Economic report

GENERAL ECONOMIC CONDITIONS

Economic development

The spread of the COVID-19 pandemic sent huge shock waves through the global economy. The large-scale lockdown imposed in the spring of 2020 to combat the pandemic triggered a massive drop in production and sent global trade plummeting. While the global economy was able to bounce back somewhat in the third quarter as the number of infections started to slow, by the end of the year the onset of the second wave of infections had once again slammed the brakes on the economic recovery. The global economy experienced a deep recession in 2020, with a 3.5 percent drop in global gross domestic product according to the IMF's latest estimate.

The European economy was hit extremely hard by the lockdown as well. In addition, the second wave of the pandemic had a significant impact on Europe in particular, hindering the economic recovery. Economic researchers therefore expect economic output to have dipped again in the fourth quarter of 2020. According to preliminary data from Eurostat, the COVID-19 pandemic was responsible for an economic slump of 6.8 percent in the eurozone looking at the year as a whole.

In Germany, gross domestic product was down by 5.0 percent in a year-on-year comparison – only the financial market crisis of 2009 resulted in a more marked decline in economic output. Almost all sectors of the economy were affected. However, the construction industry in particular was able to hold its own with a 1.4 percent increase in gross value added. Positive contributions to growth were also made by public consumption, which rose by 3.4 percent, and by construction investment, which was up by 1.5 percent.

The average inflation rate of 0.5 percent was significantly lower than in the previous year, largely due to the move to cut VAT rates until the end of 2020 as part of the German government's economic stimulus package. Heating oil and fuel, in particular, as well as consumer goods, became cheaper. The COVID-19 pandemic also put an end to the prolonged upswing on the employment market. The number of people out of work increased by an annual average of more than 400,000 to 2.7 million. This pushed the unemployment rate up by 0.9 percentage points to 5.9 percent. The lockdown also led to a very marked expansion in the use of furlough (Kurzarbeit). According to the German Federal Employment Agency, more people were on furlough in 2020 than ever before.

Financial markets

The global COVID-19 pandemic also shook the financial markets, with the stock markets suffering massive losses as a result of the lockdown. Liquidity bottlenecks also triggered a substantial sell-off of liquid government and corporate bonds in the short term, leading to higher yields and also lower prices. In a quest to stabilise the markets, a large number of countries launched large-scale aid programmes and the central banks reacted by adopting monetary policy measures.

The US Federal Reserve ("Fed") lowered the key interest rate by 50 basis points to a range of between 1.0 percent and 1.25 percent at the beginning of March. Less than two weeks later, it decided to lower the interest rate by 100 basis points to within a range of 0.0 percent to 0.25 percent. In addition, the Fed announced plans to make large-scale purchases of Treasury securities, mortgage-backed securities (MBS) and corporate bonds.

In mid-March, the ECB increased its pre-existing Asset Purchase Programme (APP) by EUR 120 billion before launching an additional Pandemic Emergency Purchase Programme (PEPP) worth EUR 750 billion only shortly afterwards.

While the markets calmed down slightly as a result of these measures, liquidity shortages were still pushing money market rates up. This prompted the ECB to take additional action at the beginning of June, including the decision to increase the PEPP by EUR 600 billion to a total of EUR 1.35 trillion and to launch new TLTRO tenders for banks, offering particularly favourable financing conditions. In December, the PEPP was increased by another EUR 500 billion and its term was extended until the end of March 2022. In addition, maturing securities were reinvested until at least the end of 2023 and the favourable TLTRO conditions for banks were extended for another year, subject to certain conditions. The ECB opted not to alter its key interest rates in 2020. The main refinancing rate remains unchanged at 0.0 percent.

Other central banks, including the Bank of England, Bank of Japan and Swiss National Bank, also took monetary policy measures to make additional liquidity available on the financial

YIELD ON TEN-YEAR BUNDS 2020
IN %

Source: Bloomberg (closing rate)

markets. The Bank of England slashed the key interest rate twice, from 0.75 percent to 0.15 percent, in the space of one week in March.

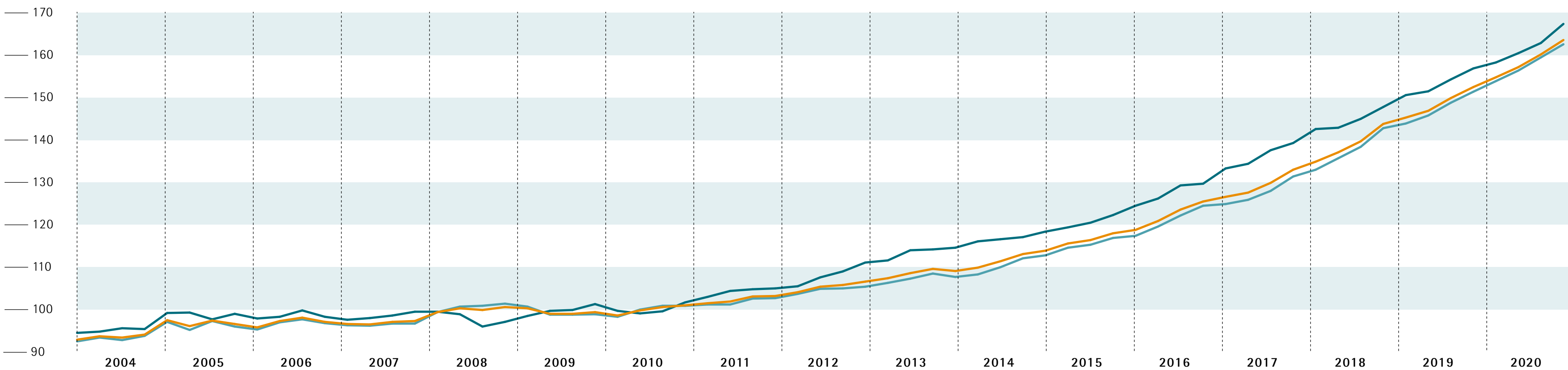
On the bond market, the pandemic and considerable uncertainty surrounding economic development first of all sent the fixed income markets tumbling to new record lows. The yield on ten-year German government bonds, for example, fell from minus 0.19 percent at the beginning of the year to minus 0.9 percent at the beginning of March 2020. Liquidity bottlenecks then triggered a significant short-term rise in yields on German government bonds to minus 0.19 percent. The ECB's measures in March and June calmed the financial markets again and yields mostly ranged between minus 0.4 percent and minus 0.6 percent in the second half of the year.

