MünchenerHyp

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Half Year Financial Statements 2017
Münchener Hypothekenbank eG

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INTERIM MANAGEMENT REPORT 2017

OVERALL ECONOMIC CONDITIONS

ECONOMIC DEVELOPMENT

The recovery of the global economy remained intact, even though growth slowed a bit in the first quarter due to declining rates of growth noted for production and consumption in the USA during the first quarter. On an overall basis, however, economic development in both the advanced economies and emerging countries continued to expand in the first half of 2017.

The economic recovery in the eurozone gained additional momentum as the cumulative gross domestic product (GDP) recorded for the first quarter of 2017 rose by 0.5 percent over the previous quarter. The primary drivers behind this growth were consumer spending and gross investments in fixed assets. Spain and Germany played a particularly important role in accelerating the pace of economic growth in the eurozone. Economic growth within the European Union (EU) picked up in the second quarter leading to a 0.6 percent expansion in the EU's GDP.

Germany's GDP rose by 0.6 percent over the previous quarter with growth mainly driven by expansion in the construction and industrial sectors. Mild weather conditions were the primary factor behind a 2.3 percent increase in investments in construction projects. Investments in commercial property construction projects posted a strong gain of 4.8 percent while, in contrast, investments in housing construction only grew by 0.8 percent. In view of the favourable economic and sentiment indicators initial assessments by economic experts foresee GDP also rising by 0.6 percent in the second quarter.

Consumer prices increased at a faster pace during the first half of 2017 compared to the rise noted in the same year-ago period. The rate of inflation recorded for June was 1.6 percent. The German job market continued to develop favourably as the number of employed persons had risen to 44.2 million in June while the jobless number declined below 2.5 million, which is equivalent to an unemployment rate of 5.5 percent. The unemployment rate twelve months earlier was still 0.4 percentage points higher.

FINANCIAL MARKETS

The American central bank (the Fed) took advantage of overall favourable economic conditions to raise its key interest rate by 25 basis points in March and again in June to its current target rate range of 1.0 to 1.25 percent. Other significant central banks, especially the European Central Bank (ECB), the Bank of England, the Bank of Japan and the Swiss National Bank, maintained their interest rate policies and did not raise their rates. However, the ECB and die Bank of England hinted that the robust economy could justify a slight reduction in measures designed to stimulate the economy. The market interpreted these kinds of remarks to mean that the period of extremely loose monetary policies was coming to an end.

Against this background bond yields indicated notable gains as 10-year Bunds rose by about 25 basis points during the first half of 2017 to 0.47 percent. In contrast, markets calmed in the USA following the sharp rise in US Treasuries seen after the election of Donald Trump as expectations that the new president would enact measures to stimulate the economy proved to be overblown. Yields of 10-year government bonds fell slightly during the period under review from 2.44 percent to 2.30 percent.

Covered bonds, and thus German Pfandbriefe, continued to benefit from the ECB's Covered Bond Purchase Programme as the ECB bought about one-third of the volume of all bonds issued during the first half of 2017. This high demand ensured that issuing levels remained at an attractive level for issuers. However, the dominance of the purchase programme continued to make it difficult for classical Pfandbrief investors to maintain their portfolio levels. As a result, the available level of tradable covered bonds declined further in the first half, which in turn further limited liquidity in the secondary market. During the first half of the year a total volume of € 75 billion in euro-denominated benchmark covered bonds were issued, which was a significantly lower volume than in the same year-ago period, although still higher than the average figure recorded for the past five years. The biggest shares of new issues were held by issuers based in France and Germany.

The German stock market began 2017 at about 11,500 points and rose to a high of almost 13,000 only to see the DAX index fall by the end of the first half of the year to 12,325 points for a gain of a good 7 percent since the start of the year. Stock markets were also generally favourable around the world as the Dow Jones index rose by over 7 percent during the first six months to 21,350.

The euro's exchange rate was supported by economic developments within the eurozone, as well as the French election results. Above all, the single European currency rose against the US dollar by over 8 percent as it climbed from 1.05 to 1.14 US dollars. In addition, the euro also increased in value vis-a-vis the Swiss franc and the British pound during the first half of the year.

PROPERTY AND PROPERTY FINANCING MARKETS

RESIDENTIAL PROPERTY – GERMANY

As expected, the upswing in the German residential property market continued into the first half of 2017. This situation was most clearly visible in the development of prices paid for single-family homes and condominiums. According to figures prepared by the Association of German Pfandbrief Banks (vdp), purchase prices in this market segment rose by 5.6 percent in the first quarter of 2017. This increase was mainly driven by higher prices for condominiums, especially in major cities and surrounding regions where potential buyers remained very keen on condominiums although supply in these areas was extremely tight. The higher-price sector was dominated by financially powerful private foreign investors.

In view of continuing discussions concerning the formation, or existence, of a property bubble in Germany, the Financial Stability Committee reviewed this issue in its fourth report covering the development of residential property prices, with special focus on credit volumes, lending standards, and building activity. The review concluded that there are still no signs of developments that could pose a threat to financial stability.

