

# Sustainable Investments

A Research Publication by DZ BANK AG

## Sustainability in focus: Deutsche Hypo plans to issue a "Green Pfandbrief" (Green Covered Bond)

**The facts:** Deutsche Hypo announced on 25 October 2017 that it intends to issue a Euro-denominated "Green Pfandbrief" (Green Covered Bond) in a volume of EUR 500 million. The proceeds from the "Green Pfandbrief" are used exclusively to finance assets in accordance with Deutsche Hypo's Green Bond Framework. This is financing energy-efficient buildings (Green Buildings) such as new buildings, replacements of old buildings, project developments, certified portfolio financing and renovation work to improve a building's energy efficiency.

**Sustainability assessment:** Deutsche Hypo achieves 57 points in our "EESG" rating model (average for the entire universe: 44 points; sector sustainability threshold: 52 points), is classified as "sustainable", and has received the DZ BANK Seal of Quality for Sustainability 10/2017 accordingly. Our model calculates a positive economic sustainability factor of 1.05. In the first half of 2017, Deutsche Hypo reported stable profitability and a continued good risk position in its core business area of commercial real estate financing, growing new business by 17.4% year-on-year despite a competitive situation that remains challenging. Sustainability is anchored within Deutsche Hypo's operating business on both the asset and liability sides. The bank offers a number of products and services with ecological and/or social use or benefit. Stringent sustainability criteria are applied within the core business, commercial real estate financing. For this purpose, the bank evaluates investments according to financial, building-law and ecological aspects as part of risk management. The sustainability topic is strategically anchored at Managing Board level at Deutsche Hypo. To this end, the Managing Board has declared the professionalisation of sustainability management as a central objective within the bank. The sustainability management function, which is situated within the communications department and forms part of the Managing Board's staff, is responsible for implementing this aim. It is supported by a sustainability group consisting of members of the bank's departments that have more extended involvement with sustainability.

**Conclusion:** Deutsche Hypo exhibits above-average performance in all four of the sustainability dimensions we analyse. Evaluating ecological, social and long-term economic impacts of products and services forms an essential role in appraising issuers in our "EESG" analysis model. Refinancing loans within their sustainability strategy through issuing a sustainable bond would exert a positive impact on the "Sustainability in the operating business" core indicator we analyse. Especially the economic sub-indicators of "Socially responsible financing and funding" and "Contribution of products and services to the Sustainable Development Goals" are impacted positively. This analysis is not connected with any assessment of the bond itself.

## SECURITIES

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### Authors:

Marcus Pratsch, ANALYST  
Marcus.Pratsch@dzbank.de

Matthias Dürr, ANALYST  
Matthias.Duerr@dzbank.de

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## SUSTAINABILITY ASSESSMENT:

### Sustainability at a glance

Deutsche Hypo achieves 57 points in our EESG rating model. The average for the entire universe currently amounts to 44 points. The sector sustainability threshold for banks lies at 52 points at present. Deutsche Hypo does not violate exclusion criteria and is not involved in any severe EESG controversies. Accordingly, Deutsche Hypo is classified as "sustainable" and has received the DZ BANK Seal of Quality for Sustainability 10/2017. Our model calculates a positive economic sustainability factor of 1.05.

**EESG score 57/100 points**  
**Classification: Sustainable**

#### DZ BANK SEAL OF QUALITY FOR SUSTAINABILITY



Source: DZ BANK Sustainable Investment Research (2017)

#### SUSTAINABILITY RATING (EESG)

Sustainability Rating (EESG)	57/100
Peer Group	Banks
Sector-specific sustainability threshold	52
Cross-sector sustainability threshold	44
Violation of exclusion criteria	No
Current, serious EESG controversies	No
Part of DZ BANK Sustainable Investment Universe	Yes

Source: DZ BANK Sustainable Investment Research (2017)

## Sustainability SWOT

Strengths	Weaknesses
German real estate bank with European orientation and presence at important national and international locations	Management compensation is not (yet) explicitly tied to sustainability targets
The business model is based on the German Covered Bond Act (PfandBG), including in joint liability with German regional banks (Landesbanken) and saving banks (Sparkassen)	
Established capital market business	
Positive ecological, social and economic impact of products and services	
Sustainability topic strategically anchored at top management level	
Opportunities	Risks
Broadening of investor base through regular Green Bond issues	Unexpected defaults in commercial real estate finance area
Positive contribution to Sustainable Development Goals and global climate targets	Stronger than expected margin pressure in commercial real estate financing and rising loan-to-value ratios in new business
Further increase in real estate prices and rise in transaction volumes	End of positive real estate cycle
	Potential change of owner

Source: DZ BANK Sustainable Investment Research (2017)

## GREEN BOND AT A GLANCE

### Facts about the issue

Deutsche Hypo announced on 25 October 2017 that it intends to issue a Euro-denominated “Green Pfandbrief” (Green Covered Bond) in a volume of EUR 500 million.

**Volume: EUR 500 million**

The issue proceeds from the “Green Pfandbrief” are to be used exclusively to finance assets in accordance with Deutsche Hypo’s Green Bond Framework.

**Green Bond Framework**

### Refinancing products

When issuing Green Bonds, Deutsche Hypo funds itself through bonds whose raised funds are used exclusively to finance energy-efficient (i.e. green) buildings, such as new buildings, replacements of old buildings, project developments, certified portfolio financing and renovation work to improve a building’s energy efficiency.

**In focus: Green Buildings**

The Bank issues unsecured bonds as well as Pfandbriefe as green bonds. The Pfandbriefe it issues fulfil all requirements under the German Pfandbrief Act. Senior unsecured bonds issued as green bonds are pari passu with other bonds of the same asset class, which may include issues in benchmark format as well as smaller volumes (private placements).