On the foreign exchange market, the US dollar was still able to gain ground against the euro at the beginning of the pandemic, reaching a high of USD 1.06 in March. The temporary economic recovery in the summer, low new infection figures in Europe and the EU's large-scale pandemic aid package reversed this trend and sent the US dollar on a marked downward trajectory. Joe Biden's victory in the US presidential election provided further support to this development, as it is now expected that US policymakers will provide larger aid packages and rack up higher government deficits. At the end of the year, the US dollar was trading close to its low for the year at USD 1.22 to the euro.

The Swiss franc fluctuated within a much narrower range against the euro last year. Compared to the 2019 year-end rate of CHF 1.085, there was hardly any change at the end of 2020, with a rate of CHF 1.082. Sterling was much more volatile, largely due to the news flow surrounding Brexit. The pound initially started the year even firmer and reached a high for the year of just under GBP 0.83 in February, only to fall to GBP 0.95 within the space of a month in the midst of market turbulence associated with the outbreak of the pandemic. In the second half of the year, the exchange rate settled down and the pound was mostly trading at around GBP 0.90 against the euro.

On the covered bond market, the pandemic created an environment of considerable uncertainty and a reluctance to buy among investors. While fears of large-scale loan defaults at banks put pressure on unsecured bank bonds in particular,

DEVELOPMENT OF PROPERTY PRICES IN GERMANY
YE 2010 = 100



Owner-occupied housing
Condominiums
Single family houses

Source: vdp Research property price index, Q3 2020
As of November 2020

spreads also widened considerably for covered bonds. The ECB's decisions on its purchase programmes played a significant role in stabilising funding spreads for banks. Pfandbriefe, in particular, were at a similarly favourable level at the end of the year as they had been at the beginning. Due to the further drop in interest rates, almost all Pfandbriefe were trading with negative yields at times. This development was encouraged by the ECB's monetary policy, which continues to force traditional Pfandbrief investors to invest in other asset classes.

Issuing activities on the primary market for covered bonds were significantly more restrained than they had been a year earlier due to the COVID-19 pandemic and the resulting favourable funding offers from central banks. All in all, the euro-denominated issue volume of benchmark covered bonds came to around EUR 92 billion in 2020, down by around 30 percent year-on-year.

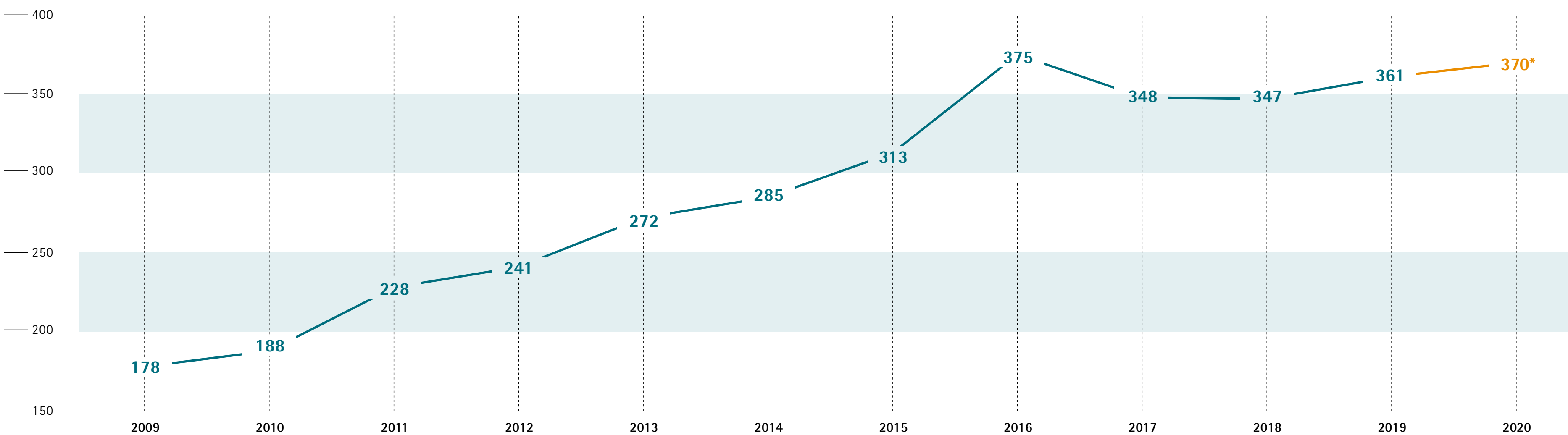
Property markets and property financing markets

Residential property – Germany

The COVID-19 pandemic did not have any negative impact on the German residential property market in the year under review, other than temporary restrictions on supply and demand during the lockdown in the spring of 2020. Analyses conducted by the Association of German Pfandbrief Banks (vdp) show that demand for residential property, as well as prices, actually increased during the pandemic. By the third quarter of 2020, the vdp price index for residential properties was up by 7.1 percent compared to the same period of the previous year. Prices of single and two-family houses were up by 7.4 percent, with condominium prices rising by 6.7 percent.

Multi-family house prices rose by 7 percent compared to the prior-year period, because investors expect the risk of rent default in this segment to be lower than for commercial properties. Average year-on-year rental price growth came to 3.4 percent at the end of the third quarter. In Germany's seven largest cities, rents rose by an average of 1.8 percent. In Berlin, the introduction of the rent cap and the rent freeze led to significantly slower rental price growth of 0.7 percent.

RESIDENTIAL BUILDING PERMITS IN GERMANY 2009–2020
FIGURES IN 000



* Estimated.

Source: German Federal Statistical Office

The trend towards stronger price developments for residential properties outside the country's major cities continued. The lockdown has led many private households to reconsider their housing situation. Residential properties on the outskirts of major cities offering attractive recreational opportunities and, in particular, more space to live and work under one roof, were in even greater demand than prior to the pandemic. While the price index for owner-occupied housing rose by 5.2 percent in the top seven cities, an increase of 7.3 percent was measured nationwide in the same period.

Despite the increase in construction investment, construction activity continues to lag behind demand. Compared to 2019, the number of new housing units approved increased by 3.9 percent to 332,000 between January and November. Although the number of approved housing units is expected to have risen to around 370,000 units by the end of the year, this is still not enough to meet the demand for housing. This is evident if we look at the construction backlog, which includes all construction projects that have not yet been started or completed. With around 740,000 housing units, the current backlog is at the highest level witnessed since 1998. This corresponds to around two and a half years' worth of housing construction.

Despite the lockdown restrictions, institutional investors were very active in the German residential property market in 2020, investing EUR 20.3 billion in German residential property portfolios, based on data evaluated by Ernst & Young. This equates to a year-on-year increase of 8 percent. The institutional housing market was dominated by domestic investors with a share of 75 percent, a trend assumed to be due primarily to the travel restrictions for international investors in 2020. Overall, the German residential property market remained a safe investment target compared with other countries.