The Committee did, however, decide to create new instruments that would tighten lending standards for the purpose of dampening new business demand in order to avoid systemic risks in the residential property market. These instruments were anchored in laws.

Developments noted during the first five months of the year did not, however, indicate any signs of greater risks of a property bubble forming. The development of new business in the property financing sector is not contributing to an overheating of the residential property market at this time. Although the Bundesbank did note a further 3 percent increase in new business (including prolongations) in the first five months of 2017, the expansion of credit is not unusually high when viewed on a historical basis.

The number of building permits issued in the first five months unexpectedly declined as permits were only issued for about 137,000 housing units, or nearly 8 percent less than the same year-ago figure. Declines were particularly noted for single family homes, as well as permits to build homes including refugee housing, while the number of permits issued to build rental housing and condominiums continued to rise (+4 percent).

Institutional investors were also quite keen on residential property as turnover of residential property portfolios and large multi-family houses amounted to about € 5.9 billion, or € 1.4 billion more than the same year-ago figure. This increase was attributable to the high share of large-volume transactions over € 100 million which in total represented about 50 percent of the entire volume invested. The top 7 cities remained the focal point of investor interest in Germany with Berlin clearly dominating this segment. Project developments increasingly moved to the forefront of investor interest in light of the unchanging very tight supply of properties. This sector generated about € 1.9 billion in turnover, or almost one third of the volume of transactions.

Overall the residential investment market continued to be dominated by domestic investors although international players were increasingly pushing into the market. This development was particularly visible in the sub-segment of student housing and micro-apartment complexes.

Prices continued to rise further in the residential property investment market due to heavy pressure exerted on investors seeking to invest, which in turn led to further slight declines in initial net yields, as well as the unbroken tight situation in the residential rental market in many locations. According to vdp figures, prices for multi-family houses rose by 6 percent in the first three months of 2017 over the same year-ago figure.

RESIDENTIAL PROPERTY – INTERNATIONAL

Prices for residential property also continued to rise internationally, and in some cases at an even notably faster pace than in the previous year. Prices paid for houses in the Eurozone in the first quarter of 2017 rose by 4 percent and 4.5 percent across the EU.

The British housing market continued to grow. Demand for residential property was high due to low mortgage rates while supply was very tight because of insufficient new construction. As a result of these factors housing prices in May 2017 were 4.7 percent more expensive than they were twelve months earlier and reflected a notably faster pace of rising prices. At the same time, however, there were significant regional differences.

According to the Federal Office of Housing (BWO), on average the Swiss housing market is showing of a slight easing for the first time since 2008. A contributing factor towards this development is a notable upswing in new construction of rental properties, which has caused prices to continue weakening slightly. The SWX IAZI Private Real Estate Price Index for single-family houses and condominiums rose by 0.7 percent in the second quarter of 2017 while prices for multi-family houses sold in the same period increased by 1 percent. Substantial imbalances did, however, remain at regional level. Zurich and area around the city has become the region with the tightest housing situation in Switzerland.

Overall favourable economic conditions and a still low level of interest rates have generated a further increase in demand for residential housing, which in turn has led to a continued rise in prices across the country. The S&P/Case Shiller Index figures for April 2017 showed a year-over-year increase of 5.5 percent, with notable regional differences. For example, the pace of price increases in Portland and Washington D.C. areas has slowed substantially while the pace has quickened in Seattle and Miami.

COMMERCIAL PROPERTY – GERMANY

During the first half of the year the commercial property investment market in Germany reported unexpected inflows of capital: nearly € 26 billion was invested in commercial property, or 47 percent more than in the same year-ago period. At the same time it was the highest volume of transactions reported to this date since 2007. The liquidity level in the market was behind the upswing, which meant that pressure to invest remained very high as interest rates remained low. This also meant that investors were ready to accept higher prices for commercial properties despite falling returns. In addition, these developments also showed that owners of commercial properties were benefiting from higher prices for their properties and took advantage of the opportunity take profits by selling them.

Furthermore, the trend favouring peripheral property locations also remained intact. Although the top 7 cities accounted for over € 12 billion of the volume of transactions completed, or nearly half, growth in regions outside of these major metropolitan areas was, however, notably stronger. Moreover, specialised properties, like hotels and logistical properties, which investors used to view with less interest, are currently experiencing a substantial upswing. Transactions involving logistics properties, in particular, have increased. This market segment represented four of the five largest transactions.

The strong interest shown by foreign investors in German property was also a major factor behind the increase in the volume of transactions as this group represented a nearly 50 percent share of the market during the first half of the year. Above all, Asian investors, who preferred to conclude large-volume purchases, expanded their activities in Germany.

German commercial property also retained its strong appeal for domestic investors as the unbroken low level of interest rates continued to leave them with hardly any investment alternatives. This led to heightened competition among investors, which in turn led to high demand which generated a further significant rise in prices. During the first quarter of 2017 the vdp index for commercial property rose by 6.7 percent. This strong increase was primarily driven by the above-average development noted for the office properties segment of the market. Prices recorded in this segment climbed by 8.4 percent compared to the same year-ago quarter.

