loss events and processes that have not been concluded are recognised only if the probability of occurrence is 50 percent or more.

Provisions with a residual term of more than one year are discounted at an interest rate published by the Deutsche Bundesbank. The average maturities-matched market interest rate of the past seven financial years is used as an interest rate.

Tax provisions are measured at the settlement amount dictated by prudent business judgement. Obligations are reported at their settlement amount.

Currency translation

Currencies are translated in accordance with the principles of sections 256a and 340h HGB and the IDW's position on accounting standard IDW RS BFA 4. Assets, liabilities and spot transactions denominated in foreign currencies that are not yet settled are translated at the mid-market spot rate on the reporting date. In accordance with the less strict principle of the lower of cost or market value, assets denominated in foreign currencies that are treated as fixed assets and not hedged in the same currency are recognised at cost. Assets and liabilities on the balance sheet and executory contracts denominated in a foreign currency are treated in accordance with section 340h HGB if they are specifically hedged. Currency risks arising in non-trading portfolios are transferred to the trading books. Income and expenses from currency translation are recognised under the net income or net expenses of the trading portfolio item.

Notes to the balance sheet

Unless otherwise stated, information in the tables includes accrued interest.

Assets

Due from banks

EUR million	2017	2016
Due from banks	**35,004**	**26,178**
This item includes:		
Other receivables with a residual maturity of		
• up to three months (including accrued interest)	4,179	4,772
• over three months up to one year (including swap interest)	4,269	5,019
• over one year up to five years	5,710	6,601
• over five years	8,849	7,736
Due from affiliated companies	**1,164**	**1,083**
Due from companies in which participations are held	**103**	**31**
Due from related savings banks	**15,137**	**14,058**
Subordinated receivables	**559**	**265**

Due from customers

EUR million	2017	2016
Due from customers	**67,337**	**68,811**
This item includes:		
Receivables with a residual maturity of		
• up to three months (including accrued interest)	8,727	7,685
• over three months up to one year (including swap interest)	6,072	8,100
• over one year up to five years	25,275	24,459
• over five years	26,151	27,185
Receivables without a fixed date of maturity	**1,111**	**1,382**
Due from affiliated companies	**47**	**29**
Due from companies in which participations are held	**160**	**73**
Subordinated receivables	**195**	**90**

Bonds and other fixed-income securities

EUR million	2017	2016
Bonds and other fixed-income securities	**16,526**	**20,661**
This item includes:		
Amounts falling due in the following year (including accrued interest)	**1,803**	**3,338**
Securitised receivables from affiliated companies	**–**	**455**
Securitised receivables from companies in which participations are held	**–**	**–**
Subordinated securities	**5**	**468**
Marketable securities, of which		
• listed	16,216	19,742
• unlisted	310	919

In the investment portfolio as a whole, bonds and other fixed-income securities were recognised on the basis of the less strict principle of lower of cost or market value at a carrying amount of EUR 11,387 million (FY 2016: EUR 14,558 million) and had a fair value of EUR 11,378 million (FY 2016: EUR 14,542 million). No writedown is made if the Bank does not consider the current fluctuations in value to be long term and assumes that the securities will be repaid in full when they mature.

Equities and other non-fixed income securities

EUR million	2017	2016
Equities and other non-fixed income securities	**95**	**40**
This item includes:		
Marketable securities, of which		
• listed	–	–
• unlisted	8	8

On the reporting date, as in the previous year, no equities or other non-fixed income securities were recognised on the basis of the less strict principle of lower of cost or market value.

Trading portfolio

EUR million	2017	2016
Trading portfolio	**7,088**	**11,097**
This item includes:		
Positive fair values of derivative financial instruments	**3,538**	**6,544**
Receivables	**1,306**	**1,545**
Bonds and other fixed-income securities	**1,541**	**2,510**
Equities and other non-fixed income securities	**361**	**342**
Other assets	**353**	**172**
Risk discount for the whole trading portfolio	**–12**	**–17**
Subordinated securities	**6**	**2**

Participations

As at the reporting date, the carrying amount of participations was EUR 245 million (FY 2016: EUR 233 million). As in the previous year, the portfolio was not encumbered by any unrecognised impairments. The participations did not include any stock market-listed securities.

Shares in affiliated companies

EUR million	2017	2016
Shares in affiliated companies	**2,289**	**2,295**
This item includes:		
Marketable securities, of which		
• listed	–	–
• unlisted	2,167	2,167

Assets held in trust

EUR million	2017	2016
Assets held in trust	**4,879**	**4,946**
This item mainly includes housing loans granted by Bayerische Landesbodenkreditanstalt and breaks down as follows:		
Due from banks	23	32
Due from customers	4,855	4,914

Intangible assets and tangible assets

Research and development costs of EUR 15 million (FY 2016: EUR 8 million) were reported under intangible assets. This included EUR 5 million in development costs (FY 2016: EUR 3 million) resulting from internally developed intangible assets categorised as fixed assets, namely internally developed software.

Land and buildings used for own operations in the amount of EUR 266 million (FY 2016: EUR 272 million) were reported in tangible assets.

Purchase/manufacturing costs

EUR million	1 Jan 2017	Additions	Disposals	Transfers	31 Dec 2017
Intangible assets[1]	288	10	–10	–	**288**
Internally generated industrial property rights	144	5	–	–	**149**
Purchased licences, industrial property rights	144	6	–10	–	**139**
Tangible assets	478	1	–1	25	**503**
Land and buildings	401	1	–	25	**427**
Furniture and office equipment	77	–	–1	–	**76**

Amortisation/depreciation and carrying amounts

EUR million	1 Jan 2017	Additions[2]	Disposals	Transfers	31 Dec 2017	Carrying amount 31 Dec 2017	Carrying amount 31 Dec 2016
Intangible assets[1]	−210	−16	10	–	−215	**73**	**78**
Internally generated industrial property rights	−88	−8	–	–	−97	52	56
Purchased licences, industrial property rights	−122	−7	10	–	−118	21	22
Tangible assets	−144	−11	1	−25	−179	**324**	**334**
Land and buildings	−84	−8	–	−25	−117	309	317
Furniture and office equipment	−59	−3	1	–	−61	15	17

Changes in securities, participations and shares in affiliated companies

EUR million	1 Jan 2017	Change[3]	31 Dec 2017
Bonds, notes, other fixed-income securities	15,254	−3,349	**11,905**
Equities, other non-fixed income securities	–	–	**–**
Participations	233	12	**245**
Shares in affiliated companies	2,295	−7	**2,289**

1 Additions include capitalised development costs plus licence costs.
2 Amortisation/depreciation and writedowns.
3 BayernLB elected to use the aggregation option under section 34 para. 3 RechKredV.

Other assets

EUR million	2017	2016
Other assets	**2,013**	**1,562**
This item includes: Emissions certificates	1,256	697
Claims from reinsurance	222	219
Receivables from participations	15	287
Claims on tax authorities	12	48

The increase in respect of emissions certificates is due to increased market activity and higher prices. The Bank's position is closed through forward transactions. The fall in receivables from participations was mainly the result of one company within the Group reinvesting to strengthen its capital base rather than distributing its profits, as it had done in the previous year.

Pre-paid expenses

EUR million	2017	2016
Pre-paid expenses	**665**	**683**
This item includes:		
Upfront payments from swaps	390	422
Premium on receivables	178	148
Discount on liabilities	75	89
Cash settlement payments	13	15

Genuine sale and repurchase agreements

EUR million	2017	2016
Carrying amounts of assets transferred under sale and repurchase agreements	404	249

Assets denominated in foreign currencies

EUR million	2017	2016
Total amount of assets denominated in foreign currencies	22,038	23,919

Assets held as cover

EUR million	2017	2016
Mortgage Pfandbriefs and Landesbodenbriefs	**2,851**	**4,065**
Cover assets contained in:		
• Due from banks	–	8
• Due from customers	5,888	6,863
• Bonds and other fixed-income securities	451	486
• Additional cover	–	–
Excess cover	**3,488**	**3,293**
Public Pfandbriefs	**16,620**	**16,231**
Cover assets contained in:		
• Due from banks	150	257
• Due from customers	21,948	22,621
• Bonds and other fixed-income securities	1,020	598
• Additional cover	304	393
Excess cover	**6,802**	**7,638**

Units in funds where more than 10 percent of the fund units are held

Fund name	Fair value EUR million	Carrying amount EUR million	Difference between fair value and carrying amount EUR million	Distribution of earnings EUR million	Daily redemption possible
Bond funds					
• BayernInvest Euro Covered Bonds Fonds	15	15	–	–	yes
• BayernInvest Euro Corporates Non-Fin Fonds	15	15	–	–	yes
• BayernInvest Renten Europa-Fonds	11	8	2	1	yes

Liabilities

Due to banks

EUR million	2017	2016
Due to banks	**41,172**	**43,292**
This item includes:		
Term liabilities with a residual maturity of		
• up to three months (including accrued interest)	4,971	5,199
• over three months up to one year (including swap interest)	5,115	5,900
• over one year up to five years	9,658	11,247
• over five years	15,099	14,687
Due to affiliated companies	**1,220**	**3,191**
Due to companies in which participations are held	**15**	**333**
Due to related savings banks	**4,350**	**4,321**

Due to customers

EUR million	2017	2016
Due to customers	**36,922**	**32,029**
This item includes:		
Other term liabilities with a residual maturity of		
• up to three months (including accrued interest)	6,325	4,652
• over three months up to one year (including swap interest)	4,684	3,701
• over one year up to five years	5,185	6,010
• over five years	10,730	10,883
Due to affiliated companies	**123**	**107**
Due to companies in which participations are held	**33**	**115**

Securitised liabilities

EUR million	2017	2016
Securitised liabilities	**36,720**	**34,737**
This item includes:		
Bonds and notes issued		
• amounts falling due in the following year	4,915	5,296
Other securitised liabilities with a residual maturity of		
• up to three months (including accrued interest)	6,266	3,407
• over three months up to one year	523	161
• over one year up to five years	–	–
• over five years	–	–
Due to affiliated companies	**–**	**–**
Due to companies in which participations are held	**10**	**8**

Trading portfolio

EUR million	2017	2016
Trading portfolio	**3,517**	**4,923**
This item includes:		
Negative fair values of derivative financial instruments	**2,943**	**4,340**
Liabilities	**573**	**583**

Liabilities held in trust

EUR million	2017	2016
Liabilities held in trust	**4,879**	**4,946**
This item breaks down as follows:		
Due to banks	1	1
Due to customers	4,878	4,945

Other liabilities

EUR million	2017	2016
Other liabilities	**649**	**609**
This item includes:		
Forward transactions on emissions certificates	325	191
Buy-in obligation resulting from the sale of securities borrowed	154	113
Interest payable on profit participation certificates and silent partner contributions	76	202
Offsetting item for foreign currency translation	–	16

Deferred income

EUR million	2017	2016
Deferred income	**702**	**809**
This item includes:		
Upfront payments from swaps	574	699
Premium on liabilities	107	83
Discount on receivables	5	8

Subordinated liabilities

EUR million	2017	2016
Subordinated liabilities	**1,347**	**3,264**
This item includes:		
Subordinated liabilities to affiliated companies	**–**	**836**

In the reporting year, interest expenses on subordinated liabilities were EUR 137 million (FY 2016: EUR 179 million).