**Unsecured bonds / Covered bonds (Pfandbriefe)**

An adequate volume of suitable Green Buildings is available for the issued bonds. Funding by way of green bonds may only be carried out to the minimum extent that the Bank has Green Buildings in its portfolio. Temporary fractional amounts can be invested on a temporary/adequate basis.

**Adequate volume of Green Buildings**

### Use of proceeds

The funds raised through the issue of Green Bonds are used exclusively to finance energy-efficient real estate.

**Energy-efficient real estate**

The proceeds can be used to finance Green Buildings both in new business and in existing business. Financing is geared towards the construction, project development, acquisition or energy-efficient renovation of buildings. The exact use of the proceeds is defined in the final terms of the respective bond issue.

**New and existing buildings**

### Eligible projects

The energy efficiency of a property to be financed, and therefore its suitability as an asset for a Green Bond, is evaluated in a multi-stage process. The requirements derived from the process in relation to acquisition, loan processing and Treasury are embedded in Deutsche Hypo’s guidelines and are therefore binding for all employees.

**Multi-stage evaluation process**

The suitability of a financing for a Green Bond issue and the related features, such as quantified energy efficiency, are recorded and managed in the Bank’s portfolio management system. The employees in the lending department (Credit Management) record all the necessary data (such as energy passes, certificates, etc.) of the financing in the Bank’s IT systems. On the basis of defined criteria, using

**Credit management and treasury**

the four eyes principle, Treasury will then review whether the financed real estate is suitable for inclusion in the real estate portfolio for a Green Bond issue.

The applicable criteria are determined by a Green Building Commission which is comprised of members of the sustainability circle that supports the sustainability management team in its tasks. The Green Building Commission defines the Green Bond Minimum Standards (short: GBMS) and ensures in its regular meetings that the minimum standards required in the target markets are at least complied with. An asset is categorised as a Green Building if the applicable GBMS are fulfilled at the time of inclusion of the financing in the Green Bond portfolio.

### Green Building Commission

The currently applicable GBMS are as follows:

### Green Bond Minimum Standards

- Energy pass with a maximum final energy demand or consumption (heat) in kWh/(m<sup>2</sup>\*a) by asset class:
  - 50 kWh/(m<sup>2</sup>\*a) for new residential properties
  - 75 kWh/(m<sup>2</sup>\*a) for old residential properties
  - 30 kWh/(m<sup>2</sup>\*a) for logistics buildings
  - 70 kWh/(m<sup>2</sup>\*a) for retail buildings (shopping malls, department stores)
  - 95 kWh/(m<sup>2</sup>\*a) for other retail buildings
  - 95 kWh/(m<sup>2</sup>\*a) for hotel buildings (up to 3 star hotels)
  - 105 kWh/(m<sup>2</sup>\*a) for hotel buildings (4 to 5 star hotels)
  - 110 kWh/(m<sup>2</sup>\*a) for production and storage buildings (with heating)
  - 110 kWh/(m<sup>2</sup>\*a) for office buildings without air conditioning
  - 135 kWh/(m<sup>2</sup>\*a) for office buildings with air conditioning
- or green building certification:
  - LEED Silver or above
  - BREEAM Good or above
  - DGNB Silver or above (for certificates given after 1 July 2015: Gold or above)
  - HQE Basic or above

The primary energy demand or consumption (warmth) should be used for valuation if the use of renewable energy reduces the primary energy demand or consumption to below the final energy figure.

### Rules for utilising renewable energies

In addition, real estate belonging to customers from business areas considered to be controversial may not be financed. This criterion is also a strict additional condition of Deutsche Hypo's business strategy and is embedded in Deutsche Hypo's sustainability programme.

### No financing of properties for customers from controversial business areas

An additional condition for the use of Green Buildings is that the financed real estate is only leased to uncontroversial main tenants. The property will be excluded from the portfolio of suitable Green Buildings should it become known that a main tenant operates in a controversial business.

**Rental exclusively to uncontroversial main tenants**

## Monitoring

The suitability of green assets in the portfolio for Green Bond issues is reviewed by Treasury employees on a regular basis and flagged in Deutsche Hypo's portfolio system.

**Treasury regularly reviews portfolio**

Unsuitable financings and the underlying assets are replaced by new financings or assets. A financing and its underlying assets are considered unsuitable if it becomes known that a main tenant is involved in an area of business that is considered to be controversial or if the energy pass or sustainability certificate expires.

**Ineligible financing facilities are replaced by new financing facilities or assets**

Deutsche Hypo has set itself the requirement that the real estate suitable for a Green Bond issue must at least correspond to the volume of the green bond that has been issued or is to be issued. If it is not possible to directly use the proceeds from Green Bonds to finance energy-efficient real estate in accordance with this framework, they must be immediately invested with a credit institution with a sufficiently positive rating granted by a recognised sustainability rating agency (here: oekom research AG with at least Prime Status) on an interim basis.

**Real estate portfolio eligible for Green Bonds must at least correspond to the volume of Green Bonds issued/to be issued**

## Reporting

Each year, Deutsche Hypo publishes a Green Bond report on its website. The report contains the following information:

**Scope of Green Bond reporting**

- Current volume of the Green Building inventory
- CO<sub>2</sub> reduction of all Green Buildings compared to the relevant average
- Characterisation of Green Buildings to property certifications, location, sustainability aspects, etc.