Data collected by the vdp indicate that loans amounting to EUR 194 billion were granted in Germany for the purchase of residential property in the first three quarters of 2020, up by 7.7 percent compared to the prior-year period.

Residential property – international

In Germany's neighbouring European countries, too, the pandemic has not yet had any negative impact on the residential property markets. Eurostat's house price index shows a year-on-year increase in residential property prices of 3.7 percent in the first half of the year. In those European residential property markets that are relevant to MünchenerHyp, prices rose by 4.1 percent in Austria and in the Netherlands in the first six months of the year.

Due to excess supply, the Swiss residential market has experienced falling asking rents on the residential market since 2015 as well as falling condominium prices since 2017. This trend continued for asking rents in 2020, with a decline of 1.8 percent year-on-year. Condominiums saw a turnaround with price increases of 5.1 percent against the previous year. The price of owner-occupied homes rose by 3.0 percent during the same period. A trend towards stronger price growth outside the major cities was also observed in Switzerland, although prices in the major cities, particularly in Lausanne and Geneva, also continued to increase nonetheless.

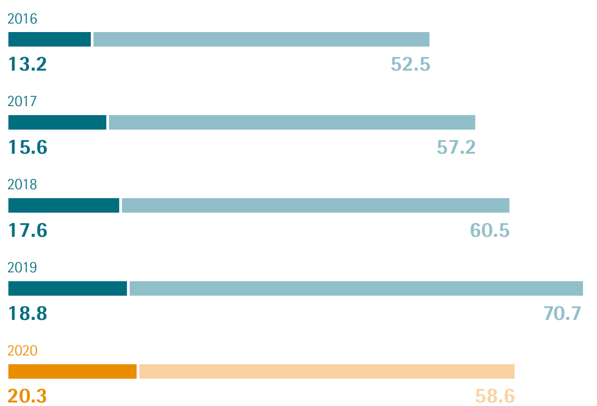
Commercial property – Germany

In 2020, EUR 58.6 billion was invested in German commercial properties, down by 17 percent compared to the previous year. Nevertheless, the investment volume came to around EUR 5 billion, outstripping the average for the last 15 years. This means that, even against the backdrop of the COVID-19 pandemic, professional investors continued to see the German commercial property market as a safe investment target in an environment dominated by low interest rates and a lack of investment alternatives.

Measures to combat the COVID-19 pandemic resulted in a shift in investor preferences with regard to property use types. After residential portfolios, the biggest winner when it came to attracting investor attention was the segment for logistics properties, whose market share rose to 11 percent. The retail sector remained virtually unchanged compared to 2019, with a 15 percent share of the total transaction volume. Within this segment, however, investors tended to prefer specialist stores and retail parks over shopping centres and commercial buildings. 41 percent of the transaction volume was attributable to office properties, which remained the most popular type of use despite a fall in market share. Investors were very cautious with regard to hotel properties in 2020, which accounted for only 3 percent of the investment volume.

In Germany's top property markets, office prime yields fell by around ten basis points over the course of the year. Office buildings in Berlin and Munich generated the lowest prime yields, at 2.6 percent in each case.

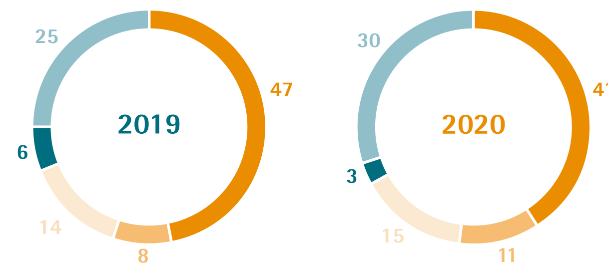
DEVELOPMENT OF COMMERCIAL PROPERTY TRANSACTIONS IN GERMANY 2016–2020
IN € BILLION



Residential (only portfolio)
Commercial

Source: EY Research
As of January 2021

TRANSACTION VOLUME BY TYPE OF USE
IN %



Office
Logistics
Retail
Hotel
Residential

Source: Real Capital Analytics
As of 11 January 2021

In the first three quarters of 2020, around 2.7 million square metres of office space was let in the top seven office cities, down by 27 percent compared to the prior-year period. The uncertain economic outlook prompted many market players to postpone their expansion plans for the time being, with a knock-on effect on lease turnover. At the beginning of the pandemic, all Germany's top property markets were reporting low vacancy rates and high demand, combined with low levels of speculative new construction. Although vacancy rates increased in tandem with the lockdown measures, they remained at relatively low levels in the country's major office locations after the end of the third quarter. Prime rents for office properties remained stable in all major German cities in 2020.

As a result of the lockdown measures and the associated loss of sales in bricks-and-mortar retailing, commercial buildings and shopping centres have been particularly hard hit by the recession. The net initial yield for commercial properties in the prime segment of the country's major cities rose by 40 basis points over the course of the year and averaged 3.5 percent.

Prime rents fell by around 3 percent in the year under review, but only very few spaces were let in shopping streets during this uncertain period. Shopping centre yields rose on a net basis from 4.3 percent to 5.0 percent over the course of the year. Both prime and average rents fell by 12 percent for shopping centres over the year as a result of the COVID-19 pandemic.

Commercial property – international

The investment volume for commercial property and residential portfolios in Europe fell by 30 percent year-on-year in 2020 to EUR 197 billion. Considering the uncertain economic development caused by the pandemic, the investment market nevertheless remained very active, a trend that can be explained primarily by the lack of alternative investment opportunities. 29 percent of the European transaction volume was invested in Germany, which is currently the most sought-after property market for investors. 40 percent of the invested capital went into office properties across Europe.

Office rents fell by around 1 percent in the European prime segment over the course of 2020, triggered by dwindling demand for space and increasing vacancy rates in all major European cities.

The property investment market in the UK has seen lower transaction volumes since the Brexit referendum of 2015, when investors started to adopt a more cautious stance. In 2020, EUR 42 billion was invested in commercial property and residential portfolios in the UK, down by 17 percent compared to the previous year. The net initial yield for office property in London remained stable over the year, although prime rents for new lettings have fallen by around 1 percent. Compared with office properties, the impact of the recession was much more pronounced for retail properties and, in particular, for shopping centres. Prime rents for commercial buildings fell by 9 percent over the year, with prime rents for shopping centres losing as much as 15 percent. Even before the outbreak of the COVID-19 pandemic, a wave of insolvencies in the UK retail sector led to shop closures and rising vacancy rates in regional markets. This process of transformation within the UK retail sector has been accelerated by the COVID-19 pandemic, particularly due to the considerable popularity of online shopping. Net initial yields for commercial properties in prime locations rose to 3.9 percent during the year, with yields for shopping centres rising to 7.0 percent.