The situation in the user market is the reason why prices have developed in this manner. During the first six months renters/occupier-users demand for office space in the top 7 markets totalled about 1.8 million square meters of space, or more than 17 percent higher than the average figure for the past five years. At the same time the vacancy rate fell to about 5 percent as new construction activity could not keep pace with the development of demand.

Furthermore, office rents became substantially more expensive as a result. Against this background it is not surprising that investors intensified their focus on office properties. Due to the fact that prices increased faster than rents, yields fell slightly until the middle of the year and once again fell to a historic low.

The Financial Stability Committee critically analysed rising prices in the commercial property sector as declines in demand and their collateral effects led to credit defaults in the past. In order to limit systemic risks the observance of lending standards is the focal point of a macro-prudential supervision. At the same time, as the result of its analysis, the Committee does not see any signs of the formation of systemic risks within the market that could threaten financial stability.

COMMERCIAL PROPERTY – INTERNATIONAL

During the first quarter of 2017 about € 56 billion was invested in commercial properties across Europe. This volume was similar to the same year-ago level. Demand was focused on office properties, which accounted to € 23 billion of total transactions, or just slightly less than the same year-ago figure. The second largest investment category was retail properties, with transactions valued at nearly € 13 billion, or 20 percent more than recorded in the previous year.

However, when viewed on a country-by-country basis there were noteworthy differences. Great Britain maintained its role as the most favoured investment market, although the volume of recorded transactions did, however, decline by almost 20 percent. This reflected the continuation of investors' hesitancy, which began immediately after the Brexit referendum. Investors focused on office properties in central London. The difference between the volume of transactions in the UK and Germany – the second largest European investment market – thus narrowed.

The previous third-ranked European investment market, France, fell to fifth place due a substantial decline in investments. It is currently ranked behind Sweden and Spain, which posted new record turnover figures in the first quarter of 2017.

Activities in the US investment market declined further. Just in the first quarter of 2017 alone the volume of transactions was almost 20 percent below the same year-ago figure. The decline was mainly due to the lack of mega-deals during this period. Preferred investment locations were Los Angeles, Manhattan, Boston and Dallas, with a clear focus on office properties. Following a slow start at the beginning of the year the office rental market regained its solid position, although it did not reach its previous year's results.

BUSINESS DEVELOPMENT

NEW MORTGAGE BUSINESS

We were able to expand our new business to a far greater extent than expected due to the unchanged high demand for residential and commercial property financing. During the first half of the year the volume of new lending commitments made rose by 19 percent to almost € 2.8 billion.

About half of our new business, or nearly € 1.4 billion, was generated by our brokerage business with cooperative partner banks in the area of residential property financing. This figure represents an increase of 4 percent over the same year-ago period.

Turnover of private residential property financing generated with independent providers of financial services declined slightly from the € 235 million noted in the first half of 2016 to € 223 million. Loans brokered via Swiss PostFinance increased by 15 percent to € 171 million. Following weaker development noted in the previous year this growth shows we were able to once again expand our market position thanks to our joint sales activities with PostFinance.

Our commercial property finance business developed quite favourably with the strong pace of growth noted at the end of our 2016 business year still intact. The number and related volumes of financing inquiries remained at a constant high level. During the first half of the year we concluded almost exactly € 1 billion in new business transactions, or 62 percent more than in the same year-ago period. Although the main emphasis of our new business was related to providing financing in Germany, we booked higher growth for our foreign business dealings, especially for financing transactions in Great Britain, the Netherlands and France.

Our syndication business benefited from the good market situation, whereby the existing demand for loan participation substantially exceeded the supply of available financing. We were able to establish ourselves quite well in this environment within the national and international syndication markets. Furthermore, we were able to pass on portions of our own financing deals to partners. We also participated in large-volume loans to third parties both within Germany and abroad.

CAPITAL MARKETS BUSINESS

Münchener Hypothekenbank continues to conduct its capital markets business on a cautious basis in accordance with our business and risk strategy. Hardly any new investments were made during the period under review. The majority of the major maturities were not replaced, which reduced our portfolio by € 0.7 billion to € 6.1 billion.

REFINANCING

We refinanced our business at very good conditions and exceeded the previous year's volume. The liquidity flowed into our new business as no large-volume bonds matured in the first half of the year.

Our emphasis during the first months of the year was on private placements, especially Mortgage Pfandbriefe. For this reason, we only issued our first benchmark issue of this year in early May. The 10-year Mortgage Pfandbrief with a volume of € 500 million and coupon of 0.625 percent was well received by investors and was in great demand. As a result, its price was set at twelve basis points below the mid-swap rate. Up until this point in time this Mortgage Pfandbrief was most expensive 10-year Pfandbrief of 2017. The order book contained 34 orders from nine countries. The investors consisted primarily of central banks and banks, with geographic focus on investors based in Germany.

We issued two larger Mortgage Pfandbriefe during the first half of the year to refinance our Swiss business activities. The Pfandbriefe had volumes of 250 million and 300 million Swiss francs and once again demonstrated our good access to the market for Swiss francs.

Furthermore, during the first half of the year we began to expand our refinancing mix by accepting customer deposits via our cooperative partner banks. We successfully tested the product we developed for this purpose during a pilot phase with selected banks.