If BayernLB goes insolvent or is liquidated, the subordinated liabilities cannot contractually be repaid until the claims of all senior creditors have been settled. Creditors have no right to demand early repayment. Under CRR not all subordinated liabilities can be reported under Tier 2 capital as original instruments. However, under the transitional rule, these securities may be offset within Tier 2 capital for a limited period and subject to limits on amounts.

There are no contractual provisions for a conversion into equity or another debt instrument.

The following borrowings exceed 10 percent of the total subordinated liabilities:

	Volume in EUR million	Interest rate	Maturity
USD Schuldschein note loan	334	6.10%	28/04/2031

Liabilities denominated in foreign currencies

EUR million	2017	2016
Total amount of liabilities denominated in foreign currencies	21,495	18,199

Contingent liabilities and other liabilities

EUR million	2017	2016
Contingent liabilities	**10,052**	**9,891**
This item includes:		
Liabilities from guarantees and indemnity agreements		
• Letters of credit	394	602
• Guarantees	780	933
• Other guarantees and indemnities	8,865	8,335

Potential liabilities from sureties, guarantees, letters of credit, other indemnities and other liabilities assumed by the Bank in the course of its ordinary business with customers are recognised under contingent liabilities. There is also a small volume of guarantees to affiliated companies.

EUR million	2017	2016
Other liabilities	**22,265**	**21,393**
This item includes:		
Irrevocable loan commitments to		
• Banks	1,718	1,947
• Customers	20,546	19,446

Other liabilities result from irrevocable loan commitments, mainly granted to customers in the course of ordinary business.

Irrevocable loan commitments to affiliated companies made as part of the Group-wide management system were not significant. The unutilised portion of lines of credit granted to two special purpose vehicles in connection with ABS customer transactions amounted to EUR 1,811 million (FY 2016: EUR 1,163 million). The commitments ensure that each of the special purpose vehicles can gain access to funding if they are unable to place securitised instruments on the market as planned.

No individual off-balance sheet amounts are material in relation to overall activities.

The risks from drawdowns for contingent liabilities and other liabilities are assessed on the basis of the creditworthiness of the principal or borrower. Provisions are made if creditworthiness deteriorates to the extent that it is no longer expected that the drawdown will be repaid in full or in part. Information on the credit risk management process can be found in the risk report.

Assignment of collateral for the Bank's own liabilities

In addition to the assets transferred under sale and repurchase agreements and receivables used as cover pools for issued Pfandbriefs, assets have been assigned as collateral in the case of the following own liabilities in the amounts shown below:

EUR million	2017	2016
Due to banks	16,421	15,058
Due to customers	1,620	1,642
Contingent liabilities	–	–

Collateral for own liabilities primarily relates to transferred receivables for pass-through loans to banks of EUR 16,418 million (FY 2016: EUR 15,048 million), collateral for issued municipal guaranteed investment contracts of EUR 1,604 million (FY 2016: EUR 1,609 million) and cash pledged as collateral for repurchase agreements of EUR 20 million (FY 2016: EUR 43 million).

BayernLB also pledged cash collateral of EUR 23 million (FY 2016: EUR 17 million) for the utilisation of the irrevocable payment obligation in connection with the bank levy and transferred securities of EUR 12 million (FY 2016: EUR 12 million) in connection with the deposit guarantee scheme.

Valuation units

Countermovements in values and cash flows were almost fully balanced on the reporting date and should continue to offset each other. When the underlying and hedging transactions mature and the valuation units therefore expire, the changes in value arising from the hedged risks will have completely offset each other.

EUR million	Hedged amount	
	2017	**2016**
Carrying amount of underlying transactions in micro valuation units	**6,024**	**7,654**
• Assets	1,799	1,917
• Liabilities	4,159	5,768
• Derivative financial instruments	66	−31
Carrying amount of underlying transactions in portfolio valuation units	**1,347**	**781**
• Assets	1,256	697
• Forward contracts	91	84

Notes to the income statement

Interest income and interest expenses

Interest income included EUR 71 million (FY 2016: EUR 9 million) of interest on tax receivables and interest expenses included EUR 42 million (FY 2016: EUR 13 million) of interest on tax liabilities.

Other operating income and other operating expenses

In the reporting year, the Bank produced other operating income of EUR 338 million (FY 2016: EUR 420 million) and other operating expenses of EUR 359 million (FY 2016: EUR 242 million), resulting in a net other operating expense for the year of EUR 21 million (FY 2016: income of EUR 178 million).

The Bank disclosed EUR 132 million (FY 2016: EUR 104 million) of gains on emissions certificates under other operating income and EUR 152 million (FY 2016: EUR 89 million) of losses under other operating expenses.

Releases of other provisions gave rise to other operating income of EUR 127 million (FY 2016: EUR 245 million, with EUR 133 million due to the first-time application of the revaluation due to section 253 para. 2 HGB).

Capitalisation of interest on provisions resulted in other operating expenses of EUR 90 million (FY 2016: EUR 98 million).

The Bank reported EUR 45 million (FY 2016: EUR 6 million) of gains arising on the purchase and sale of receivables in other operating income and EUR 51 million (FY 2016: EUR 4 million) of losses in other operating expenses.

The Bank reported EUR 6 million (FY 2016: EUR 13 million) of gains arising on standalone derivatives in the non-trading portfolio in other operating income and EUR 0 million (FY 2016: EUR 9 million) of losses in other operating expenses.

Amortisation, depreciation and writedowns on intangible assets and tangible assets

This item contained no writedowns of internally generated intangible assets (FY 2016: EUR 12 million).

Amortisation, depreciation and writedowns on receivables and certain securities and additions to provisions in the credit business

This item includes a gain from recoveries on written-off receivables of EUR 87 million (FY 2016: EUR 61 million).

Amortisation, depreciation and writedowns on participations, shares in affiliated companies and securities classified as fixed assets

This item included a redemption gain following the calling of Capital LLC’s USD hybrid bond valued at EUR 314 million.

Extraordinary income and extraordinary expenses

Extraordinary income and extraordinary expenses include solely income and expenses from restructuring measures.

Taxes on income and earnings

Corporation tax, municipal trade tax, solidarity surcharge and income taxes in other countries were reported as income tax expenses.

Distributions on profit participation certificates and silent partner contributions

All liabilities on profit participation certificates and silent partner contributions were paid from net income for financial year 2017 in accordance with the terms of the contract. A full distribution of EUR 23 million (FY 2016: EUR 23 million) and EUR 53 million (FY 2016: EUR 179 million) was paid on the profit participation certificates and silent partner contributions respectively.

Amounts not available for distribution

Capitalisation of internally generated intangible assets produced in house categorised as fixed assets produced an amount that may not be distributed of EUR 52 million (FY 2016: EUR 56 million). The difference that may not be distributed arising between provisions for pension obligations recognised according to the corresponding average market rate for the past ten years and for the past seven years was EUR 292 million (FY 2016: EUR 250 million). These amounts not available for distribution are matched by sufficient available reserves.

Geographical markets

The sum of earnings from

- interest income
- current income from equities and other non-fixed income securities, participations and shares in affiliated companies
- commission income
- net income of the trading portfolio
- other operating income

is broken down by geographical market as follows:

EUR million	2017	2016
Germany	2,782	3,045
Europe (ex Germany)	75	138
America	218	202

Derivatives transactions

The tables below show open external interest rate, foreign currency and other forward transactions and credit derivatives as at the reporting date. The transactions are primarily for hedging changes in interest rates, exchange rates or market prices and conducting trades for customers. They also include derivatives that form part of a hedge.

Derivatives transactions – volumes

	Nominal value		Positive market value[1]	Negative market value[1]
EUR million	**2017**	**2016**	**2017**	**2017**
Interest rate risks				
• Interest rate swaps	655,575	645,836	19,198	17,965
• FRAs	205,270	223,702	28	27
• Interest rate options	17,504	20,629	532	796
– *call options*	*6,633*	*6,871*	*453*	*48*
– *put options*	*10,871*	*13,758*	*79*	*748*
• Caps, floors	10,416	10,335	131	57
• Exchange-traded contracts	16,628	11,285	–	–
• Other interest-based forward transactions	737	1,321	5	38
Total interest rate risks	**906,130**	**913,108**	**19,894**	**18,883**
Currency risks				
• Forward exchange transactions	89,862	90,849	1,310	1,231
• Currency/cross-currency swaps	20,520	28,465	761	591
• Foreign exchange options	2,711	2,858	68	45
– *call options*	*1,548*	*1,533*	*66*	*1*
– *put options*	*1,163*	*1,325*	*2*	*44*
• Other currency-based forward transactions	588	336	2	7
Total currency risks	**113,681**	**122,508**	**2,142**	**1,875**
Equity and other price risks				
• Equity forward transactions	307	221	–	34
• Equity/index options	403	425	5	1
– *call options*	*365*	*387*	*5*	*–*
– *put options*	*38*	*38*	*–*	*1*
• Exchange-traded contracts	1,100	634	–	16
• Other forward transactions[2]	3,721	3,839	286	430
Total equity and other price risks	**5,531**	**5,120**	**292**	**480**
Credit derivative risks				
• Protection buyer	175	804	–	4
• Protection seller	–	160	–	–
Total credit derivative risks	**175**	**964**	**–**	**4**
Total	**1,025,517**	**1,041,700**	**22,327**	**21,241**

1 *Calculation of market values, see Accounting policies: Fair value and Derivative financial instruments.*
2 *Exclusively energy and commodity-related transactions.*

Derivatives transactions – maturities

	Nominal value							
	Interest rate risks		Currency risks		Equity and other price risks		Credit derivative risks	
EUR million	2017	2016	2017	2016	2017	2016	2017	2016
Residual maturities								
• up to three months	43,102	35,087	52,109	54,851	1,869	1,468	–	50
• up to one year	236,351	254,858	30,856	31,336	1,431	1,268	–	221
• up to five years	350,358	333,208	21,589	25,009	2,050	2,066	135	650
• more than five years	276,320	289,955	9,127	11,312	181	318	40	43
Total	**906,130**	**913,108**	**113,681**	**122,508**	**5,531**	**5,120**	**175**	**964**

Derivatives transactions – counterparties

	Nominal value		Positive market value[1]	Negative market value[1]
EUR million	2017	2016	2017	2017
OECD banks	279,861	303,792	8,556	7,561
Non-OECD banks	357	661	3	2
Public-sector entities within the OECD	10,205	13,313	642	403
Other counterparties[2]	735,094	723,934	13,126	13,275
Total	**1,025,517**	**1,041,700**	**22,327**	**21,241**

Derivatives transactions – trading portfolios

	Nominal value		Positive market value[1]	Negative market value[1]
EUR million	2017	2016	2017	2017
Interest rate derivatives	690,115	709,247	15,024	14,281
Currency derivatives	106,504	111,088	1,679	1,791
Equity derivatives	3,507	3,433	188	284
Credit derivatives	135	872	–	4
Total	**800,261**	**824,640**	**16,891**	**16,360**

Derivatives transactions – non-trading portfolios

	Nominal value		Positive market value[1]	Negative market value[1]
EUR million	2017	2016	2017	2017
Interest rate derivatives	216,015	203,861	4,869	4,602
Currency derivatives	7,177	11,420	463	83
Equity derivatives	2,024	1,687	105	196
Credit derivatives	40	92	–	–
Total	**225,256**	**217,060**	**5,437**	**4,881**

1 Calculation of market values, see Accounting policies: Fair value and Derivative financial instruments.
2 Including exchange-traded contracts.