In France, EUR 32 billion was invested in commercial property and residential portfolios in 2020, down by 29 percent compared to the previous year. Net initial yields for office property located in the heart of Paris remained constant at 2.8 percent in 2020, meaning that, looking at Europe as a whole, only Munich and Berlin had more expensive prices than Paris. Long-term infrastructure projects have accelerated neighbourhood development on the outskirts of the city, putting attractive office locations outside the city centre into the spotlight. In central Paris, the vacancy rate increased from 1.7 percent to 2.9 percent over the course of the year. This means that vacancy rates were still so low that prime rents in Paris continued to rise by 2 percent year-on-year despite the recession. As in other major European cities, commercial buildings in retail locations have so far been impacted less by the recession than shopping centres have. As a result, there has been no downward trend in rents for commercial buildings, whereas shopping centre rents dropped by 11 percent.

In the Netherlands, transaction activity was down by 27 percent year-on-year to an investment volume of EUR 15 billion. The vacancy rate in Amsterdam, the leading property market in the Netherlands, has so far risen only marginally to 6.0 percent. Office rents remained stable in the country's main markets. Retail rents in the Netherlands were comparatively firmer than in other European markets, with rents dropping by 2 percent for commercial buildings and by 8 percent for shopping centres.

In Spain, the transaction volume was sliced in half to just under EUR 8 billion. Nevertheless, net initial yields for office properties remained on a par with the prior-year level of 3.2 percent in Madrid and 3.3 percent in Barcelona. The letting volume was around one third lower than in the previous year, pushing vacancy rates up slightly and prime rents down by around 1 percent over the course of the year. Prior to the outbreak of the COVID-19 pandemic, the Spanish retail property market was considered to be one of the fastest growing markets in Europe, with rising household incomes as well as a flourishing tourism sector fuelling higher sales and, as a result, rental price growth. The impact of the pandemic resulted in a 12 percent drop in retail rents in shopping centres in Spain. Net initial yields increased by 20 basis points for commercial properties and by 50 basis points for shopping centres.

In the US, commercial property and residential portfolios worth USD 400 billion had changed hands by the end of the third quarter of 2020, down by around 30 percent year-on-year. Multi-family apartments were the most sought-after asset class, as these were expected to offer comparatively stable cash flows. Logistics properties were also very popular with investors. The major cities that are relevant to MünchenerHyp (New York, Washington DC, Boston, Chicago, Los Angeles, San Francisco, Seattle) continued to show high levels of liquidity in the property market.

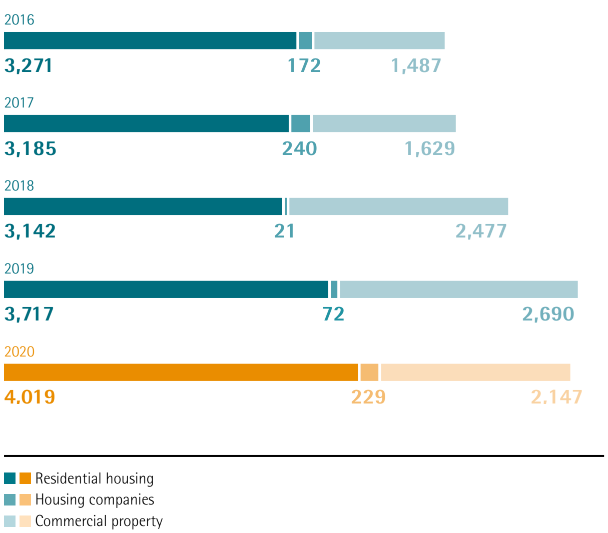
BUSINESS DEVELOPMENT

New mortgage business

The COVID-19 pandemic and the economic turbulence that it triggered made it considerably harder at times to come up with any reliable assessment of market conditions and developments. As a result, we adjusted our new business plans and lending criteria during the year to reflect the new circumstances.

Our new business showed positive development, even under the strain of the COVID-19 crisis. All in all, we issued around EUR 6.4 billion in new mortgage financing commitments in 2020, down only slightly on the previous year's record result of EUR 6.5 billion.

MÜNCHENERHYP NEW MORTGAGE BUSINESS 2016–2020
COMMITMENTS IN € MILLION



In private residential property financing, we were even able to expand our new business further thanks to the stability of the German residential property market and high demand for property and property financing in Germany throughout the year. 2020 became the first financial year in which we granted just over EUR 4 billion in private residential property financing (2019: EUR 3.7 billion), up by 8 percent year-on-year.

The increase is due primarily to brokerage business with our partner banks from the Cooperative Financial Network. With a commitment volume of EUR 3.1 billion, new business exceeded the EUR 3 billion threshold for the first time. Compared to the previous year, this corresponds to an increase of around EUR 300 million or 10 percent. There are several reasons behind this success story. Above all, our three sales campaigns were very well received by customers of our partner banks. Improved processes in our collaboration with the cooperative banks also translated into higher brokerage volumes. Demand for loans via the expanded "simplified procedure" (Vereinfachtes Verfahren) in loan processing, for example, increased by around 25 percent. Ultimately, the overall conditions for high demand remained positive in spite of the COVID-19 pandemic. This is especially true of the low interest rates. In this environment, there was high demand among customers for financing structures featuring long-term fixed interest rates and flexibility.

Sales of private property finance generated via independent financial service providers in Germany increased by 2 percent year-on-year, to EUR 670 million.