At the end of the first half of the year we had issued a volume of € 2.9 billion worth of paper of which € 2.4 billion were Mortgage Pfandbriefe and the remaining € 0.5 billion were uncovered bonds. Due to the Bank's strategic direction, we did not issue any Public Pfandbriefe.

ASSET, FINANCIAL AND EARNINGS SITUATION

BALANCE SHEET STRUCTURE

Total assets on 30 June 2017 amounted to € 39.1 billion, following € 38.5 billion at the end of 2016.

We were again able to expand our portfolio of mortgage loans. As of 30 June 2017 it had risen by € 0.8 billion to € 28.6 billion. In line with our strategy we reduced the capital markets portfolio by € 0.7 billion to € 6.1 billion. Unrealised losses for securities held as fixed assets amounted to € 4 million, while silent reserves amounted to € 49 million.

Equity capital as shown on the balance sheet amounted to € 1,301.5 million. Liable equity capital pursuant to the terms of the Capital Requirements Regulation (CRR) was € 1,381.1 million. This provided the Bank with a Common Equity Tier 1 capital ratio of 23.7 percent at the mid-year point following 22.9 percent recorded at the end of 2016. The Tier 1 capital ratio was also 23.7 percent (31.12.2016: 22.9 percent) and the total capital ratio was 25.2 percent (31.12.2016: 24.5 percent).

At the mid-year point of 2017 the leverage ratio was the same as it was at the end of 2016: 3.4 percent.

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

	Remaining term < one year	Remaining term > one year	Total
	€ 000	€ 000	€ 000
Other liabilities to customers as of 30 June 2017	**575,776**	**2,408,611**	**2,984,387**
Registered bonds	**12,902**	**1,201,345**	**1,214,247**
of which institutional investors	12,698	1,180,345	1,193,043
Promissory note loans on the liabilities side	**264,953**	**1,207,266**	**1,472,219**
of which institutional investors	64,859	1,062,065	1,126,924
Other	**297,921**	**0**	**297,921**
of which institutional investors	180,675	0	180,675

DEVELOPMENT OF EARNINGS

Net interest income[1] rose by 12 percent over the figure recorded at the end of first half of 2016 to € 124.8 million. The net commission balance[2] totalled minus € 38.3 million. The figure for net interest income and net commission income[3] was € 86.5 million, or 15 percent more than the same year-ago amount. Administrative expenses[4] rose by € 0.6 million to € 47.7 million with personnel costs rising by € 1.1 million to € 23.0 million.

Other administrative expenses fell by € 0.2 million to € 21.7 million. Depreciation and write-downs of intangible and tangible assets amounted to € 3.0 million, or € 0.3 million lower than the same year-ago figure.

The item "Write-downs and adjustments to claims and certain securities and additions to provisions for possible loan losses" totalled minus € 3.4 million compared to minus € 3.9 million on the same year-ago date. At the mid-year point the item "Income from appreciation in value on participations, shares in affiliated companies and securities treated as fixed assets" amounted to € 4.8 million.

Due to the good new business results and the favourable business performance in the first half of the year we were able to increase our results from normal business operations by € 10.7 million to € 37.8 million. After deduction of € 15.7 million for tax expenses, we recorded a pro rata temporis net income for the year of € 22.1 million (previous year: € 14.6 million).

1) Interest income is calculated by adding item 1 interest income plus item 3 current income less item 2 interest expenses as shown on the income statement.
2) Net commission balance is the net sum of item 4 net commission income plus item 5 net commission expenses as shown on the income statement.
3) Net interest and net commission balance is the sum of net interest income and the net commission balance.
4) Administrative expenses are the sum of item 7 general administrative expenses and item 8 depreciation and adjustments to the value of intangible and tangible assets as shown on the income statement.

RATING, SUSTAINABILITY AND REGULATORY CONDITIONS

RATING

The rating agency Moody's confirmed their ratings for MünchenerHyp in their most recent Credit Opinion of June 2017.

Our current ratings at a glance:

	Rating
Public Pfandbriefe	Aaa
Mortgage Pfandbriefe	Aaa
Senior unsecured liabilities	A1
Short-term liabilities	Prime-1
Long-term deposits	Aa3

Furthermore, our long-term uncovered liabilities are rated AA- by the rating agency Fitch due to the group rating the agency assigned to the Cooperative Financial Network.

SUSTAINABILITY

At the beginning of 2017 the sustainability rating agency imug confirmed all of their sustainability ratings for MünchenerHyp. Our Public Pfandbriefe are rated "very positive", Mortgage Pfandbriefe "positive", uncovered bonds were also rated "positive". Our Mortgage Pfandbriefe are rated the best among the 30 German issuers rated by imug.

BODIES AND PERSONNEL

BODIES AND PERSONNEL

Josef Hodrus, spokesman of the Board of Management of the Volksbank Allgäu-Oberschwaben eG, was elected by the Delegates Meeting as a new member of MünchenerHyp's Supervisory Board.

At the close of the Delegates Meeting, Heinz Fohrer, member of the Board of Management of the Volksbank Esslingen eG, stepped down from the Supervisory Board. The Chairman of the Supervisory Board, Wolfhard Binder, thanked Heinz Fohrer for his dedication and efforts during years when the Bank faced numerous regulatory challenges.