Notes pursuant to section 35 para. 1 no. 7 RechKredV in connection with section 28 of the Pfandbrief Act

Outstanding Pfandbriefs and cover pools

EUR million	Nominal value		Present value		Risk-related present value	
	2017	2016	2017	2016	2017	2016
Mortgage Pfandbriefs	**2,851**	**4,065**	**2,977**	**4,295**	**2,936**	**4,195**
Cover pools [1]	6,339	7,357	6,756	7,920	6,533	7,680
Excess cover	**3,488**	**3,293**	**3,779**	**3,626**	**3,597**	**3,485**
Public Pfandbriefs	**16,620**	**16,231**	**18,149**	**18,175**	**17,115**	**17,090**
Cover pools [1,2]	23,162	23,567	25,990	26,430	24,209	24,668
Excess cover	**6,542**	**7,335**	**7,841**	**8,255**	**7,094**	**7,578**

1 Including additional cover assets pursuant to sections 19 para. 1 and 20 para. 2 PfandBG.
2 Including discount for Bayerische Landesbodenkreditanstalt's receivables at below-market interest rates (BayernLabo).

Maturity profile of outstanding Pfandbriefs and interest rate lock-in periods of cover pools

EUR million	Mortgage Pfandbriefs		Cover pools [1]		Public Pfandbriefs		Cover pools [1,2]	
	2017	2016	2017	2016	2017	2016	2017	2016
Residual maturities and interest rate lock-in periods								
• up to six months	278	286	507	617	1,599	566	1,265	1,980
• over six months up to one year	607	862	335	1,039	839	1,310	1,011	1,194
• over one year up to eighteen months	327	278	118	347	434	1,526	1,234	1,378
• over eighteen months up to two years	411	635	124	384	696	676	730	1,126
• over two years up to three years	179	782	1,027	727	685	1,070	2,673	1,940
• over three years up to four years	61	179	726	1,148	1,931	681	1,919	2,133
• over four years up to five years	658	64	1,111	685	1,640	1,355	1,577	1,752
• over five years up to ten years	325	973	2,167	2,202	5,861	6,716	6,719	6,645
• over ten years	7	5	224	209	2,935	2,331	6,033	5,418
Total	**2,851**	**4,065**	**6,339**	**7,357**	**16,620**	**16,231**	**23,162**	**23,567**

1 Including additional cover assets pursuant to sections 19 para. 1 and 20 para. 2 PfandBG.
2 Including discount for Bayerische Landesbodenkreditanstalt's receivables at below-market interest rates (BayernLabo).

Net present value of mortgage Pfandbriefs and public Pfandbriefs by foreign currency

	Mortgage Pfandbriefs		Public Pfandbriefs	
EUR million	2017	2016	2017	2016
CAD	–	–	19	74
CHF	86	105	–171	–1
GBP	121	–33	332	438
SEK	–	46	–	–
USD	–204	13	–172	–47

Composition of mortgage Pfandbriefs and public Pfandbriefs by percentage

	Mortgage Pfandbriefs		Public Pfandbriefs	
in %	2017	2016	2017	2016
Share of fixed-income cover pool	68	67	93	93
Share of fixed-income Pfandbriefs	88	84	92	94

Composition of other cover assets used to cover Pfandbriefs

EUR million	2017	2016
Cover assets in accordance with		
• section 19 para. 1 no. 3 of the Pfandbrief Act (PfandBG)	451	486
• section 20 para. 2 no. 2 of the Pfandbrief Act (PfandBG)	304	393
Total	**755**	**879**

The country of domicile of the borrowers of the other cover assets is Germany. As at the reporting date the other cover assets did not comprise covered bonds as defined by Art. 129 Regulation (EU) No 575/2013.

Receivables used to cover mortgage Pfandbriefs by size

	Mortgages serving as cover	
EUR million	2017	2016
Up to EUR 300,000	4	4
Over EUR 300,000 up to EUR 1 million	31	38
Over EUR 1 million up to EUR 10 million	1,127	1,362
More than EUR 10 million	4,726	5,467
Additional cover	451	486
Total	**6,339**	**7,357**

Receivables used to cover public Pfandbriefs by size

EUR million	Cover assets 2017	Cover assets 2016
Up to EUR 10 million	3,465	3,418
Over EUR 10 million up to EUR 100 million	5,670	6,227
More than EUR 100 million	13,723	13,529
Total	**22,858**	**23,174**

Receivables used to cover mortgage Pfandbriefs by age and average loan to value

		2017	2016
Section 28 para. 1 no. 11 of the Pfandbrief Act (PfandBG) – volume-weighted average age of receivables (seasoning)	in years	5	5
Section 28 para. 2 no. 3 of the Pfandbrief Act (PfandBG) – average-weighted loan to value	in %	54	53

Receivables used to cover mortgage Pfandbriefs by country where the real estate collateral is located and by type of use

	Mortgages serving as cover			
	Commercial		Residential	
EUR million	2017	2016	2017	2016
Germany	**3,617**	**4,440**	**912**	**1,065**
• flats	–	–	–	8
• single-family homes	–	–	4	7
• multi-family homes	83	–	885	1,019
• office buildings	1,564	1,848	–	–
• retail buildings	1,178	1,244	–	–
• industrial buildings	11	12	–	–
• other commercial buildings	693	718	–	–
• unfinished new buildings not yet generating income	76	104	–	4
• building plots	12	28	23	28
• additional cover	–	486	–	–
Austria	**65**	**95**	**–**	**–**
• office buildings	–	15	–	–
• retail buildings	46	61	–	–
• other commercial buildings	19	19	–	–
Belgium	**36**	**26**	**7**	**–**
• office buildings	36	26	–	–
• building plots	–	–	7	–
Czech Republic	**50**	**188**	**–**	**–**
• office buildings	40	63	–	–
• retail buildings	10	125	–	–

	Mortgages serving as cover			
	Commercial		Residential	
EUR million	2017	2016	2017	2016
France	**325**	**320**	**–**	**–**
• office buildings	281	276	–	–
• retail buildings	44	44	–	–
Italy	**303**	**278**	**–**	**–**
• office buildings	151	172	–	–
• retail buildings	68	106	–	–
• building funds	–	–	–	–
• unfinished new buildings not yet generating income	85	–	–	–
Netherlands	**296**	**300**	**–**	**–**
• office buildings	270	232	–	–
• retail buildings	12	49	–	–
• other commercial buildings	15	19	–	–
Poland	**105**	**67**	**–**	**–**
• office buildings	84	46	–	–
• retail buildings	20	21	–	–
Slovakia	**3**	**3**	**–**	**–**
• retail buildings	3	3	–	–
Spain	**52**	**54**	**–**	**–**
• retail buildings	52	54	–	–
Sweden	**–**	**46**	**–**	**–**
• office buildings	–	46	–	–
Switzerland	**19**	**20**	**–**	**–**
• retail buildings	19	20	–	–
United Kingdom	**142**	**161**	**–**	**–**
• office buildings	142	118	–	–
• retail buildings	–	43	–	–
USA	**38**	**293**	**–**	**–**
• office buildings	38	293	–	–
Total	**5,051**	**6,292**	**919**	**1,065**

Total amount of mortgage receivables overdue for at least 90 days by country where the real estate collateral is located

EUR million	2017	2016
Germany	–	–
Total	**–**	–

Additional information on mortgage receivables pursuant to section 28 para. 2 no. 3 PfandBG

As at the reporting date, no (FY 2016: 0) commercial and no (FY 2016: 0) residential properties were the subject of foreclosure sale proceedings or pending administrative receivership proceedings.

No (FY 2016: 0) commercial property and no (FY 2016: 0) residential properties were foreclosed on in the reporting year.

No properties were repossessed in 2017 or 2016 to avoid losses on mortgages.

No interest was overdue on mortgage loans on residential property (FY 2016: 0) as at the reporting date.

No interest was overdue on mortgage loans on commercial property in financial years 2017 or 2016.

Receivables used to cover public Pfandbriefs by debtor, guarantor and its domicile

	Cover assets	
EUR million	**2017**	**2016**
Germany	**21,733**	**21,750**
• national government	1,220	1,096
• regional authorities	9,373	9,308
• local authorities	9,412	9,359
• other debtors	1,423	1,594
• additional cover	304	393
of which: export credit insurers	995	1,040
Austria	**6**	**11**
• national government	6	11
of which: export credit insurers	6	11
Belgium	**91**	**93**
• other debtors	91	93
Canada	**18**	**70**
• local authorities	18	70
France	**343**	**342**
• national government	343	342
of which: export credit insurers	304	342
Luxembourg	**13**	**19**
• national government	13	19
of which: export credit insurers	13	19
Spain	**12**	**16**
• local authorities	12	16
Switzerland	**–**	**185**
• regional authorities	–	120
• other debtors	–	65
United Kingdom	**915**	**1,043**
• national government	297	398
• local authorities	617	646
of which: export credit insurers	297	398
USA	**32**	**37**
• national government	32	37
of which: export credit insurers	32	37
Total	**23,162**	**23,566**

Total amount of payments overdue for at least 90 days on public receivables and their regional distribution

EUR million	2017	2016
Germany	**1**	**–**
• national government	1	–
Luxembourg	**1**	**1**
• national government	1	1
Total	**2**	**1**

Overdue public receivables due from regional authorities are principally receivables from private individuals which regional authorities have guaranteed.