## SUSTAINABILITY IN THE OPERATING BUSINESS

### Sustainability affects both the asset and liability businesses

Through a systematic approach, Deutsche Hypo ensures that material sustainability aspects are integrated into both the asset and liability businesses of the bank:

#### Systematic approach

- Transactions that identifiably infringe fundamental sustainable development principles such as in connection with controversial business fields like weapons or pornography are identified and declined on the basis of exclusion criteria.
- A framework of sustainability guidelines establishes the connection between individual transactions and the specific sustainability standards that Deutsche Hypo regards as relevant, such as the German Sustainability Code for the UN Global Compact. This approach integrates sustainability in a targeted and individual manner.

### Products and services with social use

When calculating the monetary value of products and services with social use or benefit, Deutsche Hypo takes into consideration the direct and indirect contributions that the core business generates for clients and society.

#### Taking direct and indirect income from the core business into account

In the social sustainability area, Deutsche Hypo has reported its lending business with clients whose business activities are of particular public interest. The following sectors are identified at Deutsche Hypo in accordance with the Bundesbank's sector key:

#### Identified sectors

- Land and residential real estate
- Education and training
- Healthcare
- Residential homes (e.g. care homes)
- Manufacturing of food and animal feed

Deutsche Hypo has committed financing volume in these sectors of around EUR 12.1 billion as of the 31 December 2016 reporting date.

#### Financing volume at the end of 2016: EUR 12.1 billion

### Products and services with ecological use

By way of analogy with social use or benefit, Deutsche Hypo has identified lending business with ecological use or benefit for the following sectors:

#### Identified sectors

- Waste disposal
- (Mechanical and plant) engineering

Deutsche Hypo has committed financing volume in these sectors of around EUR 105 billion as of the 31 December 2016 reporting date.

#### Financing volume at the end of 2016: EUR 105 billion

## ESG guidelines

Along with existing guidelines at Deutsche Hypo to implement and comply with the guidelines of "classic" banking supervision as well as other civil law and tax law regulations at German, European and international level, further guidelines exist in the bank to direct and regulate business activity in relation to the growing consideration given to economic, ecological and social aspects.

These so-called ESG guidelines supplement existing strategy and governance guidelines and principles, enabling the portfolio to be managed on a comprehensive basis. The Managing Board approves all ESG guidelines, making them binding for all staff as a consequence. An external audit is not conducted.

The purposes served by the ESG guidelines include avoiding ESG risks. Deutsche Hypo defines ESG risks as risks that can arise due to corporate management, or social or ecological aspects as part of a business transaction or business relationship. ESG risks count as operational risks in this context.

As part of its business activities, Deutsche Hypo examines certain engagements according to ESG perspectives, to identify business and reputation risks in the interests of clients and the bank at an early juncture. Like other risks, potential ESG risks are evaluated as part of the credit process, and are included in the overall vote for the business as soon as they arise or are identifiable.

The starting point to assess risk potential is formed by the specialist expertise and experience of staff, the ESG guidelines, and the regulations underlying the guidelines. Where required, unclear business transactions or potentially unclear effects of business transactions are passed to the Reputation Committee for further appraisal.

Deutsche Hypo has established a Reputation Committee to optimise the management of reputation risks in the real estate financing area. This committee is convened if the bank becomes aware of information of potential relevance to its reputation that can lead, or has led, to significant business losses and/or damage to the bank's image. Along with the compliance officer, the Reputation Committee consists of departmental heads from personnel and law, credit risk management, communications and the staff of the Managing Board, as well as the divisional head of the market area that is affected.

## Guidelines for real estate financing

As a bank specialising in covered bonds and real estate, Deutsche Hypo bears a particular responsibility to support its customers in constructing, acquiring and operating real estate whose value is also secured through taking ecological and social criteria into consideration.

To appropriately fulfil this mandate and reduce borrowing costs, a set of guidelines specifies the inclusion of sustainability aspects in the core business, commercial real estate financing. Sustainability aspects are integrated into the risk assessment of the property. If sustainable planning exists for a property, the risk of vacancy is lower, for example. For the sustainable core business, the bank evaluates investments according to financial, building law and ecological aspects as part of risk

**Financing volume at the end of 2016:  
EUR 105 billion**

**Supplementing existing guidelines  
and principles in relation to strategy  
and governance**

**Avoiding ESG risks**

**Identifying business and reputation  
risks**

**Avoiding ESG risks**

**Reputation Committee in the real  
estate financing area**

**Property values to be secured  
through taking ecological and social  
criteria into account**

**Guidelines: taking sustainability  
aspects into consideration in the  
core business**



management. The best possible financing solution is then developed together with the customer.

Financing energy-efficient buildings as part of the commercial real estate financing business area represents the core aspect here. By financing such Green Buildings, the bank aims to actively contribute to the reduction of greenhouse gases.

### Financing Green Buildings

Deutsche Hypo founded the "Green Buildings" working group to quantify sustainable aspects, among other purposes. Development projects earmarked for certification comprised 50 percent of all commitments as of 31 December 2016 (previous year: 36 percent). This percentage rate is subject to natural fluctuations, as the number of development projects and related property types can vary significantly from year to year.

### Green Buildings working group

## Financing guidelines for controversial business areas

The guidelines on the controversial business areas regulate or prohibit the arrangement of business relationships with arms industry companies and companies that produce pornography.

### Controversial business areas

Financing facilities relating to the arms industry are subject to stringent regulations. The weapons and armaments industry is not a business area forming part of Deutsche Hypo's core business. Furthermore, Deutsche Hypo only finances customers relating to weapons and armaments that serve the defence and security of the liberal and democratic constitutional order of the Federal Republic of Germany, and which are earmarked for the fulfilment of international agreements.

### Arms industry

Business relationships with companies that produce and trade in pornography as well as with companies that are related to this sector are prohibited.

