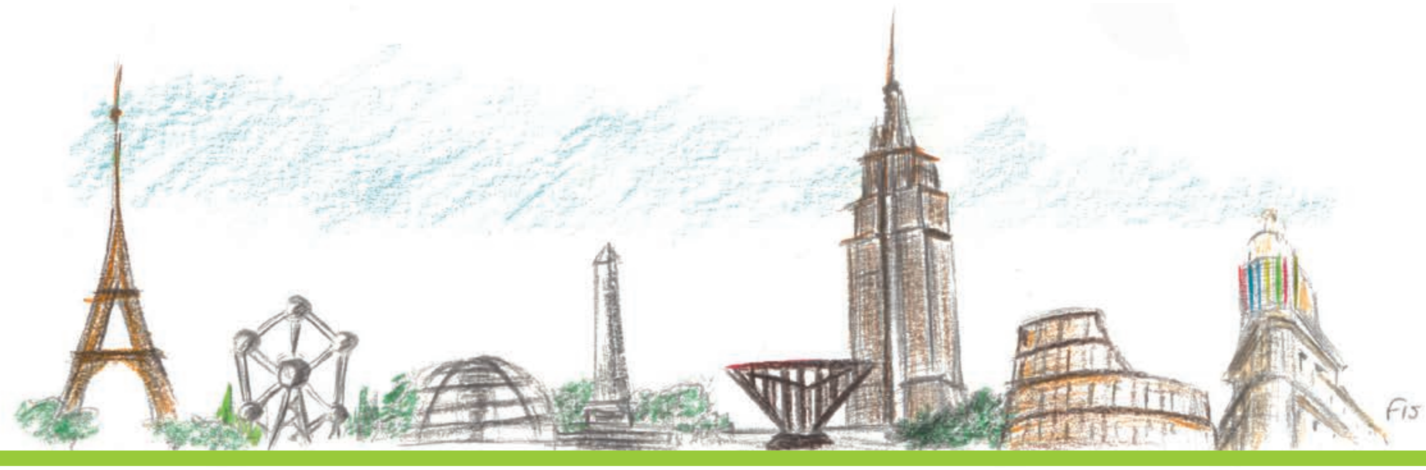

2016

Annual Report

DEXIA KOMMUNALBANK DEUTSCHLAND AG

DEXIA KOMMUNALBANK DEUTSCHLAND DKD

ANNUAL REPORT 2016

OVERVIEW OF DEXIA KOMMUNALBANK DEUTSCHLAND

1 Key balance sheet positions

in EUR million	31.12.2016	31.12.2015
Assets		
Loans to public sector entities	14,510.9	15,730.2
Other loans and advances to banks and non-bank customers	6.004,3	5.926,5
Securities	7,750.2	9,353.0
Equity and liabilities		
Pfandbriefe	17,965.3	19,678.6
Other liabilities to banks and non-bank customers	9,613.1	10,433.0
Equity	663.0	657.7
Balance sheet total	**28,809.8**	**31,395.4**

2 Key profit and loss account positions

in EUR million	31.12.2016	31.12.2015
Net interest and commission income	–69.6	78.2
Administrative expenses (incl. depreciation)	–34.6	–35.6
Risk provisioning incl. result of financial investments	103.9	–142.3
Profit/loss for the year	**–0.2**	**–99.5**

3 Other disclosures

	31.12.2016	31.12.2015
Employees (average number)	81	79
Cost-income ratio as %	–49.7	45.6

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Commercial Register No. HRB 36928, Berlin-Charlottenburg

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REPORT OF THE SUPERVISORY BOARD

The Supervisory Board fulfilled the duties required of it by law, the Bank's articles of association and the Supervisory Board's rules of procedure and advised and monitored the Bank's management on an ongoing basis. It obtained regular, timely and comprehensive information from the Management Board on business policy, basic management issues, the company's position and significant business transactions. In particular, the Management Board reported on business strategy and risk strategy derived from business strategy, key financial indicators and developments in the Bank's relevant markets. The Supervisory Board was also provided with a detailed quarterly explanation of the current liquidity situation and liquidity control measures, in risk reports in accordance with the Minimum Requirements for Risk Management (Mindestanforderungen an das Risikomanagement, MaRisk), and was notified of the risk situation as well as risk controlling and risk management measures. The company's remuneration system was reviewed at regular intervals and the Supervisory Board was informed of related findings. The Supervisory Board satisfied itself that the company's remuneration system is appropriate.