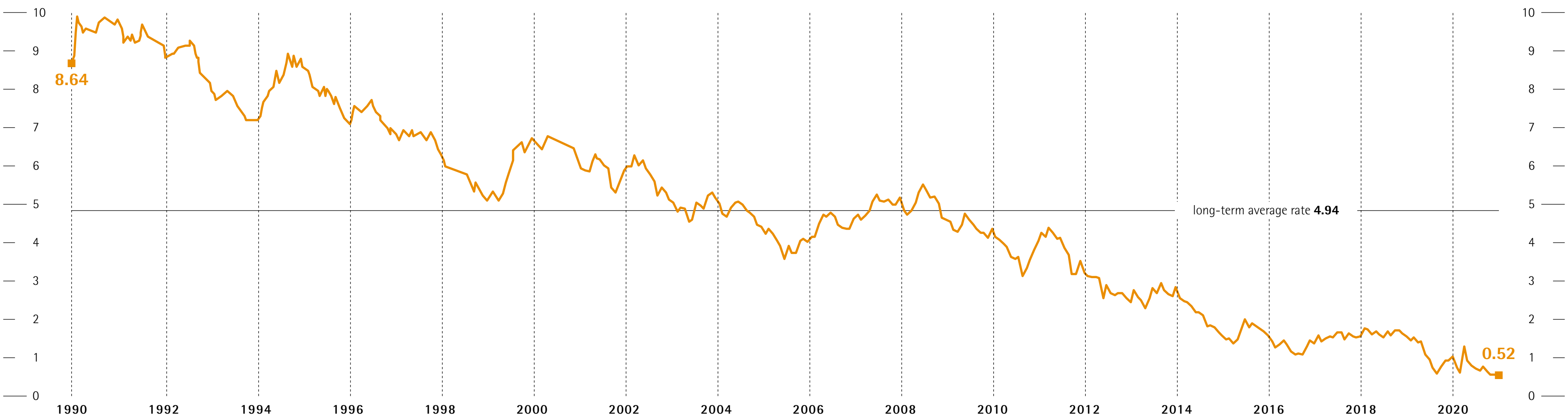
In our partnership with PostFinance in Switzerland, new business was more or less on a par with the previous year at EUR 278 million (2019: EUR 290 million). In the highly competitive Swiss market, special efforts were needed to stand out from the competition. This prompted us to launch a sales campaign hand in hand with PostFinance in the autumn of 2020, which allowed us to catch up in terms of new business. New business in Austria was still in the trial phase following our market entry in the previous year and amounted to EUR 16 million (2019: EUR 8 million).

The impact of the COVID-19 pandemic on the property markets was more visible in the commercial property financing segment. Given these overall conditions, we achieved a satisfactory new business result. The volume of commitments exceeded the EUR 2 billion mark for the third time in succession since the financial market crisis. In total, we granted commercial financing to the tune of EUR 2.4 billion, down by 14 percent on the prior-year result of EUR 2.8 billion. This means that we were able to exceed our new business target, which we had adjusted in the course of the year, an achievement that we consider to be positive in view of the economic impact of the COVID-19 pandemic.

This result was driven largely by our domestic business, which contributed the lion's share with a new business volume of EUR 1.5 billion. At almost EUR 0.9 billion, we maintained our international business at the level achieved in the previous year. Three countries once again accounted for the majority of this business: the US (syndicated business only) with 35 percent, the Netherlands with 26 percent and Spain with 22 percent.

The development of earnings in the commercial financing business was particularly worthy of note. Despite adjustments to our new business plans, we were able to achieve our original earnings target. In our international business in particular, we were able to boost our earnings power without increasing the risks involved. We were able to maintain the average loan

MORTGAGE RATES MÜNCHENERHYP
TEN YEAR FIXED RATE | IN %



As of: 04.01.2021

volumes achieved in 2019, a year in which they increased considerably. In addition, we were also able to conduct a number of large-volume underwriting transactions with subsequent syndication in 2020.

From a risk perspective, we maintained our conservative financing approach with a focus on conventional financing at completion, giving due consideration to adequate, sustainable minimum cash flows and property locations. We consider the high equity ratios in the financing structures, which averaged over 40 percent and increased slightly compared to the previous year, to be a positive aspect.

Capital markets business

Stringent regulatory requirements and low asset spreads continued to dictate our strategy for investing in securities issued by the public sector and banks in 2020. Due to the substantial ECB purchases, LCR-eligible securities are still trading at very expensive spread levels. In this environment, purchasing sovereign and bank securities with strong credit ratings was not a lucrative option and also resulted in high total asset costs. As a result, securities purchases were kept to the bare minimum.

On a net basis, the portfolio volume was reduced by EUR 0.4 billion to EUR 3.7 billion. New business in 2020 totalled EUR 97.0 million, compared with EUR 44.5 million in 2019.

Refinancing

MünchenerHyp consistently enjoyed access to funding at good conditions during the reporting year, even during the first peak of the COVID-19 pandemic in March and April. During this period, we mainly issued private placements of covered and uncovered bonds in euros and Swiss francs. The Cooperative Financial Network in particular showed a keen interest in these products. In addition, the ECB's current open market operations presented an opportunity for meeting covered funding needs at very attractive conditions.

We also issued several large-volume bonds in the reporting year. Our focus in terms of large-volume funding transactions in the first six months of the year was on uncovered bond issues.

We started by issuing a green senior non-preferred bond worth CHF 240 million in January. The first green security issued in this asset class on the Swiss capital market; it met with very high demand. The bond has a term of five years and eleven months and a coupon of 0.1 percent. The issue was placed at a price of 51 basis points above the mid-swap rate and received a total of 39 orders.

In the same month, we issued another senior non-preferred bond, this time in euros. With an issue volume of EUR 250 million, the bond achieved an issue spread of 54 basis points above the mid-swap rate.

We also tapped a Swiss franc Mortgage Pfandbrief maturing in November 2032 by a further CHF 60 million.

We started the second half of the year by issuing a CHF 200 million green senior preferred bond. This was also the first green security issued in this asset class on the Swiss capital market for us, with very high investor demand for this issue as well. Incoming orders had already reached CHF 150 million after only just under half an hour. The bond has a term of eight years and a coupon of 0.25 percent. The issue was placed at a price of 55 basis points above the mid-swap rate and received a total of 50 orders.

This was followed in September by the issue of the first of two long-dated benchmark Mortgage Pfandbriefe in the reporting year. The issue volume amounts to EUR 500 million and the term is 15 years. Investor demand was exceptionally strong. After one and a half hours, the order book was closed at over EUR 1.8 billion. The coupon is 0.125 percent. The issue was placed at a price of 7 basis points above the mid-swap rate.

We issued the second benchmark Mortgage Pfandbrief in October with a volume of EUR 500 million, a term of 20 years and a coupon of 0.01 percent. This was the lowest coupon that a Mortgage Pfandbrief with this term has ever achieved. Investor demand was also very high for this issue, meaning that the order book was closed at EUR 1.4 billion after only a short time. The Mortgage Pfandbrief was placed at a price of 2 basis points above the mid-swap rate.

Due to their long terms, both Mortgage Pfandbriefe will allow us to ensure that long loan terms in private residential property financing can be refinanced to a great extent with matching maturities.

The high-volume funding activities were concluded in December with the tap of an existing covered bond by a further CHF 115 million, maturing in 2031. The coupon is 0.20 percent. The issue was placed at a price of 9 basis points above the mid-swap rate.

MünchenerHyp's total issue volume on the capital market in the year under review was around EUR 7.5 billion. In covered funding, Mortgage Pfandbriefe accounted for EUR 4.9 billion, including our own Pfandbriefe deposited with the ECB, with a volume of EUR 2.6 billion for uncovered funding. Once again, no Public Pfandbriefe were issued, in keeping with the Bank's business strategy.