EMPLOYEES

The Bank's earnings-oriented growth strategy, as well as the numerous regulatory requirements continue to necessitate that we hire additional personnel, although at a more moderate pace. Moreover, our personnel requirements were also influenced by higher fluctuation. By the half-year mark we had hired 32 new employees.

The development of our sustainability ratings at a glance:

	2014	**2015**	**2016/2017**
oekom research	C	C	C+
imug	Public Pfandbriefe: very favourable Mortgage Pfandbriefe: neutral Uncovered bonds: neutral	Public Pfandbriefe: favourable Mortgage Pfandbriefe: neutral Uncovered bonds: neutral	Public Pfandbriefe: very favourable Mortgage Pfandbriefe: favourable Uncovered bonds: favourable
Sustainalytics	**47 of 100 points**	**57 of 100 points**	**57 of 100 points**

CORPORATE PLANNING

CORPORATE PLANNING

The business and risk strategy defines the formal planning framework for MünchenerHyp's key business activities and is regularly reviewed. The Bank's business strategy remains focused on the earnings-driven growth of our mortgage portfolio and a successive reduction of our lending business with the public sector and banks. Minor adjustments to our risk strategy were made during the period under review.

OUTLOOK

OUTLOOK – OPPORTUNITIES AND RISKS

At the mid-point of 2017 forecasts made by economic experts conveyed confidence. Expectations have risen since the start of the year as growth of the global economy has consolidated. Nevertheless, uncertainties remain, especially those surrounding future economic policy in the USA, protectionist tendencies and volatility in the financial markets. At this time these uncertainties are not yet having a noticeable effect on the upswing of the global economy. For this reason, the International Monetary Fund (IMF) already acted in April and raised its outlook for the global economy in 2017 by 0.1 percentage points to 3.5 percent. The IMF's forecast for 2018 remains unchanged at 3.6 percent.

Experts anticipate that the economic recovery in the eurozone will continue to consolidate further. Forecasts for the eurozone were recently raised in view of rising private consumption, lower unemployment figures and rising capital expenditures. The IMF now expects GDP to rise by 1.9 percent in 2017 and by 1.7 percent in 2018.

Forecasts for the German economy are also favourable. On average economic experts predict that it will grow by 1.7 percent in both 2017 and 2018 and be supported by exports, which in turn will benefit from the upbeat global economy. In addition, the domestic economy is also forecast to grow at a lively pace. Private consumption will continue to grow and be supported by continually rising incomes. Investments are also foreseen to expand at an even stronger pace. This applies especially to investments in construction, which are predicted to increase by 3.4 percent in the current year. Good economic conditions will continue to have a further favourable impact on the labour market as the average annual unemployment rate is forecast to fall to 5.7 percent in 2017.

The financial markets are currently focused primarily on one question: when will the ECB begin to unwind their expansive monetary policy, and how will it take place? In general, it is expected that the ECB will begin to taper their quantitative easing programme in early 2018. It may then be expected that the interest rate curves in Europe will steepen a bit and the very low spreads the markets are currently seeing – for example for covered bonds, sovereign bonds and corporates – are likely to become history. At the same time it may be assumed that ECB will not lift its deposit rate out of the negative area as it is anticipated that inflation is more likely to develop moderately.

In the USA it appears likely that the Fed will begin to reduce its balance sheet this year. It may also be assumed that in view of the dampened outlook for inflation the Fed is more likely to move cautiously in raising interest rates any further.

As far as the covered bond markets are concerned it is expected that central banks will reduce their share of purchases of new bond issues in the second half of 2017. This move would lead to wider spreads and somewhat higher bond yields. This would also make covered bonds more attractive to investors once again. This means that the market environment for Pfandbriefe and other covered bonds is likely to remain favourable. Experts anticipate that about € 120 billion in euro-denominated covered bonds will be issued.

Despite the discussions surrounding the end of expansive monetary policy we anticipate that property finance interest rates in the second half of 2017 will rise moderately, although rates will remain at a very low level. For this reason, the overall conditions in the property and property finance markets will not change substantially.

Demand for residential property will remain strong in major metropolitan areas and large cities. Demand for rental property currently exceeds supply, especially in the major metropolitan areas. Despite rising completion rates for new housing the market has been unable to substantially reduce excess demand. As a result, purchase prices for condominiums and single-family homes, as well as rents paid for residential properties in the aforementioned regions will rise further. This is more likely to occur as consumer prices are likely to once again increase strongly. The pace of price increases for residential property may gradually weaken in the coming years if construction of new housing units continues to rise further as it has in previous years thereby leading to a balance between supply and demand.

The German commercial properties market, and the office market in particular, will benefit from positive economic conditions. Rising employment figures are strengthening demand so that against the background of limited new construction activity office vacancy rates can decline further and in some segments lead to the formation of excess demand. As long as this trend continues and the low level of interest rates does not offer alternate investment opportunities, investing in commercial property in Germany will remain popular among investors. Accordingly, it may be anticipated that yields will remain generally stable or slightly lower and correspond with higher prices. For this reason, higher turnover figures in the investment market are also expected in the second half of the year. Against this background experts foresee that the volume of transactions in 2017 will be € 60 billion.