The Supervisory Board was involved in all key decisions and was kept suitably informed in this respect. All important activities were intensively discussed and reviewed accordingly. The Supervisory Board reviewed any transactions requiring its consent, discussed them with the Management Board and passed corresponding resolutions. If a decision needed to be taken between meetings, resolutions were passed by circulating documents.

The Supervisory Board held five meetings in the period under review, with detailed oral and written reporting. In the interim period between these meetings, the Management Board also kept the chairman of the Supervisory Board regularly and continuously informed – both in writing and orally – of any significant developments within the company. The chairman of the Management Board maintained close and regular contact with the chairman of the Supervisory Board in order to discuss any key issues and decisions. The overall Supervisory Board discussed the Bank's business and risk strategy – which is updated annually – in detail at its final meeting of the year.

Due to the changes to Section 25d of the German Banking Act (Kreditwesengesetz, KWG) – which apply in particular to significant institutions – the Supervisory Board reorganised its committees in 2016.

The Remuneration Control Committee was established as an additional committee. The Nomination Committee (previously the Personnel Committee) and the Risk and Credit Committee (previously the Credit Committee) continued to operate under new names, as did the Audit Committee. The tasks of the individual committees – which are intended to assist the overall Supervisory Board in its activities – were based on the stipulations laid down in Section 25d KWG.

In the year under review, the Nomination Committee met once and the Remuneration Control Committee met twice in order to discuss personnel and remuneration issues.

The Risk and Credit Committee met four times and dealt with credit decisions requiring approval or acknowledgement by the Supervisory Board, as well as setting counterparty limits. It also discussed with the Management Board key issues for the Bank relating to specific and general banking risks as well as lending business.

The Audit Committee met four times in 2016. These meetings focused on:

- the audit of the annual financial statements,
- accounting issues,
- the monitoring of accounting processes,
- the assessment of the effectiveness of the internal audit system,
- the review and coordination of the Internal Audit department's audit plan in the year under review and
- the annual reporting provided by the compliance and money laundering officer and by the company's data protection officer.

The committees regularly reported on their activities at the meetings of the Supervisory Board.

Moreover, within the scope of good corporate governance and in compliance with the regulatory requirements relating to its activities the Supervisory Board regularly reviews the efficiency of its activities and those of the Management Board and assesses the information which it receives from the Management Board.

Annual financial statements 2016

Deloitte GmbH, Wirtschaftsprüfungsgesellschaft, has audited the annual financial statements and the management report for the financial year 2016, including the bookkeeping records. This firm was appointed to act as auditors at the General Meeting of Shareholders. In their unqualified audit opinion, the auditors declared that the bookkeeping records and the annual financial statements give a true and fair view of the net assets, financial position and results of operations and that the management report is consistent with the annual financial statements. The Supervisory Board approved the audit findings.

Based on the final outcome of its review of the annual financial statements, the management report and the proposal for the appropriation of earnings, the Supervisory Board concluded that there were no objections to be raised. The Supervisory Board has approved the management report presented by the Management Board and the annual financial statements as of December 31, 2016. The annual financial statements have thus been adopted. The Supervisory Board agrees to the Management Board's proposal of carrying forward the accumulated losses for the past financial year.

The Management Board has submitted to the Supervisory Board its report on relationships with affiliated companies pursuant to Section 312 of the German Stock Corporation Act (Aktiengesetz, AktG). The Supervisory Board unreservedly approved the Management Board's report and the results of this review.

Personnel changes

With effect as of July 1, 2016, Jürgen Jung replaced Dr. Dirk Hoffmann as a member of the Supervisory Board.