Total receivable amount of payments overdue for at least 90 days on public-sector receivables by region

EUR million	2017	2016
Germany	**4**	**–**
• national government	4	–
Luxembourg	**7**	**8**
• national government	7	8
Total	**11**	**8**

Supplementary information

Shareholdings

Name and location of the investee	Type of share-holding	Percentage held	Equity in EUR ’000	Earnings in EUR ’000
Affiliated companies				
Bauland GmbH, Baulandbeschaffungs-, Erschließungs- und Wohnbaugesellschaft, Munich	Indirect	94.5	–10,106	–
Bavaria Immobilien-Beteiligungs-Gesellschaft mbH & Co. Objekt Fürth KG, Munich	Indirect	100.0	–	–
Bavaria Immobilien-Beteiligungs-Gesellschaft mbH, Munich	Indirect	100.0	4	–1
Bayerische Landesbank Europa-Immobilien-Beteiligungs-GmbH, Munich	Indirect	100.0	109	–
Bayerische Landesbank Immobilien-Beteiligungs-Gesellschaft mbH & Co. KG, Munich	Direct	100.0	37,115	4,560
Bayerische Landesbank Immobilien-Beteiligungs-Verwaltungsgesellschaft mbH, Munich	Direct	100.0	51	4
Bayern Bankett Gastronomie GmbH, Munich[1]	Direct	100.0	514	–
Bayern Card-Services GmbH - S-Finanzgruppe, Munich	Direct	50.1	23,818	3,573
Bayern Corporate Services GmbH, Munich	Indirect	100.0	205	–
Bayern Facility Management GmbH, Munich[1]	Direct	100.0	2,560	–
BayernFinanz Gesellschaft fur Finanzmanagement und Beteiligungen mbH, Munich[1]	Direct	100.0	725	–
Bayernfonds Australien 4 GmbH i.L., Munich	Indirect	100.0	25	–
Bayernfonds Immobilien Concept GmbH, Munich	Indirect	100.0	18	–4
Bayernfonds Immobiliengesellschaft mbH, Munich	Direct and indirect	100.0	4,087	–982
Bayernfonds Kambera GmbH, Munich	Indirect	100.0	25	–
Bayernfonds Opalus GmbH, Munich	Indirect	100.0	25	–
BayernImmo 2. Joint Venture Verwaltungs GmbH, Munich	Indirect	100.0	22	–3
BayernInvest Kapitalverwaltungsgesellschaft mbH, Munich[1]	Direct	100.0	18,754	–
BayernInvest Luxembourg S.A., L - Munsbach	Indirect	100.0	1,288	–35
BayernLB Capital Partner GmbH, Munich	Direct	100.0	1,325	41
BayernLB Capital Partner Verwaltungs-GmbH, Munich	Direct	100.0	44	2
BayernLB Mittelstandsfonds GmbH & Co. Unternehmens-beteiligungs KG, Munich	Direct and indirect	100.0	25,508	1,584
BayernLB Private Equity GmbH, Munich	Direct	100.0	25,565	9,255
BayTech Venture Capital Initiatoren GmbH & Co. KG, Munich	Indirect	46.8	16	–41
Berchtesgaden International Resort Betriebs GmbH, Munich[1]	Direct	100.0	9,368	–
Berthier Participations SARL, F - Paris	Direct	100.0	398	12
BestLife 3 International GmbH & Co. KG, Munich	Indirect	50.4	10,418	–3,457
BGFM Bayerische Gebäude- und Facilitymanagement AG & Co. KG, Munich	Indirect	100.0	42	84
BGV IV Verwaltungs GmbH, Munich	Indirect	100.0	40	1
BGV VII Verwaltungs GmbH, Munich	Indirect	100.0	25	–
BGV VI Verwaltungs GmbH, Munich	Indirect	100.0	16	–7
BGV V Verwaltungs GmbH, Munich	Indirect	100.0	34	1
BLB-Beteiligungsgesellschaft Sigma mbH, Munich[1]	Direct	100.0	971	–
BLB-VG22-Beteiligungsgesellschaft mbH, Munich	Direct	100.0	2,467	–4
Deutsche Kreditbank Aktiengesellschaft, Berlin[1]	Direct	100.0	2,435,912	–
DKB BayernImmo Beteiligungs GmbH & Co. KG, Munich[2]	Indirect	100.0		

Name and location of the investee	Type of share-holding	Percentage held	Equity in EUR ’000	Earnings in EUR ’000
DKB Finance GmbH, Berlin	Indirect	100.0	12,115	–
DKB Grund GmbH, Berlin	Indirect	100.0	126	9
DKB Immobilien Beteiligungs GmbH, Potsdam	Indirect	100.0	2,165	157
DKB Service GmbH, Potsdam	Indirect	100.0	7,100	–
DKB Wohnen GmbH, Berlin	Indirect	94.5	25	–
DKB Wohnungsbau- und Stadtentwicklung GmbH, Berlin	Indirect	100.0	2,500	–
FMP Forderungsmanagement Potsdam GmbH, Potsdam	Indirect	100.0	8,190	3,535
GbR Olympisches Dorf, Potsdam	Indirect	100.0	86	86
German Centre for Industry and Trade Shanghai Co. Ltd., PRC - Shanghai/PRC	Indirect	100.0	40,034	1,334
German Centre for Industry and Trade Taicang Co. Ltd., PRC - Taicang	Indirect	100.0	3,300	−798
German Centre Limited, BVI - Tortola	Direct	100.0	30,185	1,152
gewerbegrund AIRPORT GmbH Beteiligungsgesellschaft, Munich	Indirect	100.0	61	−1
gewerbegrund Bauträger GmbH & Co. Objekt IGG KG, Munich	Indirect	100.0	64	7
gewerbegrund Projektentwicklungsgesellschaft (gpe) mbH, Munich[1]	Direct	100.0	50	–
Global Format GmbH & Co. KG, Munich	Direct	52.4	1,992	170
Global Format Verwaltungsgesellschaft mbH, Munich	Indirect	100.0	30	1
LB Immobilienbewertungsgesellschaft mbH, Munich[1]	Direct	100.0	827	–
LB-RE S.A., L - Luxembourg	Indirect	100.0	5,082	–
Melhoria Immobiliengesellschaft mbH, Potsdam	Indirect	100.0	3,102	–
MVC Unternehmensbeteiligungsgesellschaft mbH, Berlin	Indirect	100.0	224	16
Oberhachinger Bauland GmbH, Wohnbau- und Erschließungsgesellschaft, Munich	Indirect	91.0	−2,416	–
Potsdamer Immobiliengesellschaft mbH, Potsdam	Indirect	100.0	44	8
PROGES DREI GmbH, Berlin	Indirect	100.0	662	−4
PROGES EINS GmbH, Berlin	Indirect	100.0	480	–
PROGES ENERGY GmbH, Berlin	Indirect	100.0	732	278
PROGES Sparingberg GmbH, Berlin	Indirect	100.0	110	−474
PROGES VIER GmbH, Berlin	Indirect	100.0	210	51
PROGES ZWEI GmbH, Berlin	Indirect	100.0	3,941	2,718
Real I.S. AG Gesellschaft für Immobilien Assetmanagement, Munich[1]	Direct	100.0	45,455	–
Real I.S. Australia Pty. Ltd., AUS - Sydney	Indirect	100.0	169	107
Real I.S. Beteiligungs GmbH, Munich	Indirect	100.0	88	8
Real I.S. BGV VII Europa Verwaltungs GmbH, Munich	Indirect	100.0	24	−1
Real I.S. Finanz GmbH, Munich[1]	Direct	100.0	25	–
Real I.S. Fonds Service GmbH, Munich[1]	Direct	100.0	196	–
Real I.S. France SAS, F - Paris	Indirect	100.0	886	197
Real I.S. Fund Management GmbH, Munich	Indirect	100.0	58	8
Real I.S. Gesellschaft für Immobilien Entwicklung und Projektrealisierung mbH & Co. KG, Munich	Indirect	100.0	4,388	−33
Real I.S. Gesellschaft für Immobilienentwicklung mbH, Munich	Indirect	100.0	1,151	7
Real I.S. GREF Verwaltungs GmbH, Munich	Indirect	100.0	23	−2
Real I.S. Investment GmbH, Munich	Indirect	100.0	3,000	–
Real I.S. Management Hamburg GmbH, Munich	Indirect	100.0	27	1
Real I.S. Management SA, L - Munsbach	Indirect	100.0	267	12
Real I.S. Melbourne Australien 10 GmbH & Co. KG, Munich[2]	Indirect	100.0		

Name and location of the investee	Type of share-holding	Percentage held	Equity in EUR ’000	Earnings in EUR ’000
Real I.S. Objekt Bruchsal Verwaltungsgesellschaft mbH i.L., Oberhaching	Indirect	100.0	29	3
Real I.S. SMART Verwaltungs GmbH, Munich	Indirect	100.0	23	−2
Schütz Group GmbH & Co. KG, Rosbach	Indirect	54.4	2,783	1
Schütz Group Verwaltungsgesellschaft mbH, Rosbach	Indirect	100.0	49	2
SEPA Objekt Bruchsal GmbH & Co. KG i.L., Oberhaching	Indirect	100.0	91	−10
SEPA/Real I.S. Objekt Bruchsal Rathausgalerie GmbH & Co. KG, Oberhaching	Indirect	100.0	2,162	770
SEPA/Real I.S. Objekt Bruchsal Rathausgalerie Verwaltungs-GmbH, Oberhaching	Indirect	94.0	32	2
TFD und BGV VI Verwaltungs GmbH, Munich	Indirect	100.0	22	–
TFD und RFS Verwaltungs GmbH, Munich	Indirect	100.0	23	–
TFD Verwaltungs GmbH, Munich	Indirect	100.0	22	−3
Versorgungskasse I BayernLB Gesellschaft mit beschränkter Haftung, Munich	Direct	100.0	18,434	3,187
Versorgungskasse II BayernLB Gesellschaft mit beschränkter Haftung, Munich	Direct	100.0	19,335	2,076
Participations				
ABG Allgemeine Bauträger- und Gewerbeimmobiliengesellschaft & Co. Holding KG, Munich	Indirect	50.0	158	−134
ABG Allgemeine Bauträger- und Gewerbeimmobiliengesellschaft mbH, Munich	Indirect	50.0	60	1
AKA Ausfuhrkredit GmbH, Frankfurt am Main	Direct	7.2	231,752	22,885
AKG ImmoPlus GmbH, Berlin[2]	Indirect	50.0		
AQUILA Technische Entwicklungen GmbH i.I., Schönhagen[2]	Indirect	16.1		
Bau-Partner GmbH i.I., Halle (Saale)	Indirect	49.6	−239	−553
BayBG Bayerische Beteiligungsgesellschaft mbH, Munich	Direct	12.9	226,714	12,688
Bayerische Garantiegesellschaft mbH für mittelständische Beteiligungen, Munich	Direct	8.2	48,737	2,360
Bayernfonds Asia-Pacific Growth GmbH & Co. KG, Munich	Indirect	0.1	17,967	−1,220
Bayernfonds Immobilien Bürocenter Leipzig Käthe Kollwitz Straße KG, Munich	Indirect	0.2	–	2,232
Bayernfonds Immobilien Bürocenter Magdeburg KG, Munich	Indirect	0.1	6,582	−811
Bayernfonds Immobilien City-Investitionen Objekte Erfurt und Jena KG, Munich	Indirect	5.1	17,010	1,218
Bayernfonds Immobilien Dresden Bürozentrum Falkenbrunnen KG, Munich	Indirect	0.0	18,406	844
Bayernfonds Immobilien Fachmarktzentrum Erfurt, Leipziger Straße KG, Munich	Indirect	0.2	3,383	678
Bayernfonds Immobiliengesellschaft mbH & Co. Objekt Bad Kissingen Burkardus Wohnpark KG i.L., Munich	Indirect	0.2	–	8,032
Bayernfonds Immobiliengesellschaft mbH & Co. Objekt Hannover Forum im Pelikanviertel KG, Munich	Indirect	0.1	3,361	452
Bayernfonds Immobilien Jena Gewerbepark KG, Munich	Indirect	0.1	9,291	563
Bayernfonds Immobilien Objekt Berlin Hofgarten Friedrichstraße KG i.L., Munich	Indirect	0.0	79,584	53,238
Bayernfonds Immobilien Objekt Essen Holle-Karree KG, Munich	Indirect	0.1	8,206	676
Bayernfonds Immobilien Objekt Leipzig, Friedrich List Haus KG, Munich	Indirect	0.0	24,806	737
Bayernfonds Immobilienverwaltung Austria Objekt Bischofshofen KG, Munich	Indirect	0.0	7,393	266