### Pornography

The ESG guidelines for sectors and banking areas are always developed together with staff from the specialist areas. Awareness about the ESG guidelines is raised in the relevant areas. Processes are further evolved and adapted to current developments as part of an annual quality test.

### Continuous further development of guidelines

## Sustainable refinancing

Funding is also structured on an ecologically sustainable basis. Through issuing Green Bonds, Deutsche Hypo also aims to meet the objectively measurable growth in investor demand for ecologically sustainable investments.

### Ecologically sustainable funding

With the issuing of Green Bonds, the bank, as a financial intermediary, endeavours to meet our society's target of reducing global warming.

### Contribution to climate targets

## ISSUER PROFILE

### Issuer at a glance

Deutsche Hypo was founded in 1872 by Berlin-based merchants and bankers as the Deutsche Hypothekenbank (Actien-Gesellschaft).

**Founded in 1872**

The bank's head office with its approximately 400 staff is located in Hannover. Deutsche Hypo is also present in Berlin, Hamburg, Düsseldorf, Frankfurt and Munich, as well as in Amsterdam, London, Paris, Madrid and Warsaw. It sees itself as a German real estate bank with a European orientation, supporting its clients in the strategic target markets of Germany, the United Kingdom, France, Benelux, Spain and Poland.

**German real estate bank with a European orientation**

Deutsche Hypo's main business activities can be divided into two business areas.

**Two business areas**

Commercial real estate financing forms the bank's core business area with a more than 80% share of the bank's total interest and commission results. This area includes all real estate financing for clients that generate most of their cash flow from real estate or regularly realise significant real estate investments.

**Core business area:  
Commercial real estate financing**

The second business area, the capital market business, includes securities, deposits and derivatives business with banks, as well as refinancing. This area also (still) includes the government financing business, whose portfolio has been undergoing continuous reduction for some years.

**Capital market business**

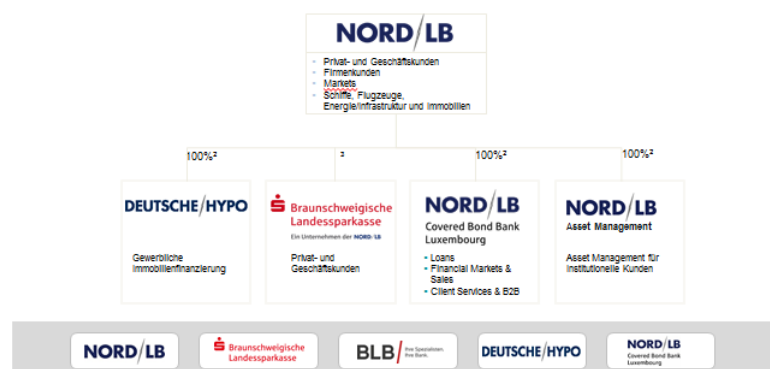
As a company owned by Norddeutsche Landesbank Girozentrale, Deutsche Hypo forms the expertise centre for commercial real estate financing within the Group. This also includes its role as a significant issuer of mortgage bonds within the NORD/LB Group. In addition, the bank refinances itself through unsecured debt securities. The aim at all times is to possess long-term stable refinancing capability on competitive terms.

**Expertise centre for commercial real estate financing in the NORD/LB Group**

Deutsche Hypo comprises a strategic interest of NORD/LB as a wholly owned subsidiary, and is included in its consolidated financial statements.

**Strategic interest of NORD/LB**

### STRUCTURE OF THE NORD/LB GROUP



Source: NORD/LB (2017)

## Strategy and sustainable governance

### » Strategy

Deutsche Hypo performs its tasks based on its corporate principles. The bank has also introduced management principles to supplement these corporate principles.

**Corporate principles supplemented by management principles**

The bank's main corporate objectives include:

**Significant corporate objectives**

- the sustainable securing and enhancing of corporate value, profitability and profit transfer, including through an appropriate return on equity by the bank and the Group,
- strengthening the business model through diversifying the earnings base and expanding competences, including through boosting RWA-dependent income and limiting risk through a granular portfolio,
- optimally serving customer requirements,
- securing refinancing and liquidity at all times,
- promoting employee performance and loyalty.

Deutsche Hypo regards sustainability as an important element of its business model. Its aim is to structure the bank to be sustainably profitable, thereby securing profitability and jobs for coming generations.

**Sustainability as an important element of the business model**

Deutsche Hypo has identified a total of five sustainability action areas, thereby assigning them strategic focus:

**Five sustainability action areas**

- Governance
- Customers and investors
- Employees
- Society
- Environment.

Deutsche Hypo's sustainability strategy addresses central aspects of global change for the bank as well as for its customers and investors, and shows how the resultant opportunities can be efficiently realised and risks can be managed responsibly.

**In focus: global change**

Here, Deutsche Hypo pays attention with differing degrees of urgency and intensity to long-term trends relating to topics such as climate change, demographic shift, the urbanisation process or raw material shortages, to adjust tried and tested business models at an early juncture and regularly to align with these trends' complex effects, and to create corresponding solutions.

**Identifying trends and effects, and creating solutions**

## » Sustainable Governance

The Deutsche Hypo Managing Board has declared the professionalisation of sustainability management as a central objective within the bank.

Responsibility for the implementation of this objective lies with the sustainability management function, which is situated within the communications department and forms part of the Managing Board's staff. This comprises one of the main areas of activities of this area. Responsibilities of the sustainability management function include implementing sustainability standards, coordinating sustainability measures and further developing the sustainability strategy.

The sustainability management function is supported by a sustainability group consisting of members of departments of the bank that have greater involvement with sustainability. Its members derive from the following departments: communications and the staff of the Managing Board, domestic lending, credit department and real estate valuation, credit risk management, organisation and IT, personnel and law, treasury, corporate development and corporate steering.