In addition, on November 1, 2016 Isabelle Bouvet was elected as a new Supervisory Board member to replace the retiring Supervisory Board chairman Claude Piret.

- Benoît Debroise was appointed the new chairman of the Supervisory Board and
- Véronique Hugues was appointed the deputy chairman of the Supervisory Board.

The Supervisory Board would like to express its thanks and appreciation to all of the Bank's employees and to the Management Board for their work in 2016.

For the Supervisory Board

Paris, March 2017

Benoît Debroise

Supervisory Board chairman

MANAGEMENT REPORT

BASIC INFORMATION

Profile of the Dexia Group

The Dexia Group is a European banking group which has pursued the orderly resolution of its assets since the end of 2011. The Belgian and French governments have owned 94.4% of the Group since the end of 2012, when they made a EUR 5.5 billion capital injection.

The Dexia Group's restructuring plan, which was approved by the European Commission in December 2012, aims to avoid the Group's bankruptcy and liquidation which, given the Group's residual size, might destabilise the entire European banking sector.

As a significant bank within the meaning of the SSM Framework Regulation, the Dexia Group has been under the direct prudential supervision of the European Central Bank within the framework of the Single Supervisory Mechanism (SSM) since November 4, 2014. The Group's parent company, Dexia S. A., is a public limited company (société anonyme) and financial holding company governed by Belgian law whose shares are listed on Euronext Brussels.

As of December 31, 2016, the Dexia Group had 1,134 employees. Dexia Crédit Local is the Dexia Group's main operating entity and benefits from a funding guarantee, up to a maximum amount of EUR 85 billion, provided by the governments of Belgium, France and Luxembourg, to allow for the execution of the restructuring plan. Dexia Crédit Local is domiciled in France, where it holds a banking licence, with branches in Ireland, the USA, Spain and Portugal and subsidiaries in Germany, Italy and Israel. Some of these entities hold local banking licences.

The Dexia Group has discontinued all of its commercial activities and is now solely focused on managing its legacy assets – mainly loans to public sector entities – while protecting the interests of its government owners and guarantors. To meet this objective, the Group has established three main goals:

- Maintain the ability to fund its balance sheet throughout the orderly resolution of its assets;
- Preserve its capital base in order to comply with regulatory requirements;
- Ensure operational continuity by retaining the necessary expertise and resources and developing appropriate information systems.

Notwithstanding the unstable market environment, the Dexia Group was able to optimise its funding structure in 2016.

Despite the high and volatile level of the net position required of the Dexia Group to secure its derivatives counterparties, it was able to reduce its funding volume. This was due to the decrease in the volume of its credit exposures to EUR 146.5 billion as of December 31, 2016 (previous year: EUR 162.8 billion).

The decline in its funding volume to EUR 655 million (previous year: EUR 15.9 billion) enabled the Dexia Group to reduce its dependency on the ECB's funding, which is currently more expensive than funding on the capital market. In consequence, the Group's funding underwent a significant structural adjustment. The Dexia Group currently generates almost all of its funding through issuance of government-guaranteed debt (December 31, 2016: 49%) and by taking out secured funding on the capital market (December 31, 2016: 41%).

In addition, preserving its capital base and complying with regulatory requirements are among the core elements of the orderly rundown of the Dexia Group.

In 2017, the growing scope of the deduction of the AFS reserve from capital in line with the timeframe specified in the EU Capital Requirements Directive IV (CRD IV) and the increasing Dexia-specific regulatory requirements will place significant pressure on the Dexia Group's solvency indicators. The Dexia Group has therefore implemented measures to reduce its capital requirements, so as to increase its capital buffer. These measures, which have been coordinated with its planned asset sales, have resulted in a decrease in the AFS reserve and a considerable reduction in its risk-weighted assets. They also entail the sale of equity investments which are directly deducted from equity capital.

Allowing for these effects, as of December 31, 2016 the Group's CET1 ratio had reached 16.2% (previous year: 15.9%) and its total capital ratio 16.8% (previous year: 16.3%).