The European property investment market will also continue to benefit from the low interest rate environment. Coupled with the very high level of liquidity in the market, demand for property will remain at a very high level. In this scenario Germany will be able to further reinforce its position in the European investment market as Brexit is expected to dampen development in Great Britain, and especially in the office market. Brexit will also impact the housing market where it is likely to further slow the pace of rising prices. The first signs of this are already visible in London where tempo of rental prices is increasingly slowing down.

The development of prices in the Swiss housing market is likely to weaken further as incomes and rents paid for residential property currently show no potential to increase. These factors coupled with the fact that new construction activity is gaining momentum indicate a risk of falling prices. The greatest danger of overheating is currently seen in Zurich and central Switzerland.

Future developments in the USA remain clouded by uncertainty. The IMF does not expect that the foreseen increases in government spending coupled with lower taxes will accelerate economic growth. Nevertheless, overall conditions remain positive for the housing market, as well as the commercial property market, with prices expected to rise in both segments. However, pace of rising prices paid for office properties is likely to slow in certain regions.

In view of the unchanged good overall conditions we are confident that we will also be able to successfully expand our new business over the course of the entire year, as predicted in the 2016 Annual Report.

In our collaboration with the cooperative banks we want to use a high-profile sales campaign and improved service offers to further expand the very good results we reported for the first half of the year. We anticipate that our brokerage business with independent providers of financial services will result in stable to positive results in the second half of the year. We await that this we will enable us to achieve a slight increase in sales for the full year 2017 so that sales via this channel will exceed last year's performance. We expect that our business with PostFinance will continue to develop successfully due to high demand for property loans in Switzerland and ongoing joint sales activities. We will retain our conservative lending standards in all of these activities.

We expect that our new commercial property finance business will continue to develop favourable and that we will record a higher volume of new lending commitments than in the previous year. This forecast applies to both our domestic and international areas of business. In the international segment we anticipate greater volumes of business to be generated by Spain, the Netherlands and France. We believe that the inflow of business from Great Britain will slow to a certain extent due to the uncertain outcome of the Brexit negotiations. The unbroken market trend of low margins and a willingness to accept higher risks in the commercial property financing sector may, however, have an impact on our new business as we are hesitant to accept higher risks due to strategic risk reasons.

During the second half of 2017 we plan to re-enter the American market to participate in syndication business. Beyond this we will increasingly involve partner banks from the Cooperative Financial Network in syndication deals in Germany.

The reduction of our portfolio of assets in the banks and the public-sector segment, which primarily serves to manage liquidity and our cover pool is likely to slow in the second half of the year.

Our liquidity requirements for 2017 will – as planned – amount to about € 7 billion. Mortgage Pfandbriefe remain our most important source of refinancing. We plan to issue at least one additional benchmark issue in the second half of the year. Furthermore, we will continue to examine the issuance of a new sustainable Pfandbrief. In addition, we want to realise the potential offered by foreign currencies – with a continued focus on the Swiss franc. In the area of large-volume maturities, a Public Pfandbrief with a nominal value of over € 500 million will mature in September.

As part of our activities to attract customer deposits via cooperative partner banks we plan to develop additional tranches with varying terms within the expanded pilot phase.

We anticipate that the favourable development of business noted in the first half of the year will continue and we will substantially achieve our business targets for 2017.

We are striving to achieve a net income for the 2017 business year that will exceed the previous year's performance.

DISCLAIMER REGARDING FORWARD-LOOKING STATEMENTS

This Half Year Financial Statements contain statements concerning future expectations and forecasts. These forward-looking statements, especially those pertaining to the development of MünchenerHyp's business and income, are based on our planned assumptions and estimates and are subject to risks and uncertainties. There are a number of factors that could affect our business. These include, above all, economic developments, the state and further development of the financial and capital markets in general and our refinancing conditions in particular, as well as unexpected defaults on the part of our borrowers. Therefore, the actual results and developments may vary from the assumptions that we have made today. For this reason, they are only valid at the time this report was prepared.

BALANCE SHEET AS OF 30 JUNE 2017

ASSETS		30 June 17	31 Dec 16
	€	€	€ 000
1. Cash reserve			
a) Cash on hand	11,927.98		19
b) Balances with Central Banks	29,990,964.36		291,634
of which			
with Deutsche Bundesbank € 29,990,964.36			
		30,002,892.34	**291,653**
2. Claims on banks			
a) Mortgage loans	8,650,181.88		9,987
b) Public-sector loans	243,001,372.64		343,041
c) Other claims	2,550,731,933.66		2,626,199
of which			
payable on demand € 1,290,563,526.12			
		2,802,383,488.18	**2,979,227**
3. Claims on customers			
a) Mortgage loans	28,500,139,203.17		27,707,189
b) Public-sector loans	3,341,018,048.92		3,597,899
c) Other claims	224,621,206.77		46,627
		32,065,778,458.86	**31,351,715**
4. Bonds and other fixed-income securities			
a) Bonds and notes	2,549,256,184.41		2,936,256
aa) Public-sector issuers € 1,338,786,282.51			(1,422,146)
of which			
eligible as collateral for Deutsche Bundesbank advances € 1,234,693,980.43			
ab) Other issuers € 1,210,469,901.90			(1,514,110)
of which			
eligible as collateral for Deutsche Bundesbank advances € 1,096,461,871.15			
b) Own bonds and notes	1,101,051,376.38		600,000
Nominal value € 1,101,000,000.00			
		3,650,307,560.79	**3,536,256**
Carried forward:		38,548,472,400.17	38,158,851