Name and location of the investee	Type of share-holding	Percentage held	Equity in EUR ’000	Earnings in EUR ’000
Bayernfonds Immobilienverwaltung Austria Objekte Salzburg und Wien KG, Munich	Indirect	0.1	24,401	686
Bayernfonds Immobilienverwaltung GmbH & Co. Australien 7 KG, Munich	Indirect	0.0	71,730	2,664
Bayernfonds Immobilienverwaltung GmbH & Co. Australien 8 KG, Munich	Indirect	0.0	82,432	4,457
Bayernfonds Immobilienverwaltung GmbH & Co. Australien 9 KG, Munich	Indirect	0.0	83,661	3,027
Bayernfonds Immobilienverwaltung GmbH & Co. Hamburg Steindamm KG, Munich	Indirect	0.3	16,989	902
Bayernfonds Immobilienverwaltung GmbH & Co. Kambera KG, Munich	Indirect	0.0	129,395	9,446
Bayernfonds Immobilienverwaltung GmbH & Co. Objekt England I KG, Munich	Indirect	0.2	20,954	575
Bayernfonds Immobilienverwaltung GmbH & Co. Objekt Hamburg 3 KG, Munich	Indirect	5.3	24,753	134
Bayernfonds Immobilienverwaltung GmbH & Co. Objekt Hamburg I KG, Munich	Indirect	0.3	6,654	456
Bayernfonds Immobilienverwaltung GmbH & Co. Objekt München KG, Munich	Indirect	0.3	10,874	522
Bayernfonds Immobilienverwaltung GmbH & Co. Objekt München Landsberger Straße KG, Munich	Indirect	0.3	23,417	1,110
Bayernfonds Immobilienverwaltung GmbH & Co. Objekt München Ungerer Straße KG, Munich	Indirect	0.3	13,383	252
Bayernfonds Immobilienverwaltung GmbH & Co. Opalus KG, Munich	Indirect	0.0	100,727	8,482
Bayernfonds Immobilienverwaltung GmbH & Co. Regensburg KG, Munich	Indirect	0.3	33,267	1,371
Bayernfonds Immobilienverwaltung Objekt Bad Homburg KG, Munich	Indirect	5.1	7,810	714
Bayernfonds Immobilienverwaltung Objekt Berlin Schönhauser Allee Arcaden KG, Munich	Indirect	5.7	5,891	2,753
Bayernfonds Immobilienverwaltung Objekt Berlin Taubenstraße KG, Munich	Indirect	0.4	– 10,434	868
Bayernfonds Immobilienverwaltung Objekt Düsseldorf Bonneshof GmbH & Co. KG, Munich	Indirect	0.3	27,425	927
Bayernfonds Immobilienverwaltung Objekt Wiesbaden, Hagenauer Straße 42, 44 und 46 KG, Munich	Indirect	5.1	13,899	– 56
Bayernfonds Pacific Growth GmbH & Co. KG, Munich	Indirect	0.0	19,655	– 92
Bayerngrund Grundstücksbeschaffungs- und -erschließungs-Gesellschaft mit beschränkter Haftung, Munich	Direct	50.0	8,951	5
BayernImmo 1. Joint Venture GmbH & Co. KG, Munich	Indirect	50.0	7,588	– 3
BayernImmo 1. Joint Venture Verwaltungs GmbH, Munich	Indirect	50.0	20	– 5
Bayern Mezzaninekapital GmbH & Co. KG - Unternehmensbeteiligungsgesellschaft, Munich	Direct	25.5	31,864	2,358
Bayern Mezzaninekapital Verwaltungs GmbH, Munich	Direct	49.0	46	1
BF Gewerbepark I GmbH i.L., Oberhaching	Indirect	6.0	22	–
BF Immobilienverwaltung Objekte München, Rüsselsheim, Düsseldorf-Ratingen KG, Munich	Indirect	0.3	7,606	14,426
BF REAL I.S. - DB Real Estate Immobilienverwaltung Objekte Berlin, Düsseldorf, Essen KG, Munich	Indirect	5.5	47,876	29,094
BGV Holding GmbH & Co. KG, Oberhaching	Indirect	0.0	44,456	3,196
BGV III Feeder 1 S.C.S. SICAV-FIS, L - Luxembourg	Indirect	0.1	–	17,990

Name and location of the investee	Type of share-holding	Percentage held	Equity in EUR '000	Earnings in EUR '000
BGV IV LYON 1 SCI, Munich	Indirect	0.0	12,467	–705
BGV IV PARIS 1 SCI, F - Paris	Indirect	0.0	5,731	72
BGV VI FAUBOURG SCI, F - Paris[2]	Indirect	0.0		
BGV V LYON 1 SCI, F - Paris	Indirect	0.0	19,405	–1,473
BGV V Paris 1 SCI , F - Paris	Indirect	0.0	7,930	–609
BGV V PARIS 2 SCI, F - Paris	Indirect	0.0	21,990	–1,346
BGV V ST GENEVIEVE 1 SCI, F - Paris	Indirect	0.0	7,830	–707
Cap Decisif S.A.S., F - Paris	Indirect	6.0	2,265	–14
CLS Group Holdings AG Zürich, CH - Zurich	Direct	0.7	431,717	37,777
CommuniGate Kommunikationsservice GmbH, Passau	Indirect	50.0	3,607	406
Deutsche Life Science GmbH, Berlin	Indirect	10.2	–15,052	655
Deutsche WertpapierService Bank AG, Frankfurt am Main	Direct	3.7	180,188	8,725
DKB Wohnimmobilien Beteiligungs GmbH & Co. KG, Potsdam	Indirect	5.1	36,746	1,832
Einkaufs-Center Györ Verwaltungs G.m.b.H., Hamburg	Indirect	50.0	31	2
Erste Tinten Holding GmbH, Hohenbrunn	Indirect	21.0	4,717	203
Fay & Real I.S. IE Regensburg GmbH & Co. KG i.L., Oberhaching	Indirect	50.0	425	200
Fay & Real I.S. IE Regensburg Verwaltungs GmbH i.L., Oberhaching	Indirect	50.0	36	2
FidesSecur Versicherungs- und Wirtschaftsdienst Versicherungsmakler GmbH, Munich	Indirect	14.0	4,757	25
Fondations Capital I S.C.A., L - Senningerberg	Direct	23.2	271,667	21,194
Fondsbörse Deutschland Beteiligungsmakler AG, Hamburg	Indirect	2.5	3,384	–
Galintis GmbH & Co. KG, Frankfurt am Main	Direct	15.9	532,745	13,597
GbR Datenkonsortium OpRisk, Bonn[2]	Direct	0.0		
German Biofuels GmbH, Pritzwalk	Indirect	19.9	–7,712	1,169
German Centre for Industry and Trade India Hold-ing-GmbH, Munich	Direct	50.0	906	–500
GESO Gesellschaft für Sensorik, Geotechnischen Umweltschutz und mathematische Modellierung mbH i.I., Jena	Indirect	43.1	–353	–
GHM Holding GmbH, Regenstauf	Indirect	40.0	17,219	–17
GHM MPP Reserve GmbH, Regenstauf	Indirect	50.0	357	–4
GHM MPP Verwaltungs GmbH, Regenstauf	Indirect	50.0	21	–1
G.I.E. Max Hymans, F - Paris	Indirect	33.3	–24,848	4,093
GLB GmbH & Co. OHG, Frankfurt am Main	Direct	6.3	6,236	494
GLB-Verwaltungs-GmbH, Frankfurt am Main	Direct	6.2	52	2
Immo 3 Rue Jean Monnet S.à.r.l., L - Luxembourg	Indirect	10.0	55,388	1,132
JFA Verwaltung GmbH, Leipzig	Indirect	10.7	–13,033	78
KGAL GmbH & Co. KG, Grünwald	Direct	3.4	59,140	21,914
Kreditgarantiegemeinschaft des bayerischen Gartenbaus GmbH, Munich	Direct	7.2	649	–
Kreditgarantiegemeinschaft des bayerischen Handwerks GmbH, Munich	Direct	9.9	4,846	–
Kreditgarantiegemeinschaft des Hotel- und Gaststätten-gewerbes in Bayern GmbH, Munich	Direct	8.6	4,359	–
Kreditgarantiegemeinschaft für den Handel in Bayern GmbH, Munich	Direct	6.8	6,317	–
LEG Kiefernsiedlung Grundstücksgesellschaft b.R., Berlin	Indirect	6.4	–3,360	338
LEG Wohnpark am Olympischen Dorf Grundstücks-gesellschaft b.R., Berlin	Indirect	7.5	–5,767	668

Name and location of the investee	Type of share-holding	Percentage held	Equity in EUR ’000	Earnings in EUR ’000
LEG Wohnpark Heroldplatz Grundstücksgesellschaft b.R., Berlin	Indirect	7.7	−1,512	112
Mediport Venture Fonds Zwei GmbH i.I., Berlin	Indirect	53.8	267	−1,687
MTI Main-Taunus Immobilien GmbH, Bad Homburg v.d.H.	Indirect	50.0	177	−4
MVP Fund II GmbH & Co. KG, Munich	Direct	10.0	54,998	−2,909
Neue Novel Ferm Verwaltungs GmbH, Berlin	Indirect	49.0	24	−3
Neumarkt-Galerie Immobilienverwaltungsgesellschaft mbH i.L., Cologne	Indirect	49.0	82	−2
nfon AG, Munich	Indirect	6.4	5,428	−687
Novel Ferm Brennerei Dettmannsdorf GmbH & Co. KG, Berlin	Indirect	49.0	–	−21
PARIS EDEN MONCEAU SCI, F - Paris	Indirect	0.0	60,399	−351
RAC 2 N.V., B - Watermael-Boitsfort[2]	Indirect	0.0		
Real I.S. Grundvermögen GmbH & Co. geschlosssene Investment-KG, Munich	Indirect	5.4	68,710	594
Real I.S. Institutional Real Estate 1 GmbH & Co. geschlossene Investment-KG, Munich	Indirect	0.0	66,086	7,224
Real I.S. Westbahnhof Wien GmbH & Co. geschlossene Investment-KG, Munich[2]	Indirect	0.0		
RealMatch Ltd., IL - Kfar Sava	Indirect	9.2	1,133	−3,207
RSU Rating Service Unit GmbH & Co. KG, Munich	Direct	20.0	14,946	1,825
S CountryDesk GmbH, Cologne	Direct	2.5	405	32
SIGNA 03 Milano S.a.s. di SIGNA Milano S.r.l. & C., I - Bolzano	Indirect	2.0	26,161	−2,366
SIZ GmbH, Bonn	Direct	5.0	4,920	334
S-Karten-Service-Management GmbH - Saarbrücken - München, Munich	Indirect	50.0	100	1
Sophia Euro Lab S.A.S. i.L., F - Sophia Antipolis Cedex	Indirect	32.3	1,550	148
SOUTH CITY OFFICE FONSNY S.A., B - Bruxelles[2]	Indirect	0.0		
TAG Wohnungsgesellschaft Berlin-Brandenburg mbH, Hamburg	Indirect	5.2	8,235	−369
TEGES Grundstücks-Vermietungsgesellschaft mbH, Berlin	Indirect	50.0	18	–
TEGES Grundstücks-Vermietungsgesellschaft mbH & Co. Objekt Berlin KG, Berlin	Indirect	47.0	−6,714	295
THE GREEN CORNER S.A., B - Watermael-Boitsfort[2]	Indirect	0.0		
True Sale International GmbH, Frankfurt am Main	Direct	7.7	4,809	46
Visa Inc., USA - San Francisco	Direct and indirect	0.0	32,760,000	6,699,000

The information is based on the most recent available annual financial statements of the investees. Foreign currency amounts were converted to euros at the respective spot exchange rate at the end of the year.