Profile of Dexia Kommunalbank Deutschland

Dexia Kommunalbank Deutschland is a wholly-owned subsidiary of Dexia Crédit Local, the main company of the Dexia Group. It thus belongs to a banking group in which the Belgian and French governments hold a 94.4% stake. With its balance sheet total of EUR 28.8 billion as of December 31, 2016, the Bank is the largest subsidiary of Dexia Crédit Local.

Dexia Kommunalbank Deutschland benefits from

- the letter of support provided by Dexia Crédit Local, in which this company undertakes to ensure that the Bank is able at all times to comply with its obligations and to fulfil the requirements of the German banking supervisory system,
- a revolving liquidity facility provided by Dexia Crédit Local with a volume of EUR 500 million, which the Bank has not yet called upon, and
- other technical and organisational support from the Dexia Group.

In accordance with the plan approved by the European Commission in late December 2012 for the restructuring of the Dexia Group, an orderly resolution of the assets of Dexia Kommunalbank Deutschland is envisaged, without any new lending business. In view of the not insignificant share of non-current assets held in the Bank's overall loan book, it is clear that this process will take some time. An accelerated, actively pursued resolution by means of the premature sale of assets is not planned, except where market opportunities are exploited to a limited extent.

Over the next ten years, the assets of Dexia Kommunalbank Deutschland will continuously decrease on account of natural maturities. As of December 31, 2021, its balance sheet total is expected to have declined to EUR 20.8 billion, and its cover pool for Public Pfandbriefe (covered bonds) to EUR 13.6 billion. As of December 31, 2026 these figures will amount to EUR 13.9 billion and EUR 8.8 billion respectively. Since the rate of interest on the capital markets is expected to remain low for the next few years, these projections assume that the creditors' termination rights which are embedded in these receivables will not be exercised.

In view of the changed nature of the commercial focus of the Dexia Group, the business activities of Dexia Kommunalbank Deutschland concentrate on the administration, management and funding of its extensive portfolio of securities and loans, with the following core areas of focus:

- preserving operational stability and avoiding operational risks in an increasingly stringent regulatory environment,
- optimising the funding mix in order to secure advantageous funding costs and to widen the funding base,
- maintaining cost discipline, for personnel expenses as well as other administrative expenses.

ECONOMIC REPORT

OVERALL ECONOMIC AND INDUSTRY ENVIRONMENT

2016, Dexia Kommunalbank Deutschland's 25th year of business, was dominated by two events whose impacts on Europe will, in some cases, be considerable.

In a referendum held on June 23, 2016, a majority of Britons (51.9%) voted for the United Kingdom to leave the European Union (EU). The Brexit vote was the first ever occasion that an EU member state had opted to withdraw from the federation of states established 25 years ago under the Treaty of Maastricht. In early October 2016, the new prime minister, Theresa May, announced that she would submit notification of EU withdrawal under Article 50 of the Treaty of Lisbon by the end of the 1st quarter of 2017. The negotiations over an agreement setting out the future relationship between the United Kingdom and the EU and the details of the UK's withdrawal are thus likely to begin imminently. This agreement will require the approval of the European Parliament and a qualified majority of the EU's member states in order to come into effect.

In January 2017, May spelled out her government's plans for the United Kingdom's post-Brexit future in a twelve-point plan. She proclaimed as her goal a "truly global Britain" outside the European single market and the European Economic Area. The aim is to secure a comprehensive free-trade agreement between the EU and the United Kingdom as a reliable, amicable partner. The British government is particularly keen to gain sovereign control over future immigration and its own legislation, outside the jurisdiction of the European Court of Justice.

With around 13% of its population and 16% of its gross domestic product, the United Kingdom represents a significant share of the EU. Since the precise terms of withdrawal are not yet known, it is difficult at the present time to assess the consequences of Brexit for the EU. It is to be hoped that it proves possible to arrive at a fair solution which is acceptable for both parties and which does not place an unnecessary burden on the manifold relationships between the United Kingdom and the EU.