FINANCIAL PERFORMANCE, FINANCIAL POSITION AND NET ASSETS

Development of earnings

Net interest income [1] increased once again in the year under review, rising by EUR 48.0 million, or 16.0 percent, to EUR 347.8 million. The increase was driven primarily by successful new business in the year under review and in particular in previous years. This means that the Bank has trebled its net interest income within the last ten years. The mortgage loan portfolio has doubled in the same period.

Commission paid totalled EUR 122.5 million, up by EUR 11.8 million or 11 percent on the prior-year level thanks to very successful new business. Commission received fell to EUR 13.0 million, resulting in net commission income [2] of minus EUR 109.5 million, compared with minus EUR 95.3 million in the previous year.

This resulted in net interest and commission income [3] of EUR 238.3 million, which corresponds to an increase of EUR 33.8 million, or 16.5 percent.

General administrative expenses fell by EUR 7.0 million to EUR 118.2 million. This included an increase in personnel costs of EUR 1.7 million, or 3.0 percent. In addition to increases under collective agreements, this was primarily due to necessary expansion of the workforce.

Other administrative expenses fell by EUR 8.7 million, or 12.6 percent. This reduction, which was largely the result of cost discipline, was achieved despite a renewed increase in regulatory costs. Expenses for the banking levy and various regulatory authorities alone increased by 15 percent to around EUR 18 million.

Depreciation, amortisation and write-downs of intangible assets and fixed assets rose by EUR 4.0 million year-on-year, to EUR 10.2 million.

Total administrative expenses [4] amounted to EUR 128.4 million compared with EUR 131.3 million in the previous year. The cost-income ratio [5] was 53.9 percent, as against 64.2 percent a year earlier.

The net result of other operating expenses and income amounted to minus EUR 3.6 million.

The operating result before risk provisions [6] increased by 54.4 percent year-on-year, to EUR 106.4 million.

The item "Write-downs of and valuation allowances of loans and advances and specific securities, as well as additions to loan loss provisions" amounted to minus EUR 10.6 million. The credit risk situation was satisfactory despite the ongoing COVID-19 pandemic. The net result of changes in loan loss provisions (including direct write-downs) amounted to minus EUR 10.1 million (previous year: plus EUR 18.2 million).

Net expenses from the sale of promissory note loans and the redemption of registered securities and debt securities amounted to EUR 0.5 million.

The item "Depreciation, amortisation and write-downs of participating interests, shares in affiliated companies and securities treated as fixed assets" amounted to minus EUR 0.4 million.

Income from ordinary business activities amounted to EUR 95.3 million. After tax expenses of EUR 37.6 million and an allocation of EUR 20 million to the "fund for general banking risks" (Section 340g of the German Commercial Code (Handelsgesetzbuch – HGB)), net income for the financial year comes to EUR 37.7 million, which is 5.6 percent higher year-on-year.

The return on equity (RoE) before tax amounted to 6.2 percent [7]. After tax, the Bank achieved an RoE of 3.7 percent [8].

[1] Net interest income is calculated by adding item 1 'Interest income' plus item 3 'Current income' plus item 4 'Income from profit-pooling, profit transfer or partial profit transfer agreements' minus item 2 'Interest expenses' as shown in the income statement.
[2] Net commission income is calculated by offsetting item 5 'Commission received' and item 6 'Commission paid' as shown in the income statement.
[3] The net interest and commission result is the sum of net interest income and net commission income.
[4] Total administrative expenses are the sum total of item 8 'General administrative expenses' and item 9 'Depreciation, amortisation and write-downs of intangible assets and fixed assets' as shown in the income statement.
[5] Ratio of total administrative expenses to net interest and net commission income.
[6] Net result of items 1 to 10 in the income statement.
[7] RoE before tax is calculated as the ratio of income statement item 14 Income from ordinary activities to balance sheet liability item 10 Fund for general banking risks (previous year) plus liability item 11a Members' capital contributions (current year) plus item 11b Revenue reserves (previous year) plus income statement item 19 Retained earnings brought forward from previous year.
[8] RoE after tax is calculated as the ratio of income statement item 17 Allocation to fund for general banking risks plus item 18 Net income to balance sheet liability item 10 Fund for general banking risks (previous year) plus liability item 11a Members' capital contributions (current year) plus item 11b Revenue reserves (previous year) plus income statement item 19 Retained earnings brought forward from previous year.

Balance sheet structure

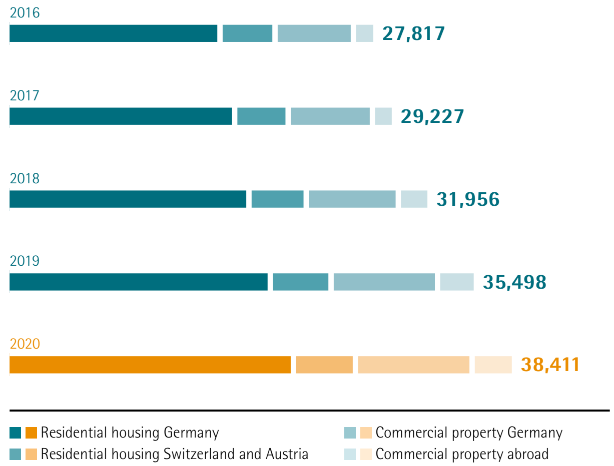
Total assets increased to EUR 48.6 billion at the end of the 2020 financial year, compared with EUR 42.9 billion at 31 December 2019.

This 13 percent increase is due partly to growth in the mortgage loan business portfolio and partly to a EUR 3.1 billion increase in the own bonds portfolio.

During the course of the year, the mortgage loan portfolio grew by EUR 2.9 billion, to EUR 38.4 billion. Private residential property financing in Germany was once again the fastest growing segment, with growth of EUR 1.8 billion.

The private residential property financing portfolio is structured as follows: domestic – EUR 21.5 billion (previous year: EUR 19.7 billion); foreign – EUR 4.7 billion (previous year: EUR 4.7 billion). In addition to the financing business in Switzerland, this portfolio also includes financing in Austria. The commercial property financing portfolio totals EUR 12.2 billion (previous year: EUR 11.1 billion). Of this amount, EUR 3.2 billion (previous year: EUR 3.0 billion) is attributable to financing outside Germany. The most important international market is the USA with 23 percent (previous year: 21 percent), followed by the Netherlands with 21 percent (previous year: 17 percent), Spain with 19 percent (previous year: 15 percent) and the UK with 17 percent (previous year: 18 percent).