1 A profit and loss transfer agreement has been concluded with the company.

2 Approved annual financial statements are not available yet.

Participations in large limited companies (including credit institutions) exceeding 5 percent of the voting rights

Name and location of the investee
AKA Ausfuhrkredit GmbH, Frankfurt am Main
BayBG Bayerische Beteiligungsgesellschaft mbH, Munich
Bayerische Garantiegesellschaft mbH für mittelständische Beteiligungen, Munich
Bayern Card-Services GmbH - S-Finanzgruppe, Munich
BayernInvest Kapitalverwaltungsgesellschaft mbH, Munich
BayernInvest Luxembourg S.A., L - Munsbach
Deutsche Kreditbank Aktiengesellschaft, Berlin
DKB Service GmbH, Potsdam
Real I.S. AG Gesellschaft für Immobilien Assetmanagement, Munich
Real I.S. Investment GmbH, Munich

As at the reporting date, BayernLB was a general partner in the following entities:

- ABAKUS, Hannover, GbR
- GbR Datenkonsortium OpRisk, Bonn, GbR
- GLB GmbH & Co. OHG, Frankfurt am Main, GmbH & Co. OHG

Letters of comfort

Certain of BayernLB's subsidiaries and their creditors have been issued with letters of comfort, giving the subsidiaries significant benefits in terms of improved business terms and better financing conditions. BayernLB also benefits as the value of its subsidiaries is enhanced. At the same time, however, it is also potentially liable for losses.

BayernLB is liable for ensuring that Deutsche Kreditbank Aktiengesellschaft, Berlin is able to fulfil its contractual obligations in proportion to the size of its equity interest except in cases of political risk.

Expiry of the letter of comfort for LB(Swiss) Privatbank AG as at 21 December 2009 and for Landesbank Saar as at 21 June 2010

Prior to the reporting year, BayernLB issued letters of comfort for LB(Swiss) Privatbank AG, Zurich (LB(Swiss)) and Landesbank Saar, Saarbrücken (SaarLB). At the end of 21 December 2009 BayernLB transferred its equity interest in LB(Swiss) to Landesbank Hessen-Thüringen, Frankfurt am Main and at the end of 21 June 2010 sold its 25.2 percent stake in SaarLB to the Saarland. SaarLB therefore no longer qualifies as an affiliated company of BayernLB under section 271, para. 2 HGB (German Commercial Code). As a result the letter of comfort for LB(Swiss) expired at the end of 21 December 2009 and for SaarLB at the end of 21 June 2010. The liabilities of LB(Swiss) created after the end of 21 December 2009 and the liabilities of SaarLB created after the end of 21 June 2010 are not covered by the letters of comfort and therefore any previous declarations were revoked.

Expiry of the letter of comfort for Banque LBLux S.A. (since renamed Banque LBLux S.A. in Liquidation), Luxembourg as at 1 May 2015

BayernLB previously issued a letter of comfort for Banque LBLux S.A. (since renamed Banque LBLux S.A. in Liquidation), Luxembourg. This letter of comfort was rescinded with effect from the end of 30 April 2015. As a result, the letter of comfort will in particular no longer cover liabilities of Banque LBLux S.A. (since renamed Banque LBLux S.A. in Liquidation) that were created after 30 April 2015, and all previously issued letters were also revoked.

Other financial obligations

Other financial obligations, which arise from daily operations principally under agency, rental, lease, usage, service and maintenance, consulting and marketing agreements, were within normal bounds.

As at the reporting date, there were call commitments for capital not fully paid up of EUR 6 million (FY 2016: EUR 8 million) and liabilities from limited partnership interests of EUR 29 million (FY 2016: EUR 29 million). Amounts due to affiliated companies totalled EUR 29 million (FY 2016: EUR 30 million).

As at the reporting date, BayernLB had EUR 35 million (FY 2016: EUR 29 million) of irrevocable payment obligations in connection with the bank levy and deposit guarantee scheme. Cash collateral of EUR 23 million (FY 2016: EUR 17 million) was pledged for the bank levy and EUR 12 million (FY 2016: EUR 12 million) of securities collateral provided for the deposit guarantee scheme.

Following implementation of the Deposit Guarantee Scheme Act (EinSiG), which became law on 3 July 2015, agreement was reached on a new system for calculating the target volume in the guarantee scheme. Member institutions have until 3 July 2024 to achieve the target volume of funds for the guarantee scheme (the fill-up phase). The amount of the target volume is calculated each year based on the data as at 31 December of the previous year. The annual contribution needed to achieve this (the target volume) will be calculated by 31 May each year by the German Savings Bank Association (DSGV), the body responsible for the guarantee scheme.

Under the terms of the statutes of the deposit insurance fund run by the Association of German Public Banks, VÖB, e. V. (Bundesverband Öffentlicher Banken Deutschlands (VÖB)), BayernLB has undertaken to compensate the fund for all proven defaults which it has incurred on the basis of payments it has made to Deutsche Kreditbank Aktiengesellschaft, Berlin (DKB) pursuant to the statutes if it is unable to enforce its rights of recourse against DKB pursuant to the statutes.

Under the terms of the contract of 10 December 2012 to spin off Bayerische Landesbausparkasse (LBS AöR-old) to LBS Bayerische Landesbausparkasse (LBS AöR-new), BayernLB and LBS AöR-new are jointly and severally liable for BayernLB's liabilities that were created up until the date of spin-off and assigned to LBS AöR-new in the spin-off agreement. BayernLB is liable for the liabilities within the meaning of the preceding sentence only if they mature within five years of the date of spin-off and the resulting claim is legally asserted against BayernLB. Due to the stable net assets, financial position and results of operations of LBS AöR-new there is currently no risk of a claim being brought.

Transactions with related parties

BayernLB maintains commercial relationships with related parties. These include the Free State of Bavaria and the Association of Bavarian Savings Banks, Munich (SVB), whose indirect stakes in BayernLB are 75 percent and 25 percent respectively, subsidiaries, joint ventures and associates. In addition, the members of BayernLB's Board of Management and Supervisory Board and their close family members and companies controlled by these parties or jointly controlled if these parties are members of their management bodies are also deemed related parties.

Transactions with related parties were concluded at standard market terms and conditions.

Administrative bodies of BayernLB

Supervisory Board

Gerd Haeusler
Chairman of the BayernLB Supervisory Board
Munich

Walter Strohmaier
Deputy Chairman of the BayernLB Supervisory Board
Chairman of the Board of Directors
Sparkasse Niederbayern-Mitte
Straubing

Dr Roland Fleck
Managing Director
NürnbergMesse GmbH
Nuremberg

Dr Ute Geipel-Faber
Senior Advisor
Invesco Real Estate GmbH
Munich

Dr Kurt Gribl
since 1 January 2017
Member of the BayernLB Supervisory Board
Lord Mayor
Augsburg

Dr Ulrich Klein
Under Secretary
Bavarian State Ministry of Finance,
Regional Development and Regional Identity
Munich

Dr Thomas Langer
Under Secretary
Bavarian State Ministry for Economic Affairs
and the Media, Energy and Technology
Munich

Wolfgang Lazik
Deputy Secretary
Bavarian State Ministry of Finance,
Regional Development and Regional Identity
Munich

Professor Dr Bernd Rudolph
LMU Munich and Steinbeis-Hochschule Berlin

Henning Sohn
Chairman of the General Staff Council
BayernLB
Munich

Stephan Winkelmeier
since 1 May 2017
Member of the BayernLB Supervisory Board
Spokesman of the Board of Directors
FMS Wertmanagement AöR
Munich

Professor Dr Christian Rödl
until 30 April 2017
Member of the BayernLB Supervisory Board
Managing Partner
Rödl & Partner GbR
Nuremberg

Board of Management (including allocation of responsibilities as from 1 January 2018)

Dr Johannes-Jörg Riegler
CEO
Corporate Center
Deutsche Kreditbank Aktiengesellschaft

Dr Edgar Zoller
Deputy CEO
Real Estate & Savings Banks/Association
Bayerische Landesbodenkreditanstalt[1]
Real I.S. AG Gesellschaft für Immobilien Assetmanagement

Marcus Kramer
CRO
Risk Office

Michael Bücker
Corporates & Mittelstand

Dr Markus Wiegelmann
CFO/COO
Financial Office
Operating Office

Ralf Woitschig
Financial Markets
BayernInvest Kapitalverwaltungsgesellschaft mbH

1 Dependent institution of the Bank.

Remuneration of the administrative bodies

EUR '000	2017	2017	2016	2016
Total remuneration for the financial year:				
Members of the Board of Management		**4,282**		**4,074**
• CEO	731		724	
– Base salary	700		700	
– Variable compensation	31		24	
• Deputy CEO	713		698	
– Base salary	650		650	
– Variable compensation	63		48	
• Ordinary members of the Board of Management	2,651		2,590	
– Base salary	2,400		2,400	
– Variable compensation	251		190	
• Ancillary remuneration (non-cash compensation)	188		62	
Members of the Supervisory Board		**714**		**851**
Former members of the Board of Management and their surviving dependants		**4,263**		**4,127**
Pension provisions established for former members of the Board of Management and their surviving dependants		**84,074**		**82,293**

Loans to the administrative bodies

There were no loans to administrative bodies as at the reporting date.

Mandates held by legal representatives or by other employees

Name	Mandates held in supervisory bodies constituted under German law for large limited companies (including all credit institutions) [1]
Board of Management	
Dr Johannes-Jörg Riegler	Deutsche Kreditbank Aktiengesellschaft, Berlin
Dr Edgar Zoller	Deutsche Kreditbank Aktiengesellschaft, Berlin Real I.S. AG Gesellschaft für Immobilien Assetmanagement, Munich
Marcus Kramer	Deutsche Kreditbank Aktiengesellschaft, Berlin
Dr Markus Wiegelmann	Deutsche Kreditbank Aktiengesellschaft, Berlin
Ralf Woitschig	BayernInvest Kapitalverwaltungsgesellschaft mbH, Munich
Employees	
Oliver Aschauer	BayernInvest Kapitalverwaltungsgesellschaft mbH, Munich
Dr Jörg Hader	BayernInvest Kapitalverwaltungsgesellschaft mbH, Munich
Alexander Plenk	BayernInvest Kapitalverwaltungsgesellschaft mbH, Munich
Bernd Mayer	Real I.S. AG Gesellschaft für Immobilien Assetmanagement, Munich

1 *This information is valid as at 31 December 2017.*

External auditor's fees

EUR million	2017	2016
Total fees recorded as expenses in the financial year for		
• the financial statements audits	5	4
• other certification services	–	1
• tax consultancy services	–	–
• other services	–	1
Total	**6**	**5**

The financial statements audit services includes fees of EUR 0.4 million for the review of the Group Half-Yearly Financial Report for 2017. For other assurance services, fees were paid to the external auditors for certifications/confirmations required under supervisory law and the voluntary issuance of a letter of comfort. Other services comprises fees for other certifications/confirmations contractually agreed between BayernLB and the external auditor for a third party (e.g. with the German Savings Bank Association (DSGV)). There are no services included under other assurance services and other services that are significant in terms of amounts.