Almost six months after the Brexit decision, on November 8, 2016 the American people elected Donald Trump as the 45th president of the USA. In his inaugural address in January 2017, he confirmed his government programme which, under the slogan "America first", is primarily intended to bring back lost jobs, protect the country's borders and stimulate the economy through tax cuts and improvements to the US infrastructure. Trump represents a new trade philosophy, which emphasises America's national interest over the free exchange of goods and services. He has repeatedly stated his sceptical attitude towards the EU's values and has declared Brexit a "great thing" and NATO to be "obsolete".

His first official acts upon taking office included signing an order withdrawing the USA from the Trans-Pacific Partnership (TPP), announcing the quick renegotiation of the NAFTA agreement with Mexico and Canada and imposing an immediate immigration ban on the citizens of seven predominantly Muslim countries. The hope that Trump's election rhetoric would give way to a more moderate approach once he took office thus evaporated for the time being.

In view of Trump's openly protectionist statements opposing free trade, fears grew in Europe over the future of the traditionally strong trans-Atlantic trade relationship. In late January 2017, in his letter to 27 heads of state and government on the future of the EU, the president of the European Council, Donald Tusk, criticised the "worrying declarations by the new American administration" as a reflection of Eurosceptic or even anti-European attitudes in an increasingly multipolar world. Tusk described as a further threat to the EU the growing nationalist and xenophobic mood in the community of states, as well as waning confidence in political integration and basic values of liberal democracy. He called for courage, decisiveness and solidarity in countering the enemies of European unity and for an aggressive defence of the EU's interests. This would require a more robust EU foreign policy, including strengthening the EU's external borders and increasing defence spending as well as encouraging growth, investments and social inclusion.

Unimpressed by Brexit and by Trump's election, in the second half of the year under review the Eurozone countries' aggregate real gross domestic product (GDP) growth picked up, with a rate of 0.4% in the 3rd quarter and 0.5% in the 4th quarter. For the year 2016 as a whole, the GDP growth rate increased slightly, to 1.7% (previous year: 1.6%).

Germany, whose export-oriented economy benefited from the euro's low exchange rate, once again registered an above-average performance:

- With GDP growth of 1.9% (previous year: 1.7%), economic growth once more exceeded the Eurozone average.
- In December 2016 employment had improved by 0.5%, with 43.5 million persons in gainful employment (previous year: 43.3 million persons in gainful employment), while unemployment fell to 5.8% (previous year: 6.1%).
- Germany achieved a budget surplus of 0.6% (previous year: 0.7%) of GDP and reduced its gross debt to 68.1% (previous year: 71.2%) of GDP.

Within the Eurozone, the member states' GDP growth rates changed only slightly on the previous year. Of the other key Eurozone countries, France reached a level of 1.3% (previous year: 1.3%), Italy 0.7% (previous year: 0.7%) and Spain 3.2% (previous year: 3.2%). › 4

The credit ratings of European countries were also relatively stable. Only the United Kingdom was subject to a significant downgrade by Standard & Poor's and Fitch (from AAA or AA+ to AA) four days after the Brexit decision, due to an expected slowdown in growth and a less stable political environment. The rating agency Moody's had already downgraded this country from Aaa to Aa1 in 2013. The European club of "pure" AAA countries, whose bonds have been awarded top ratings from all three of these major rating agencies, currently consists of seven members: Denmark,

4 Economic data of selected countries

	Price-adjusted GDP growth*		Budget surplus/deficit*		Gross debt*		CDS spreads (5 years)	
	31.12.2016	31.12.2015	31.12.2016	31.12.2015	31.12.2016	31.12.2015	31.12.2016	31.12.2015
	as %	as %	as % of GDP	as % of GDP	as % of GDP	as % of GDP	in basis points	in basis points
Eurozone countries								
Belgium	1.2	1.5	–3.0	–2.5	107.0	105.8	33.4	32.5
Germany	1.9	1.7	0.6	0.7	68.1	71.2	21.8	12.9
France	1.3	1.3	–3.3	–3.5	96.4	96.2	37.0	26.4
Italy	0.7	0.7	–2.4	–2.6	133.0	132.3	157.2	97.2
Netherlands	1.7	2.0	–0.8	–1.9	63.0	65.1	27.6	15.9
Austria	1.5	1.0	–1.5	–1.0	83.5	85.5	28.1	22.2
Portugal	0.9	1.6	–2.7	–4.4	130.3	129.0	274.0	170.5
Spain	3.2	3.2	–4.6	–5.1	99.5	99.8	75.6	89.9
Other countries								
Japan	0.7	0.5	–5.0	–5.3	250.4	248.0	30.0	46.9
UK	1.9	2.2	–3.5	–4.3	89.2	89.1	31.1	19.1
USA	1.6	2.6	–4.6	–4.4	107.5	105.8	26.7	17.6