PORTFOLIO DEVELOPMENT MÜNCHENERHYP 2016–2020
IN € MILLION



In line with our business and risk strategy, the portfolio of public-sector and bank loans and securities decreased from EUR 4.1 billion to EUR 3.7 billion, EUR 1.9 billion of which was made up of securities and bonds.

At the end of 2020, the net sum of hidden charges and hidden reserves in the securities portfolio amounted to EUR 43 million (previous year: EUR 47 million). These figures include hidden charges of EUR 1 million (previous year: EUR 0 million) arising from securities issued by countries located on the periphery of the eurozone and banks domiciled in these countries. These securities had a total volume of EUR 0.2 billion at the end of 2019 (previous year: EUR 0.2 billion).

A detailed examination of all securities indicated that there are no permanent impairments. We have accounted for these bonds on a held-to-maturity basis. Write-downs to a lower fair value were not necessary.

The portfolio of long-term refinancing instruments increased by EUR 3.2 billion to EUR 39.6 billion. Mortgage Pfandbriefe accounted for EUR 28.9 billion of this amount, Public Pfandbriefe for EUR 1.9 billion and uncovered bonds for EUR 8.8 billion. The total volume of refinancing instruments – including money market funds and customer deposits – increased to EUR 45.9 billion as of 31 December 2020.

The item "Other liabilities to customers" can be broken down as follows:

OTHER LIABILITIES TO CUSTOMERS
IN € 000

	Remaining term < one year	Remaining term > one year	Total
Other liabilities to customers as of 31 Dec. 20	**1,769,426**	**2,112,200**	**3,881,626**
Registered bonds	33,353	1,406,019	1,439,372
of which institutional investors	33,310	1,388,019	1,421,329
Promissory note loans on the liabilities side	707,649	681,181	1,388,830
of which institutional investors	102,555	520,181	622,736
Other	1,028,424	25,000	1,053,424
of which institutional investors	586,250	25,000	611,250

Members' capital contributions grew by EUR 80.6 million, to EUR 1,153.1 million. Together with the issue of the Additional Tier 1 bond in the amount of CHF 125 million in 2019, regulatory equity capital totalled EUR 1,676.4 million (previous year: EUR 1,573.2 million).

Common Equity Tier 1 capital rose from EUR 1,406.8 million in the previous year to EUR 1,517 million. At 31 December 2020, the Common Equity Tier 1 capital ratio was 20.6 percent (previous year: 19.8 percent), the Tier 1 capital ratio was 22.2 percent (previous year: 21.4 percent) and the total capital ratio was 22.8 percent (previous year: 22.1 percent). The leverage ratio at 31 December 2020 was 3.6 percent (previous year: 3.6 percent).

RATINGS, SUSTAINABILITY AND REGULATORY CONDITIONS

Ratings

In October 2019, the rating agency Moody's changed Germany's Macro Profile from "Very Strong (-)" to "Strong (+)" in its model. This led to it taking rating actions on nine German banks, including MünchenerHyp: the deposit rating, the senior unsecured and the issuer rating remained unchanged at Aa3, but the outlook was changed to negative. So far, Moody's has not changed this assessment.

Moody's remains positive about the fact that MünchenerHyp has a strong reputation on the capital market as an issuer of Pfandbriefe, noting that it has an accordingly high level of refinancing strength, and also acknowledges the firm ties and corresponding support the Bank enjoys within the Cooperative Financial Network.

CURRENT RATINGS AT A GLANCE

	Rating
Mortgage Pfandbriefe	Aaa
Junior Senior Unsecured	A2
Senior Unsecured	Aa3*
Short-term liabilities	Prime–1
Long-term deposits	Aa3*

* Outlook: negative

MünchenerHyp has not issued any Public Pfandbriefe for some years now, as these are only profitable through cross-selling income. As a result, it withdrew its rating for Public Pfandbriefe in 2020.

Even to achieve the highest Aaa rating for Pfandbriefe, Moody's still only requires compliance with the legal requirement of 2 percent over-collateralisation. There is therefore no requirement for voluntary over-collateralisation.

Our long-term unsecured liabilities are rated AA- by the two other major rating agencies, Standard & Poor's and Fitch, via the combined rating of the Cooperative Financial Network.

Sustainability

In the reporting year, we continued to pursue our existing sustainability activities and launched a number of new projects.

In the private residential property financing business, our loans with a social and environmental focus (MünchenerHyp Green Loan and MünchenerHyp Family Loan) accounted for 20 percent of new business. In order to further increase the positive contribution made by the Green Loan in terms of saving or avoiding CO_2 emissions, in May 2020 we lowered the criterion for the annual maximum primary energy consumption of financed properties from 70kWh / m^2 per year to 55 kWh / m^2.

In terms of sustainable securities, we issued ESG Pfandbriefe, green bonds, commercial paper and term deposits with a volume of around EUR 500 million. We also revised our Green Bond Framework and re-certified it with a positive Second Party Opinion (SPO) prepared by ISS ESG.

In terms of the Bank's sustainability rating, ISS ESG awarded MünchenerHyp a rating of C+ for sustainability management in 2020. This is a slight downgrade compared to the B- rating awarded in previous years and is mainly due to the fact that the Bank did not prepare any GRI disclosures in 2018 and 2019. Nevertheless, the current rating still places us among the top performers in the Financials / Mortgage & Public Sector rating peer group. As a result, ISS ESG has granted us "Prime Status" again.

At the beginning of 2020, the agency imug raised MünchenerHyp's rating slightly in one rating category, although this did not result in a higher rating classification. The sustainability rating therefore remains "positive", while Mortgage Pfandbriefe are also assessed as "positive" and Public Pfandbriefe as "very positive".

The agency Sustainalytics has introduced a new rating methodology. In addition to the management of sustainability issues, the new approach also assesses the specific sustainability risks for the company concerned and the sector in which it operates. A "risk score" (of 0 to 40+ points) replaces the previous scoring system of 0 to 100 points. Whereas a high number of points used to represent strong performance, a low risk score now determines the strength of sustainability management. MünchenerHyp's current risk score is 17.4 (low risk).

Development of sustainability ratings over the last two years at a glance:

THE DEVELOPMENT OF THE SUSTAINABILITY RATINGS SINCE 2019

		2019	2020
ISS-ESG		B-(Prime Status)	C+(Prime Status)
imug	Sustainability rating / Unsecured bonds:	positive (BB)	positive (BB)
	Mortgage Pfandbriefe:	positive (BBB)	positive (BBB)
	Public Pfandbriefe:	very positive (A)	very positive (A)
Sustainalytics		65 out of 100 points	Risk score of 17.4 (low risk)

In 2020, as part of our efforts to further enhance our sustainability management, we looked at the mounting social and environmental challenges facing us, as well as the growing demands of our stakeholders. This prompted us to launch projects aimed in particular at deepening the understanding of sustainability issues within the Bank, consolidating our management processes and further establishing sustainability as a firm component of the Bank's strategy. For example, in line with the expectations of the European Central Bank (ECB) and the European Banking Authority (EBA), the Risk Controlling department is working towards making sustainability aspects, and most importantly environmental and climate risks, more integral components of the risk management system.