Number of employees (annual average)

	2017	2016
Female	1,451	1,442
Male	1,658	1,645
Total	**3,109**	**3,087**

The total figure includes 949 (FY 2016: 913) part-time employees, which corresponds to 655 (FY 2016: 624) full-time employees. The 66 (FY 2016: 87) trainees and students on a vocationally integrated course at a vocational academy are not included.

Events after the reporting period

The following event of major significance occurred after the close of financial year 2017:

The economic deterioration of a credit exposure meant that a large addition had to be made to the risk provisions in the fourth quarter of 2017. The exposure was sold off in full in the first quarter of 2018. As a result, BayernLB expects to release the double-digit million euro risk provision recognised in the 2017 annual financial statements. In the first quarter of 2018, BayernLB also received recoveries on written down receivables in the lower double-digit million euros from an earlier loan exposure.

No other events of major significance occurred after 31 December 2017.

Proposal for the appropriation of income

BayernLB's Board of Management has proposed that EUR 313 million of the EUR 363 million net income for the financial year 2017 be allocated to retained earnings and that the distributable profit of EUR 50 million be paid to the providers of capital.

Responsibility statement by the Board of Management

To the best of our knowledge, and in accordance with the applicable reporting principles for the preparation of the annual financial statements, the Bank's financial statements give a true and fair view of the net assets, financial position and results of operations of Bayerische Landesbank, Munich, and the management report includes a fair view of the development and performance of the business and the position of Bayerische Landesbank, together with a description of the principal opportunities and risks associated with the expected performance of Bayerische Landesbank.

Munich, 19 March 2018

Bayerische Landesbank
The Board of Management

Dr Johannes-Jörg Riegler	Dr Edgar Zoller	Marcus Kramer
Michael Bücker	Dr Markus Wiegelmann	Ralf Woitschig

Independent Auditor’s Report

To Bayerische Landesbank AöR, Munich

Report on the Audit of the Annual Financial Statements and the Management Report

Audit Opinions

We have audited the annual financial statements of Bayerische Landesbank AöR, Munich, which comprise the balance sheet as at 31 December 2017 and the statement of profit and loss for the financial year from 1 January to 31 December 2017, and the notes to the financial statements, including the recognition and measurement policies presented therein. In addition, we have audited the management report of Bayerische Landesbank AöR, Munich for the financial year from 1 January to 31 December 2017. In accordance with the German legal requirements, we have not audited the content of the management report specified in the “Other information” section of our auditor’s report.

In our opinion, on the basis of the knowledge obtained in the audit,

- the accompanying annual financial statements comply, in all material respects, with the requirements of German commercial law applicable to business corporations and the supplementary provisions of the Bayerische Landesbank Act and the Statutes of Bayerische Landesbank, and give a true and fair view of the assets, liabilities and financial position of the Company as at 31 December 2017 and of its financial performance for the financial year from 1 January to 31 December 2017 in compliance with German Legally Required Accounting Principles, and
- the accompanying management report as a whole provides an appropriate view of the Company’s position. In all material respects, this management report is consistent with the annual financial statements, complies with German legal requirements and appropriately presents the opportunities and risks of future development. Our audit opinion on the management report does not cover the content of the management report specified in the “Other information” section of our auditor’s report.

Pursuant to Section 322 (3) Sentence 1 German Commercial Code (HGB), we declare that our audit has not led to any reservations relating to the legal compliance of the annual financial statements and of the management report.

Basis for the Audit Opinions

We conducted our audit of the annual financial statements and of the management report in accordance with Section 317 German Commercial Code (HGB) and the EU Audit Regulation (No. 537/2014; referred to subsequently as “EU Audit Regulation”) and in compliance with German Generally Accepted Standards for Financial Statement Audits promulgated by the Institut der Wirtschaftsprüfer (IDW). Our responsibilities under those requirements and principles are further described in the “Auditor’s Responsibilities for the Audit of the Annual Financial Statements and of the Management Report” section of our auditor’s report. We are independent of the Company in accordance with the requirements of European law and German commercial and professional law, and we have fulfilled our other German professional responsibilities in accordance with these requirements. In addition, in accordance with Article 10 (2) Point (f) of the EU Audit

Regulation, we declare that we have not provided non-audit services prohibited under Article 5 (1) of the EU Audit Regulation. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinions on the annual financial statements and on the management report.

Key Audit Matters in the Audit of the Annual Financial Statements

Key audit matters are those matters that, in our professional judgment, were of most significance in our audit of the annual financial statements for the financial year from 1 January to 31 December 2017. These matters were addressed in the context of our audit of the annual financial statements as a whole and in forming our audit opinion thereon; we do not provide a separate audit opinion on these matters.

In the following we present the key audit matters we have determined in the course of our audit:

1. Risk provisions in lending business
2. Measurement of trading transactions
3. Completeness and measurement of pension provisions

Our presentation of these key audit matters has been structured as follows:

a) Description (including reference to corresponding information in the annual financial statements)
b) Auditor’s response

1. Risk provisions in lending business

a) The annual financial statements of Bayerische Landesbank AöR as at 31 December 2017 show amounts due from customers and banks in the amount of EUR 102.3 billion, equivalent to 74.0 percent of total assets. There are also contingent liabilities and other obligations of EUR 32.3 billion. The Bank reviews the recoverability of its credit transactions on a regular basis and whenever there is objective evidence this is necessary. A potential need to recognise a provision, i.e. a depreciation to the lower attributable value, is calculated using a procedure set by the Bank as the difference between the current carrying amount of the receivable and the expected future cash inflows discounted using the receivable’s original effective interest rate. Corresponding provisions must also be recognised where necessary for off balance sheet transactions when either drawdown by a doubtful borrower is imminent (guarantees, warranties) or impairments are expected due to obligations to pay (irrevocable loan commitments). Because estimation of the expected future cash flows involves significant discretion, there is a considerable risk that the amount of any necessary value adjustments required may not be appropriate.

   In view of the fact that lending is a core business activity of the Bank and the measurement of receivables and the creation of provisions for drawdowns of contingent liabilities and other obligations depend to a material extent on estimates made at the discretion of the Bank’s Board of Management, this was an especially important matter for our audit.

The disclosures made by the executive directors of the Bank on the risk provisions recognised can be found in particular in the sections in the notes headed Receivables and liabilities (non-trading portfolio) and Events after the reporting date, and under Risk provisions in the management report.

b) As part of our audit we reviewed the relevant internal controls in the lending business for identifying evidence of impairment, rating customers and calculating impairments for the suitability of their design, implementation and effectiveness.

We also assessed, using risk-based samples, the measurement of receivables where the Bank deemed it necessary to conduct an impairment test, including the appropriateness of the values estimated. This involved examining the underlying assumptions, in particular the amount and timing of expected future incoming cash flows.

2. Measurement of trading transactions

a) Bayerische Landesbank AöR enters into trading transactions, especially in securities, Schuldschein note loans and financial derivatives, which are recognised in the annual financial statements at fair value less a risk discount in accordance with Section 340 e (3) Sentence 1 German Commercial Code (HGB) and are mainly reported under assets and liabilities held for trading. For the purposes of drawing up the financial statements and the information in the notes, the Bank mainly calculates the fair value of these holdings using measurement methods and procedures whose key inputs can be directly or indirectly observed in the market. Where no market prices are available for a financial instrument to be measured, price quotations for similar instruments on active markets, price quotations on inactive markets, other observable inputs which are not price quotations, market-based inputs and non-observable inputs are used.

For over-the-counter traded (OTC) derivative financial instruments, the Bank calculates fair value adjustments for counterparty risks (bilateral credit valuation adjustments) and for funding costs (funding valuation adjustments).

Measurement using models gives rise to increased valuation uncertainty and larger reasonable ranges; consequently, we identified measurement of these financial instruments as subject to discretion and thus a key audit matter.

Disclosures of the measurement of trading transactions can be found in particular in the notes in the section headed Fair value.

b) Our audit paid particular attention to financial instruments which had been measured using models and were recognised at fair value. We assessed the appropriateness and effectiveness of the relevant internal control system at Bayerische Landesbank AöR for measuring such financial instruments, especially examining the appropriateness and effectiveness of the audit-relevant controls on the independent price verification (IPV) process and the model validation. Taking a risk-based approach, we assessed the suitability of the valuation models used for selected products with the aid of our internal valuation specialists on the audit team.

We also satisfied ourselves that financial instruments were correctly measured by taking samples. As part of our analysis of securities recognised by the Bank at fair value we consulted experts from the Deloitte network and considered their results, which mainly consisted of comparison prices calculated for securities. We conducted our measurements, particularly of Schuldschein note loans, using sample-based, independent comparison valuations as at the reporting date and compared them with the valuation used by the Bank. In addition, we carried out our own independent ex-post valuation of selected OTC derivative products as at the reporting date and compared this with the valuation used by Bayerische Landesbank AöR. We then checked the methodology used for calculating fair value adjustments for counterparty risks (bilateral credit valuation adjustments) and for funding costs (funding valuation adjustments) on OTC derivatives to see if they were suitable for reporting fair value properly.

3. Completeness and measurement of pension provisions

a) Various retirement benefit plans are in place for active employees of the Bank, those who have left with vested benefits and those who have retired. These are shown in the balance sheet under provisions for pensions and similar obligations and amounted to a total of EUR 2,505.5 million as at the reporting date. This is equivalent to 1.3 percent of total assets. The amount of the provision is calculated based on an actuarial report commissioned by the Bank using the projected unit credit method and taking the plan assets held in account. To calculate pension obligations, assumptions have to be made about the long-term trend in salaries and pensions, staff turnover, the trend in statutory pensions, inflation and mortality. The discount rates on the reporting date in the list of yields for comparable maturities calculated and provided by the Deutsche Bundesbank in accordance with the Regulation on the Discounting of Provisions were used, applying the simplification rule in Section 253 (2) Sentence 2 German Commercial Code (HGB). Bayerische Landesbank AöR calculates the relevant maturity for each category of employee. When measuring the provisions for allowances in the event of illness and other medical benefits, the trend in healthcare costs also has to be taken into consideration. The assumptions in each case are made by the executive directors.

   We identified this as a key audit matter, since the completeness and measurement of pension obligations depends to a considerable extent on the correct underlying data being passed on to the actuary and the calculation is based on assumptions and estimates that rely on the discretion of the executive directors.

   Disclosures on the pension provisions can be found in particular in the notes in the section headed Provisions.

b) As part of our audit we assessed, inter alia, the actuarial reports commissioned by the Bank. Given the specific features of the actuarial calculations, we were supported in this by specialists in our audit team who are qualified members of the German Association of Actuaries and the Institute of Pension Actuaries. To assess the reports for our audit we satisfied ourselves of the competence, ability and objectivity of the external advisers and subjected the valuation processes and assumptions to critical scrutiny and examination. Based on this, we then tracked the figures, the actuarial parameters, the calculation of the provisions and what is shown in the balance sheet and the notes on the basis of the reports.