The sustainability group supports the sustainability management function in identifying sustainability topics, develops target measures, and proposes them to the Managing Board for implementation. The members also support the implementation of the measures in their respective areas. Since it was founded, the sustainability group has met at least once every quarter, discussing and developing sustainability topics at overall bank level.

The individual areas and the sustainability management function also hold regular bilateral discussions at which they jointly develop new topics. As occasion requires, these are then proposed to the Managing Board for implementation.

### Anchoring sustainability at the level of the Managing Board

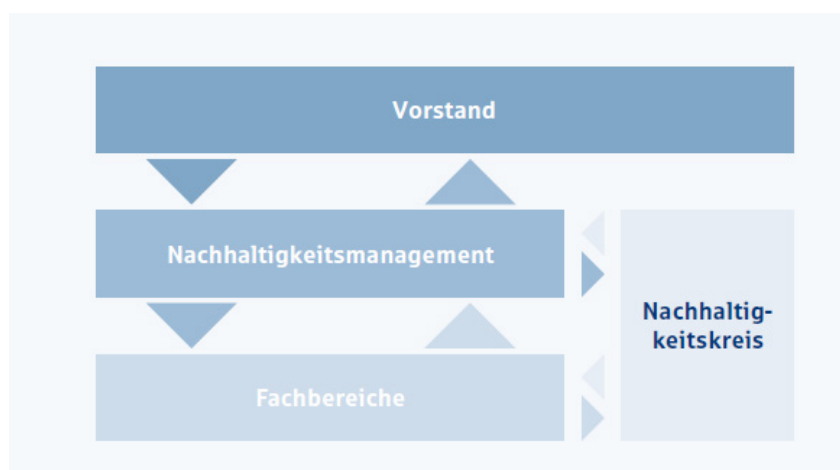
### Sustainability management

### Sustainability group ...

### ... supports sustainability management in identifying sustainability topics

### Bilateral discussions with individual areas of the bank

#### ORGANISATIONAL STRUCTURE OF SUSTAINABILITY MANAGEMENT



Source: Deutsche Hypo (2017)

Deutsche Hypo conducts dialogue with relevant stakeholder groups (including sustainability rating agencies) to generate new ideas for the orientation of its sustainability management function. This ensures that corporate activity is structured in accordance with the interest groups' requirements, thereby securing long-term

### Regular stakeholder dialogue

success and competitiveness. The results from these stakeholder dialogues are integrated into the sustainability programs, giving Deutsche Hypo impulses for the orientation of its sustainable activities.

## » Sustainability-related principles, guidelines and initiatives

For Deutsche Hypo as a financial services company, taking into consideration the ten internationally recognised principles of the UN Global Compact deriving from the aspects of human rights, labour, environment and anti-corruption, forms an important element of responsibility for its clients and employees, and as a "corporate citizen" for society.

**UN Global Compact**

As a subsidiary of NORD/LB – a signatory to the UNEP Statement Commitment – Deutsche Hypo is also oriented to the Finance Initiative, and is consequently committed to sustainable development, forward-looking environmental management, and open communications in relation to the promotion of environmental aspects.

**UNEP Statement of Commitment**

With its membership in the German Property Federation (ZIA), Deutsche Hypo is voluntarily committed as part of its corporate real estate activities to the ZIA Sustainability Guidelines: "Sustainability in the Real Estate Sector – Code of Conduct, Reports and Compliance".

**ZIA Sustainability Guidelines**

Deutsche Hypo prepares its annually published sustainability report in compliance with the guidelines of the Global Reporting Initiative (GRI).

**Global Reporting Initiative**

Deutsche Hypo is committed to the German Sustainability Code, a transparency standard for corporate sustainability management.

**German Sustainability Code**

Through signing the Diversity Charter, Deutsche Hypo wishes to advance the recognition, appreciation and inclusion of diversity in corporate culture in Germany – irrespective of gender, nationality, ethnic origin, religion or worldview, handicap, age, sexual orientation and identity.

**Diversity Charter**

## Operating trends

In a market environment that continued to be characterised by high demand for real estate as well as a highly competitive commercial real estate lending market, Deutsche Hypo grew its commitment volumes both in Germany and abroad.

**High competitive intensity**

In the first half of 2017, the bank grew its new business volume to EUR 2.116 billion, representing 17.4% year-on-year growth. With a 62.1% share (previous year: 60.6%), the geographic focus of new business remained in Germany (and especially on office and retail properties in Germany).

**New business volume growth with geographic focus on Germany**

Overall, the real estate financing portfolio reported 3% growth compared with the end of 2016.

**Slight growth in real estate financing portfolio**

Total assets were down by -3% compared with the end of the previous year to EUR 24.4 billion (Dec 31, 2016: EUR 25.2 billion). The background to this is the continuation of the strategic portfolio downsizing in the capital market business, reflected in reductions in local government loans as well as third-party securities. This trend arises mainly from scheduled maturities. Individual disposals were also realised as part of active portfolio management.

**Reduction in total assets due to continued strategic portfolio downsizing in the capital market business**

Overall, Deutsche Hypo increased its result from normal operations by 4.5% to EUR 35.2 million in the first half of 2017 (previous year: EUR 33.7 million). The earnings growth reflected a reduction in net interest income of -3.2% to EUR 98.6 million, a positive earnings contribution from the capital market business of EUR 2.9 million (previous year: EUR -10.9 million), an improvement in the risk result of EUR -19.5 million (previous year: EUR -25.5 million) and an 8% rise in administrative expenses to EUR 46 million.