LIABILITIES, CAPITAL AND RESERVES		30 June 17	31 Dec 16
	€	€	€ 000
1. Liabilities to banks			
a) Registered Mortgage Pfandbriefe issued	784,200,920.24		663,345
b) Registered Public Pfandbriefe issued	157,518,971.43		127,368
c) Other liabilities	4,234,154,574.51		3,815,153
of which			
payable on demand € 991,150,082.92			
		5,175,874,466.18	**4,605,866**
2. Liabilities to customers			
a) Registered Mortgage Pfandbriefe issued	9,098,538,141.31		8,782,709
b) Registered Public Pfandbriefe issued	2,320,663,956.05		2,710,773
c) Other liabilities	2,984,387,138.78		3,497,502
of which			
payable on demand € 26,478,150.32			
		14,403,589,236.14	**14,990,984**
3. Certificated liabilities			
a) Bonds issued	17,378,980,721.24		16,228,040
aa) Mortgage Pfandbriefe € 12,552,580,302.17			(11,009,435)
ab) Public Pfandbriefe € 1,721,130,193.99			(1,968,997)
ac) Other bonds and fixed income securities € 3,105,270,225.08			(3,249,608)
b) Other Certificated liabilities	113,092,843.58		699,618
of which			
money market paper € 113,092,843.58			
		17,492,073,564.82	**16,927,658**
4. Liabilities incurred as trustee		**16,412.65**	**21**
of which			
loans € 16,412.65			
5. Other liabilities		**404,940,398.56**	**406,989**
Carried forward:		37,476,494,078.35	36,931,518

ASSETS		30 June 17	31 Dec 16
	€	€	€ 000
Brought forward:		38,548,472,400.17	38,158,851
5. Equities and other variable-yield securities		**155,177,430.37**	**12,336**
6. Participations and shares in cooperatives			
a) Participations	104,535,199.49		104,535
of which			
credit institutions € 22,955,936.29			
b) Shares in cooperatives	18,500.00		19
of which			
in credit cooperatives € 15,500.00			
		104,553,699.49	**104,554**
7. Shares in affiliated companies		**11,151,601.64**	**11,152**
8. Assets held in trust		**16,412.65**	**21**
of which			
loans € 16,412.65			
9. Intangible assets			
Concessions acquired for consideration, commercial rights and similar rights and values, as well as licenses to these rights and values	5,827,644.32		4,339
		5,827,644.32	**4,339**
10. Tangible assets		**70,517,877.15**	**71,090**
11. Other assets		**104,822,968.36**	**100,365**
12. Deferred items			
a) From issuing and lending business	43,315,548.85		46,285
b) Other	7,341,000.00		0
		50,656,548.85	**46,285**
Total assets		**39,051,196,583.00**	**38,508,993**

LIABILITIES, CAPITAL AND RESERVES		30 June 17	31 Dec 16
	€	€	€ 000
Brought forward:		37,476,494,078.35	36,931,518
6. Deferred items			
From issuing and lending business	27,146,983.28		23,539
		27,146,983.28	**23,539**
7. Provisions			
a) Provisions for pensions and similar obligations	29,538,447.00		28,838
b) Provisions for taxes	0.00		30
c) Other provisions	27,723,428.04		30,076
		57,261,875.04	**58,944**
8. Subordinated liabilities		**156,200,000.00**	**156,200**
9. Profit-participation certificates		**2,556,459.40**	**6,136**
of which			
due in less than two years € 2,556,459.40			
10. Fund for general banking risks		**30,000,000.00**	**30,000**
11. Capital and reserves			
a) Subscribed capital	988,733,860.00		986,710
aa) Members' capital contributions € 986,733,860.00			(955,961)
ab) Silent participations € 2,000,000.00			(30,749)
b) Revenue reserves	290,500,000.00		290,500
ba) Legal reserves € 286,000,000.00			(286,000)
bb) Other revenue reserves € 4,500,000.00			(4,500)
c) Unappropriated profit	22,303,326.93		25,446
		1,301,537,186.93	**1,302,656**
Total liabilities, capital and reserves		**39,051,196,583.00**	**38,508,993**
1. Contingent liabilities			
Contingent liability on guarantees and indemnities		**49,456.24**	**252**
2. Other commitments			
Irrevocable loan commitments		**3,640,067,638.45**	**3,223,168**