Separate non-financial report

MünchenerHyp has been reporting on the non-financial aspects and the material economic, environmental and social impacts of its business activities since 2012. We comply with the requirements set out in the German CSR Directive Implementation Act (CSR-Richtlinie-Umsetzungsgesetz – CSR-RUG) by publishing a non-financial report. The non-financial report is published at the same time as the annual report on the Bank's website and in the electronic Federal Gazette (Bundesanzeiger).

Regulatory conditions

Capital

MünchenerHyp calculates its capital requirements largely using the internal ratings based approach (IRBA). The ECB's Targeted Review of Internal Models (TRIM) confirmed the correct application of these models and the suitability of the systems.

The Liquidity Coverage Ratio (LCR) was maintained without issue throughout the year, with values above 300 percent on average. The minimum was 148 percent. The Net Stable Funding Ratio (NSFR), which the Bank did not yet have to meet in 2020, averaged 101.2 percent.

Basel III also introduced a leverage ratio, which must be met. At the end of financial year 2020, MünchenerHyp reached a leverage ratio of 3.6 percent.

The "finalisation" of Basel III also includes a gradual introduction of an output floor of 72.5 percent to limit the effects of internal approaches compared with standard approaches. This means that in particular banks with low risk weightings for their receivables, such as MünchenerHyp, will be adversely affected by the changes. The introduction of this floor will also impact MünchenerHyp's capital ratios. Overall, we take a critical view of this new regulation, because it will make lending more expensive. The Bank is monitoring developments and, given the currently high Common Equity Tier 1 ratio of 20.6 percent, believes that this regulatory change will be manageable.

The Bank's Compliance unit follows discussions on the publication of new national and international regulations very closely and forwards any new regulations to the responsible departments within the Bank, where they are implemented in various measures and projects. The abundance of additional regulatory requirements imposed by supervisory authorities causes significant costs and poses a considerable challenge for our Bank's human and financial resources.

Single Supervisory Mechanism for EU banks
During the reporting year the ECB conducted the annual Supervisory Review and Evaluation Process (SREP) only to very reduced extent, comprising generally a detailed evaluation of the business model, internal governance and capital and liquidity adequacy. Any additional capital and liquidity requirements may be derived from that process. In 2020, however, the ECB has decided not to issue a new notice as a rule, but generally to adopt the one from the previous year. As part of the SREP, the additional capital requirement (P2R) remains unchanged 1.5 percent of total capital; no additional requirements were set for liquidity.

Minimum requirements for risk management (MaRisk)
German minimum requirements for risk management under MaRisk (Mindestanforderungen an das Risikomanagement) remained unchanged in the year under review. The sixth amendment is currently in the consultation phase.

Recovery and resolution plan
The recovery plan was updated and the information required for the resolution plan was sent to the resolution authority. There were no significant changes compared with the previous year.

IBOR reform
IBOR interest reference rates came under heavy criticism in the wake of the manipulation scandals a few years ago; at the same time, the abolition of the submission obligation for panel banks made it necessary to replace the LIBOR rates. Alternative risk-free rates (RFRs) are currently being developed and established; existing IBOR reference rates are being replaced based on the new RFR benchmarks.

MünchenerHyp is affected both by the announced changes in relation to the interest rate benchmarks and by the Benchmarks Regulation. However, due to the highly specialised business model, there is much less of a need for change than for most other banks directly supervised by the ECB. The necessary adjustments are being undertaken as part of a project, with everything going to plan so far.

REGISTERED OFFICE, EXECUTIVE BODIES, COMMITTEES AND EMPLOYEES

Registered office

Münchener Hypothekenbank eG has its registered office in Munich. The Bank also has a branch in Berlin and 10 regional offices.

Executive bodies and committees

Ulrich Scheer (52) was appointed General Executive Manager of MünchenerHyp effective 1 September 2020. The Supervisory Board intends to appoint Ulrich Scheer to the Board of Management of MünchenerHyp after a preparatory period and once this has been approved by the banking supervisory authorities.

Employees

The top priority of our human resources work last year was the health of our employees. The Bank established a crisis team early on after the outbreak of the COVID-19 pandemic and it has met more than 30 times in the last twelve months. The crisis team, whose work is based on professional business continuity management, has taken all necessary measures to protect the workforce depending on the prevailing situation. As well as implementing hygiene regulations, the option for employees to work from home, in particular, was expanded on a large scale, meaning that a good half of the workforce was able to work from home when use of this model was at its peak. Since March 2020, a total of 14 colleagues have been infected with the coronavirus. All of them have since recovered. Moreover, there was not a single case in which an individual was infected within the Bank.

Even in a year marked by the COVID-19 pandemic, recruitment was at the forefront of our human resources work. A total of 94 new employees were recruited to fill vacancies. A key focus of human resources work in the reporting year was therefore once again on the integration of new employees. The number of new hires necessary was also driven by 60 employees leaving the Bank (excluding employees who retired). With an employee turnover rate of 9.2 percent – excluding employees retiring – the Bank is slightly above the industry average.

Further human resources work focused on enhancing our employer brand, as well as on initial training and further professional development.

The Bank employed 611 employees[9] (previous year: 573) and 15 apprenticed trainees (previous year: 15) on average over the year. The average length of service remains unchanged at 10.4 years.

Corporate governance statement in accordance with Section 289f HGB

The proportion of women in the Bank as a whole was 50 percent in the reporting year. At Board of Management level, the proportion came to 0 percent, while the proportion at the first management level below the Board was 16 percent, at the second level 20 percent and at the third level 37 percent. The proportion of women on the Supervisory Board was 17 percent in 2020. MünchenerHyp has set itself the objective of increasing the proportion of women in management positions. For the Supervisory Board and the two management levels below the Board of Management, the Bank is aiming for a proportion of women of 20 percent, with a target quota for the Board of Management of 33 percent. In December 2020, the Nomination Committee of MünchenerHyp's Supervisory Board addressed the issue of the proportion of women on the Board of Management and Supervisory Board and decided to retain the existing target quotas and to strive to achieve them by 2026 in the context of upcoming succession arrangements.

[9] Number of employees in accordance with Section 267 (5) HGB; excludes trainees, employees on parental leave, in early retirement or in partial retirement (non-working phase)