**Growth in result from normal operations**

Equity as reported on the balance sheet reduced year-on-year from EUR 913 million to EUR 838 million due to the repayment as of the balance sheet date of the silent partners' capital that was already discontinued in the previous financial year. Due to the control and profit transfer agreement, Deutsche Hypo transfers all its earnings to NORD/LB.

**Reduction in reported equity**

As far as regulatory equity backing is concerned, Deutsche Hypo utilises the waiver regulation whereby the obligations to file an individual bank report as well as to comply with requirements in terms of equity and equity backing do not apply. The bank nevertheless calculates an equity ratio that takes into consideration all existing capital components in line with regulatory provisions. A total of EUR 1.1546 billion (previous year: EUR 1.1824 billion) was eligible for regulatory equity backing in accordance with the regulatory provisions. The slight reduction in equity was offset by a 4.9% decrease in risk-weighted assets. Consequently, the equity ratio reported a slight increase to 19.4% as of 30 June 2017 (previous year: 18.9%).

**Improvement in equity ratio**

## EESG ANALYSIS METHODOLOGY OF DZ BANK SUSTAINABLE INVESTMENT RESEARCH

### Concept of DZ BANK Sustainable Investment Research

The aim of the DZ BANK Sustainable Investment Research was to develop an analysis methodology for issuers which in terms of a long-term sustainability assessment (as opposed to traditional short-term credit assessment and fundamental analysis) corrects the shortcomings in both traditional ratings and available sustainability ratings on the market. The rating graduations do not represent a rating category within the meaning of the EU Rating Regulation.

The result is an integrated, four-dimensional EESG analysis model.

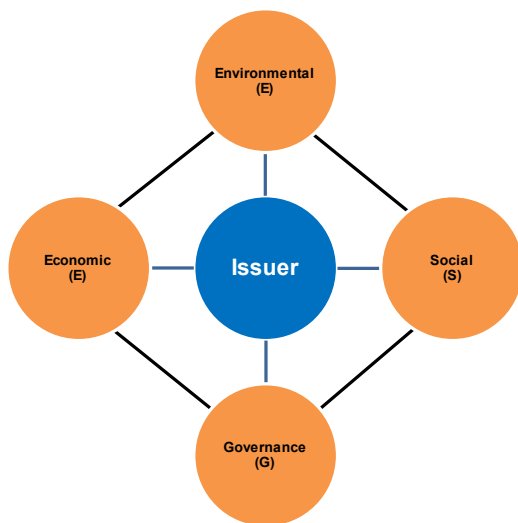
DZ BANK Sustainable Investment Research takes the view that these four sustainability dimensions should not be seen in isolation, but rather in a joint context, as the sub-disciplines influence one another.

Correct the shortcomings in traditional ratings and available ESG ratings on the market

EESG analysis model

Four interacting sustainability dimensions

### DIMENSIONS OF DZ BANK SUSTAINABLE INVESTMENT RESEARCH



Source: DZ BANK Sustainable Investment Research (2016)

On the one hand, in contrast to traditional financial ratings, the integrated sustainability concept of DZ BANK Sustainable Investment Research includes Environment (E), Social (S) and Governance (G) aspects which are important for issuers' long-term and sustainable development and may have an impact on their stability and credit rating.

On the other hand, as opposed to the available sustainability ratings on the market, the concept goes beyond a purely ESG approach, i.e. an exclusive analysis of ecological, social and governance factors, as sustainability is an investment matter and current and future economic success is also a core consideration for every issuer. Moreover, every investor's goal is to achieve a return. This also applies to

Traditional sustainability dimensions E, S and G ...

... are supplemented by an economic sustainability dimension (E)

investors who are purely interested in sustainability. Therefore, the integration of the economic perspective (E) in the sustainability analysis is crucial.

In comparison to traditional financial analysis, the long-term aspect is even more at the forefront of sustainability analysis, as economic sustainability postulates that current society, and therefore also issuers as part of this society, should not live beyond their means so as to rule out losses for future generations.

**Economic sustainability analysis:  
long-term orientation**

Furthermore, the sustainability concept of DZ BANK Sustainable Investment Research takes into consideration the fact that sustainability is not a rigid construct, but rather a complex, dynamic process. The subjects of the analysis develop dynamically over time, in that an issuer who is currently classified as sustainable may already no longer be classified as sustainable in the next evaluation, or vice versa.

**Sustainability as a complex,  
dynamic investment process**

The analysis methodology of DZ BANK Sustainable Investment Research is based on the principle of materiality. It is not focused solely on internal guidelines, rules, processes or strategies, but also includes ecological, social and long-term economic effects, i.e. the impact, of products and services when evaluating an issuer.