We also analysed and evaluated the organisational and procedural measures taken by Bayerische Landesbank AöR to see how they ensure that data for individual employees' employment contracts are recorded and that figures transferred to and from the actuary are complete. In addition, our internal specialists in the audit team compared the values for obligations calculated by the Bank's external expert with their own calculations, on a sample basis.

To verify the market values of the plan assets of indirect pension obligations, we examined statements from life insurance companies and external retirement benefit institutions and other evidence of assets. We checked whether these market values had been taken into account as offsettable assets when calculating the deficit on indirect pension obligations.

Other Information

The executive directors are responsible for the other information. The other information comprises

- The combined non-financial report pursuant to Sections 289b to 289e, 315b and 315c German Commercial Code (HGB) mentioned in the management report,
- The report on equality and equal pay (equal pay report) pursuant to Section 21 of the Equal Pay Transparency Act, and
- The responsibility statement by the Board of Management on the annual financial statements and on the management report pursuant to Section 264 (2) Sentence 3 and Section 289 (1) Sentence 5 German Commercial Code (HGB) respectively.

Our audit opinions on the annual financial statements and on the management report do not cover the other information, and consequently we do not express an audit opinion or any other form of assurance conclusion thereon.

In connection with our audit, our responsibility is to read the other information and, in so doing, to consider whether the other information

- is materially inconsistent with the annual financial statements, with the management report or our knowledge obtained in the audit, or
- otherwise appears to be materially misstated.

Responsibilities of the Executive Directors and the Supervisory Board for the Annual Financial Statements and the Management Report

The executive directors are responsible for the preparation of the annual financial statements that comply, in all material respects, with the requirements of German commercial law applicable to business corporations and the supplementary provisions of the Bayerische Landesbank Act and the Statutes of Bayerische Landesbank, and that the annual financial statements give a true and fair view of the assets, liabilities, financial position and financial performance of the Company in compliance with German Legally Required Accounting Principles. In addition, the executive directors are responsible for such internal control as they, in accordance with German Legally Required Accounting Principles, have determined necessary to enable the preparation of annual financial statements that are free from material misstatement, whether due to fraud or error.

In preparing the annual financial statements, the executive directors are responsible for assessing the Company's ability to continue as a going concern. They also have the responsibility for disclosing, as applicable, matters related to going concern. In addition, they are responsible for financial reporting based on the going concern basis of accounting, provided no actual or legal circumstances conflict therewith.

Furthermore, the executive directors are responsible for the preparation of the management report that as a whole provides an appropriate view of the Company's position and is, in all material respects, consistent with the annual financial statements, complies with German legal requirements, and appropriately presents the opportunities and risks of future development. In addition, the executive directors are responsible for such arrangements and measures (systems) as they have considered necessary to enable the preparation of a management report that is in accordance with the applicable German legal requirements, and to be able to provide sufficient appropriate evidence for the assertions in the management report.

The supervisory board is responsible for overseeing the Company's financial reporting process for the preparation of the annual financial statements and of the management report.

Auditor's Responsibilities for the Audit of the Annual Financial Statements and of the Management Report

Our objectives are to obtain reasonable assurance about whether the annual financial statements as a whole are free from material misstatement, whether due to fraud or error, and whether the management report as a whole provides an appropriate view of the Company's position and, in all material respects, is consistent with the annual financial statements and the knowledge obtained in the audit, complies with the German legal requirements and appropriately presents the opportunities and risks of future development, as well as to issue an auditor's report that includes our audit opinions on the annual financial statements and on the management report.

Reasonable assurance is a high level of assurance, but is not a guarantee that an audit conducted in accordance with Section 317 German Commercial Code (HGB) and the EU Audit Regulation and in compliance with German Generally Accepted Standards for Financial Statement Audits promulgated by the Institut der Wirtschaftsprüfer (IDW) will always detect a material misstatement. Misstatements can arise from fraud or error and are considered material if, individually or in the aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of these annual financial statements and this management report.

We exercise professional judgment and maintain professional scepticism throughout the audit. We also

- identify and assess the risks of material misstatement of the annual financial statements and of the management report, whether due to fraud or error, design and perform audit procedures responsive to those risks, and obtain audit evidence that is sufficient and appropriate to provide a basis for our audit opinions. The risk of not detecting a material misstatement resulting from fraud is higher than for one resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal controls.

- obtain an understanding of internal control relevant to the audit of the annual financial statements and of arrangements and measures relevant to the audit of the management report in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an audit opinion on the effectiveness of these systems of the Company.
- evaluate the appropriateness of accounting policies used by the executive directors and the reasonableness of estimates made by the executive directors and related disclosures.
- conclude on the appropriateness of the executive directors' use of the going concern basis of accounting and, based on the audit evidence obtained, whether a material uncertainty exists related to events or conditions that may cast significant doubt on the Company's ability to continue as a going concern. If we conclude that a material uncertainty exists, we are required to draw attention in the auditor's report to the related disclosures in the annual financial statements and in the management report or, if such disclosures are inadequate, to modify our respective audit opinions. Our conclusions are based on the audit evidence obtained up to the date of our auditor's report. However, future events or conditions may cause the Company to cease to be able to continue as a going concern.
- evaluate the overall presentation, structure and content of the annual financial statements, including the disclosures, and whether the annual financial statements present the underlying transactions and events in a manner that the annual financial statements give a true and fair view of the assets, liabilities, financial position and financial performance of the Company in compliance with German Legally Required Accounting Principles.
- evaluate the consistency of the management report with the annual financial statements, its conformity with German law, and the view of the Company's position it provides.
- perform audit procedures on the prospective information presented by the executive directors in the management report. On the basis of sufficient appropriate audit evidence we evaluate, in particular, the significant assumptions used by the executive directors as a basis for the prospective information, and evaluate the proper derivation of the prospective information from these assumptions. We do not express a separate audit opinion on the prospective information and on the assumptions used as a basis. There is a substantial unavoidable risk that future events will differ materially from the prospective information.

We communicate with those charged with governance regarding, among other matters, the planned scope and timing of the audit and significant audit findings, including any significant deficiencies in internal control that we identify during our audit.

We also provide those charged with governance with a statement that we have complied with the relevant independence requirements, and communicate with them all relationships and other matters that may reasonably be thought to bear on our independence, and where applicable, the related safeguards.

From the matters communicated with those charged with governance, we determine those matters that were of most significance in the audit of the annual financial statements of the current period and are therefore the key audit matters. We describe these matters in our auditor's report unless law or regulation precludes public disclosure about the matter.

Other Legal and Regulatory Requirements

Further Information pursuant to Article 10 of the EU Audit Regulation

We were elected as auditor by the annual general meeting on 27 April 2017. According to the resolution of the Supervisory Board on the appointment pursuant to Section 11 (2) no. 1 of the Statutes of Bayerische Landesbank AöR, we were engaged by the supervisory board in its confirmation dated 17 July 2017. We have been the auditor of Bayerische Landesbank AöR, Munich, without interruption since the financial year 2012.

We declare that the audit opinions expressed in this auditor's report are consistent with the additional report to the audit committee pursuant to Article 11 of the EU Audit Regulation (long-form audit report).

German Public Auditor Responsible for the Engagement

The German Public Auditor responsible for the engagement is Herbert Apweiler.

Munich, 19 March 2018

Deloitte GmbH
Wirtschaftsprüfungsgesellschaft

(Löffler)
(Wirtschaftsprüfer)
German public auditor

(Apweiler)
(Wirtschaftsprüfer)
German public auditor

Supplementary information

Financial measures not calculated in accordance with HGB

For its entire financial reporting and other documents it publishes, BayernLB uses financial measures not calculated in accordance with accounting standards governed by the German Commercial Code. These measures indicate historical or future financial performance, financial position and cash flows derived from the financial statements prepared in accordance with the relevant accounting framework.

They should be seen as a supplement to and not a replacement of the figures calculated in accordance with the accounting standards governed by the German Commercial Code. Readers of the financial reports and other documents containing these measures should be aware that similarly named financial measures published by other companies may have been calculated differently.

BayernLB uses the following financial measures not calculated in accordance with accounting standards governed by the German Commercial Code:
- Return on equity (RoE)
- Cost/income ratio (CIR)

The RoE and CIR are important financial performance indicators. They provide information about profitability and are used by BayernLB to manage it.

Return on equity (RoE)

RoE is calculated on the basis of internal management information by dividing gains or losses on ordinary activities by average regulatory capital. In financial year 2016, the RoE calculation was modified by adjusting gains or losses on ordinary activities by a risk buffer reported pursuant to section 340e para. 4 HGB and by other taxes, unless disclosed under other operating expenses. This adjustment ceased to be made from 1 January 2017. The previous year was adjusted accordingly. As a result of this changeover, the calculation method strictly follows the breakdown of the income statement defined under the German Ordinance Regulating Accounting for Financial Institutions and Financial Service Providers (RechKredV). To determine the "average regulatory capital", the average Common Equity Tier 1/CET1 capital available over the financial year is used.

RoE reconciliation calculation

EUR million	**2017**	**2016**
Gains or losses on ordinary activities	397	415
Average regulatory capital (CET1)	8,261	8,675
RoE (%)	4.8	4.8[1]

1 Previous year's value adjusted.

Cost/income ratio (CIR)

The CIR is determined by dividing administrative expenses – adjusted for the expenses for the bank levy and deposit guarantee scheme, plus amortisation, depreciation and writedowns on intangible assets and tangible assets – by the sum of gross profit, net income or net expenses of the trading portfolio and the net of other operating income, expenses, and other taxes. Gross profit corresponds to the sum of interest income, interest expenses, current income, income from profit-pooling agreements, profit transfer agreements and partial profit transfer agreements, commission income and commission expenses. In financial year 2016, the net income of the trading portfolio was adjusted by the addition to the fund for general bank risks in accordance with section 340e para. 4 HGB. This adjustment ceased to be made from 1 January 2017. The previous year was adjusted accordingly. As a result of this changeover, the calculation method strictly follows the breakdown of the income statement defined under the German Ordinance Regulating Accounting for Financial Institutions and Financial Service Providers (RechKredV).

CIR reconciliation calculation

EUR million	2017	2016
Administrative expenses	**–872**	**–825**
Expenses for the bank levy and deposit guarantee scheme	**64**	**60**
Amortisation, depreciation and writedowns on intangible assets and tangible assets	**–27**	**–47**
Gross profit	**904**	**1,209**
• Interest income	2,004	2,195
• Interest expenses	–1,303	–1,478
• Current income	13	23
• Income from profit-pooling agreements, profit transfer agreements and partial profit transfer agreements	14	274
• Commission income	229	249
• Commission expenses	–53	–54
Net income or net expenses of the trading portfolio	**116**	**98**
Net of other operating income, expenses and other taxes	**–12**	**180**
CIR (%)	**82.8**	**54.6**[1]

1 Previous year's value adjusted.

BayernLB 2017 Annual Report and Accounts

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The Annual Report can be downloaded as a pdf file
from www.bayernlb.com/ir.
It is also available in German.

The translation of the annual financial statements, comprising the balance sheet, the income statement and the notes to the financial statements, together with the management report and the report by the Supervisory Board of Bayerische Landesbank as well as the auditor's report is for convenience only; the German versions prevail.

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