INCOME STATEMENT

1 JANUARY THROUGH 30 JUNE 2017

			1 Jan to 30 June 2017	1 Jan to 30 June 2016
	€	€	€	€ 000
1. Interest income from			**524,912,668.17**	**536,364**
a) Lending and money market operations		491,855,593.55		487,393
b) Fixed-income securities and debt register claims		33,057,074.62		48,971
2. Interest expenses			**400,488,911.34**	**425,202**
3. Current income from			**385,091.65**	**750**
a) Participations and shares in cooperatives		385,091.65		750
4. Commissions received			**3,622,436.65**	**3,848**
5. Commissions paid			**41,904,351.89**	**40,716**
6. Other operating income			**500,393.52**	**411**
7. General administrative expenses			**44,676,837.23**	**43,811**
a) Personnel expenses		22,950,043.93		21,900
aa) Wages and salaries	19,364,089.77			(18,112)
ab) Social security contributions and cost of pensions and other benefits	3,585,954.16			(3,788)
of which				
for pensions € 712,834.54				(1,071)
b) Other administrative expenses		21,726,793.30		21,911
8. Depreciation and write-downs of intangible and tangible assets			**3,000,000.00**	**3,300**
9. Other operating expenses			**2,919,902.38**	**2,858**
10. Write-downs on and adjustments to value to claims and certain securities, as well as additions to provisions for possible loan losses			**3,425,296.20**	**3,862**
11. Income from reversals of write-downs on participating interests, shares in affiliated companies and securities treated as fixed assets			**4,797,456.06**	**5,505**
12. Results from ordinary business activities			**37,802,747.01**	**27,129**
13. Taxes on revenue and income			**15,700,288.37**	**12,515**
14. Net income			**22,102,458.64**	**14,614**
15. Retained earnings brought forward from previous year			**200,868.29**	**171**
16. Unappropriated profit			**22,303,326.93**	**14,785**

NOTES TO THE INTERIM FINANCIAL STATEMENTS AS OF 30 JUNE 2017 (ABRIDGED)

GENERAL INFORMATION ON ACCOUNTING POLICIES

Münchener Hypothekenbank eG's financial accounts for the first half of 2017 were prepared using the same methods used to prepare the balance sheet and determine valuations shown in the annual statement of accounts as of 31 December 2016.

The explanations of the significant amendments of the items in the abridged balance sheet and abridged profit and loss statement were provided in the interim management report.

Tax expenses noted for the period 1 January to 30 June 2017 were calculated based on the weighted average of the annual tax rate on income.

The annual fee due for the European bank levy was accounted for on a pro rata temporis basis for the first half of 2017.

AUDITING ASSOCIATION

DGRV – Deutscher
Genossenschafts- und Raiffeisenverband e. V.,
Berlin, Pariser Platz 3

Munich, 25 July 2017
MÜNCHENER HYPOTHEKENBANK eG
Board of Management

Dr. Louis Hagen   Bernhard Heinlein   Michael Jung

CERTIFICATION FOLLOWING REVIEW

To Münchener Hypothekenbank eG, Munich

We have conducted a review of the abridged half year financial statements – comprising the balance sheet, the income statement, as well as the abridged notes to the financial statements and the interim management report of Münchener Hypothekenbank eG, Munich, for the period 1 January to 30 June 2017, all of which are elements of the half year financial statements pursuant to Art. 37w Securities Trading Act (WpHG). The preparation of the abridged half year financial statements in accordance with German commercial law, and the interim management report pursuant to the applicable terms of the WpHG, are the responsibility of the cooperative's legal representatives. Our responsibility is to issue a certificate for the abridged half year financial statements and the interim management report based on our review.

We have conducted our review of the abridged half year financial statements and interim management report in accordance with the generally accepted German standards for the review of financial statements promulgated by the Institute of Public Auditors in Germany. These standards require that we plan and perform the review so that, by way of a critical assessment, we can exclude with a reasonable measure of certainty that the principal elements of the abridged half year financial statements have not been drawn up in conformity with the German commercial rules, and that the principal elements of the interim management report have not been drawn up in conformity with the WpHG regulations applicable to the interim management report. A review is limited primarily to interviewing the personnel of the cooperative and to analytical assessments and therefore does not achieve the level of certainty provided by an audit cannot be achieved. As we were not assigned to conduct an audit we cannot issue an audit certificate.

Based on the information gained from our review, we are unaware of any circumstances that could lead us to the conclusion that principal elements of the abridged half year financial statements were not drawn up in conformity with the requirements of German commercial law, or that the principal elements of the interim management report were not drawn up in conformity with the applicable terms of the WpHG.

Berlin, 25 July 2017
DGRV – Deutscher Genossenschafts- und Raiffeisenverband e.V.

Dieter Gahlen
Auditor

Thorsten Schraer
Auditor

AFFIRMATION OF THE LEGAL REPRESENTATIVES

To the best of our knowledge and in accordance with applicable reporting principles for interim financial reporting, the interim financial statements give a true and fair view of the assets, liabilities, financial position and earnings situation of the company, and the interim management report of the company includes a fair review of the development and performance of the business and the position of the company, together with a description of the principal opportunities and risks associated with the anticipated development of the company for the remaining business year.

Munich, 25 July 2017
MÜNCHENER HYPOTHEKENBANK eG
Board of Management

Dr. Louis Hagen

Bernhard Heinlein

Michael Jung

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