**Materiality**

**Impact of products and services**



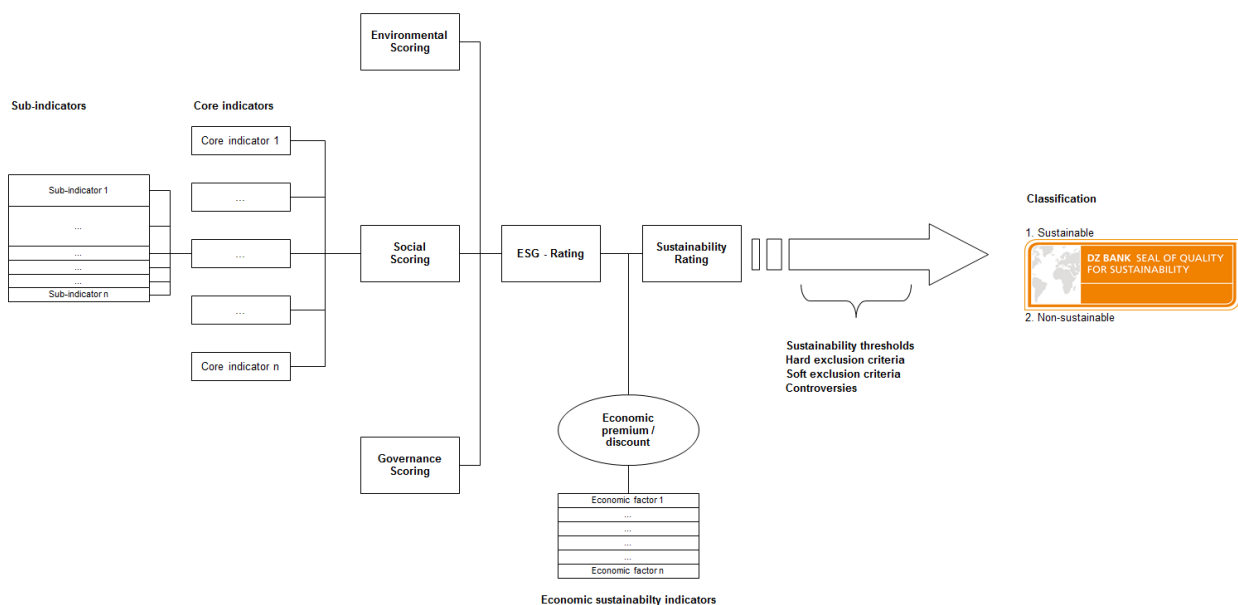
## Methodology of DZ BANK's sustainability rating

The sustainability rating of DZ BANK Sustainable Investment Research is the result of a **Integrated sustainability analysis ...** multi-stage, integrated analysis process. In addition to the specialist knowledge of sustainability analysts, equity, fixed income and economic research expertise is also utilised.

Identification of the sustainably investable universe takes place in three steps.

**... in three steps**

### MULTI-STAGE, INTEGRATED ANALYSIS PROCESS



Source: DZ BANK Sustainable Investment Research (2016)

Firstly, the three traditional sustainability dimensions Environment (E), Social (S) and Governance (G) are analysed and combined to form an ESG rating.

**Step 1: traditional ESG analysis**

The next step is to integrate the economic sustainability dimension (E). Using economic sustainability indicators, an economic factor is calculated in the form of a premium or a discount which forms the basis for calculating our integrated sustainability rating.

**Step 2: Integration of economic sustainability dimension**

In a final analysis step the analysed issuers are classified in the categories "sustainable" or "non-sustainable". Dynamic sustainability thresholds (sector and cross-sector thresholds), exclusion criteria (hard and soft) and current EESG controversies are also taken into account.

**Step 3: Classification with the aid of sustainability thresholds, exclusions and controversies**

Issuers classified as sustainable are labelled with the "DZ BANK Seal of Quality for Sustainability" in research publications.

**DZ BANK Seal of Quality for Sustainability**

A detailed description of our EESG analysis and our sustainability rating can be found in our methodology report from 1 September 2016.

**Detailed description of analysis and rating methodology**

## OUR SUSTAINABILITY RATINGS

## SUSTAINABILITY RATING FOR CORPORATES



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## Sustainable Investments

A Research Publication by DZ BANK AG

## DZ BANK Sustainable Investment Research Sustainability Rating for Corporates

Sustainability rating methodology of DZ BANK for corporates



## SECURITIES

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1 Sep 2016 16:52

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Author:  
Marion Praluch, ANALYST  
+49 (0) 69 7447-1582  
Marion.Praluch@dzbank.deMatthew Dorn, ANALYST  
+49(0) 69 7447-1377  
Matthew.Dorn@dzbank.de

Bank on Germany

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## SUSTAINABILITY RATING FOR COUNTRIES



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## SUSTAINABLE INVESTMENTS

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## DZ BANK SUSTAINABLE INVESTMENT RESEARCH SUSTAINABILITY COUNTRY RATING

DZ BANK methodology of country sustainability assessment



## SRI

Study  
10 Dec 2015

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Author:  
Marion Praluch, ANALYST  
Matthew Dorn, ANALYST

Bank on Germany

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## SUSTAINABILITY RATING FOR SSAS

Genossenschaftliche FinanzGruppe  
Volksbanken Raiffeisenbanken

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## SUSTAINABLE INVESTMENTS

A Research Publication by DZ BANK AG

### DZ BANK SUSTAINABLE INVESTMENT RESEARCH SUSTAINABILITY RATING FOR SSAs

Sustainability rating methodology of DZ BANK for Supranationals, Sub-Sovereigns and Agencies (SSAs)



**SRI**

Study  
4 Feb 2016

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AUTHOR:	
Monika Pothmann, ANALYST	
Matthias Dorn, ANALYST	

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## I. IMPRINT

### Published by:

DZ BANK AG Deutsche Zentral-Genossenschaftsbank, Frankfurt am Main,  
Platz der Republik, 60265 Frankfurt am Main

**Telephone:** + 49 69 7447 - 01

**Telefax:** + 49 69 7447 - 1685

**Homepage:** [www.dzbank.de](http://www.dzbank.de)

**E-mail:** [mail@dzbank.de](mailto:mail@dzbank.de)

### Represented by the Board of Managing Directors:

Wolfgang Kirsch (Chief Executive Officer),

Hans-Bernd Wolberg (Deputy Chief Executive Officer), Uwe Berghaus,

Dr. Christian Brauckmann, Wolfgang Köhler, Dr. Cornelius Riese, Michael Speth,  
Thomas Ullrich, Stefan Zeidler

**Chairman of the Supervisory Board:** Helmut Gottschalk

**Head office of the company:** Registered as public limited company in Frankfurt  
am Main, Local Court (Amtsgericht) Frankfurt am Main, Commercial Register HRB  
45651

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**Responsible for the contents:** Stefan Bielmeier, Head of Research and  
Economics

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Statements on the **isolated evaluation of specific aspects** that **precede  
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Sample Portfolio), its defined sector strategy Euro-Stoxx (**DZ BANK Sector  
Favorites**), its defined valuation of payments to beneficiaries (**DZ BANK  
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These isolated statements **alone** are **not sufficient** to form the basis of an  
investment decision. Reference is made to the explanation of the used  
relevant methods.

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Issuers of shares and bonds are analysed on the basis of predefined  
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sustainable**'. For sovereigns, a classification as '**transformation state**' can  
be made that lies between these two classifications.

#### 4.3 Share Indices

For defined share indices, share price forecasts are made at regular  
intervals. From the comparison between the current prices and the  
prepared forecasts on the development of such equity indices, **investment  
recommendations that are not generally definable and that cannot be  
defined in advance** may be developed.

#### 4.4 Currency Areas

The assessment of an investment in a **currency area** is geared to the  
aggregate return expected from an investment in that **currency area**. As a  
rule, this aggregate return is primarily derived from the forecast change in  
the exchange rates. Aspects such as the general interest rate level and  
changes in the yield level of bonds on the relevant bond market that are  
possibly to be taken into consideration are also included in the assessment.  
"**Attractive**" refers to the expectation that an investment in a currency area  
can deliver an above-average and positive return over a horizon of six to  
twelve months.

"**Unattractive**" refers to the expectation that an investment in a currency  
area can deliver only very low returns or even losses over a horizon of six  
to twelve months.

"**Neutral**" refers to the expectation that an investment in a currency area  
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**4.5** The prevailing factor for the **allocation of market segments** and **country  
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"**Overweight**" refers to the expectation that a sub-segment can deliver a  
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"**Underweight**" refers to the expectation that a sub-segment can deliver a  
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"**Upward arrow (↑)**" means that the absolute price increase expected in  
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"Arrow pointing to the right (→)" means that the absolute price change expected in the next twelve months will lie between +10% and -10%.

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"Stable" is given if the agencies S&P, Moody's and Fitch are expected to leave their ratings unchanged in the next twelve months

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<b>Capital Markets Institutional Clients</b>	Head of Capital Markets Institutional Clients	+49 – (0)69 – 74 47 – 69 62	H.-Theo Brockmann
<b>Sales Institutional Clients</b>	Head of Sales Financial Institutions	+49 – (0)69 – 74 47 – 45 36	Norbert Schäfer
	Head of Sales Banks/Central Banks	+49 – (0)69 – 74 47 – 12 70	Lars Carlsen
	Head of Sales Institutional Clients	+49 – (0)69 – 74 47 – 4 24 20	Tilo Sperling
	Head of Regional Clients	+49 – (0)69 – 74 47 – 34 32	Jörn Schneider
	Head of Sales Asia	+65 – 65 80 – 16 23	Jeremy Lee Seow Poh
	Head of Sales Southern Asia	+65 – 65 80 – 16 24	Anand Subramanian
	Head of Sales Northern Asia	+852 – 2 86 43 – 1 82	N.N.
<b>Corporates</b>	Head of Corporates	+49 – (0)69 – 74 47 – 23 69	Roland Weiß
	Head of Money Market and Short Term Investment	+49 – (0)69 – 74 47 – 44 20	Ansgar Wittenbrink
	Head of Interest Rate & FX Executions Small Caps	+49 – (0)69 – 74 47 – 43 54	Klaus Langer
	Head of Derivative Solutions Large Caps	+49 – (0)69 – 74 47 – 44 00	Tobias Strumpel
	Head of Derivative Solutions Small Caps	+49 – (0)69 – 74 47 – 44 26	Evelyne Thiessen
	Head of Derivative Solutions Small Caps, West	+49 – (0)2 11 – 7 78 – 21 55	Ralf Vogt
<b>Debt Capital Markets</b>	Head of Debt Capital Markets	+49 – (0)69 – 74 47 – 49 97	Arnold Fohler
	Head of Origination Germany	+49 – (0)69 – 74 47 – 48 00	Jörg Müller
	Head of Origination Non-Germany	+49 – (0)69 – 74 47 – 17 10	Kai-Henning Poerschke
	Head of Corporate Origination	+49 – (0)69 – 74 47 – 71 45	Bettina Streiter
	Head of MTN-Desk	+49 – (0)69 – 74 47 – 38 11	Friedrich Luithlen

<b>EQUITY SALES</b>	Kai Böckel	+49 – (0)69 – 74 47 – 12 28	kai.boeckel@dzbank.de
Germany	Kai Böckel	+49 – (0)69 – 74 47 – 12 28	kai.boeckel@dzbank.de
Benelux	Lars Wohlers	+49 – (0)69 – 74 47 – 68 34	lars.wohlers@dzbank.de
Switzerland	Petra Bukan	+49 – (0)69 – 74 47 – 49 92	petra.bukan@dzbank.de
Austria	Thomas Reichelt	+49 – (0)69 – 74 47 – 67 09	thomas.reichelt@dzbank.de
UK	Lars Wohlers	+49 – (0)69 – 74 47 – 68 34	lars.wohlers@dzbank.de
<b>SALES TRADING</b>	Marina Semmler	+49 – (0)69 – 74 47 – 13 81	marina.semmler@dzbank.de
<b>DERIVATIVES SALES</b>	Berthold Grünebaum	+49 – (0)69 – 74 47 – 9 91 95	berthold.gruenebaum@dzbank.de

**ACCESS TO DZ BANK RESEARCH (CONTACT LARS.WOHLERS@DZBANK.DE)**

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