* for 2016: forecasts and provisional figures

Sources: German Federal Statistical Office, European Commission

5 Ratings of selected countries

	Standard & Poor's		Moody's		Fitch	
	15.01.2017	15.01.2016	15.01.2017	15.01.2016	15.01.2017	15.01.2016
Eurozone countries						
Belgium	AA	AA	Aa3	Aa3	AA–	AA
Germany	AAA	AAA	Aaa	Aaa	AAA	AAA
France	AA	AA	Aa2	Aa2	AA	AA
Italy	BBB–	BBB–	Baa2	Baa2	BBB+	BBB+
Luxembourg	AAA	AAA	Aaa	Aaa	AAA	AAA
Netherlands	AAA	AAA	Aaa	Aaa	AAA	AAA
Austria	AA+	AA+	Aa1	Aaa	AA+	AA+
Poland	BBB+	BBB+	A2	A2	A–	A–
Portugal	BB+	BB+	Ba1	Ba1	BB+	BB+
Spain	BBB+	BBB+	Baa2	Baa2	BBB+	BBB+
Hungary	BBB–	BB+	Baa3	Ba1	BBB–	BB+
Other countries						
UK	AA	AAA	Aa1	Aa1	AA	AA+
USA	AA+	AA+	Aaa	Aaa	AAA	AAA
Japan	A+	A+	A1	A1	A	A

Source: Bloomberg

Germany, the Netherlands, Luxembourg, Norway, Sweden and Switzerland. › 5

Four downgrades – Finland to Aa1/AA+ (Moody's and Fitch), Austria to Aa1 (Moody's), Belgium to AA– (Fitch) and Poland to BBB+ (Standard & Poor's) – and two upgrades – Ireland to A3/A (Moody's and Fitch) and Hungary to BBB– or Baa3 (Standard & Poor's, Fitch and Moody's) – were further important rating adjustments in the year under review.

Moreover, on January 13, 2017 the Canadian rating agency DBRS cut Italy's rating from A (low) to BBB (high). Italy thus lost the single A rating which it had been awarded by the last of the rating agencies accepted by the ECB. For investors in Italian government bonds, this move means increased haircuts on securities repurchase agreements with the ECB or other business partners, and thus higher funding costs.

In early December 2016, Moody's had already lowered the outlook for its Italy rating (Baa2) from stable to negative. It justified this step on grounds of the expected tentative pace of the fiscal and economic reforms following the resignation of the prime minister, Matteo Renzi, and the risk of a delay in reducing Italy's high level of gross debt (2016: 133% of GDP) in view of the subdued growth outlook. Renzi resigned after a majority of Italian voters on December 4, 2016 rejected a referendum on reform of the senate which he had initiated. Since this time, the government of the new prime minister, Paolo Gentiloni, has been unable to arrive at a consensus on whether to call new elections or to seek to maintain the existing three-party coalition up to the end of the current legislative period in the spring of 2018. In January 2017, it was announced that the European Commission had insisted that the Italian government find savings of EUR 3.4 billion for the budget year 2017 in order to bring down the country's deficit ratio to the required level of 2.2% of GDP. The country's economics and finance minister, Pier Carlo Padoan, promised to do so and announced "corrective measures".

On July 7, 2016, the European Commission provided notice in a press release that the two Iberian countries Spain and Portugal were unlikely to "correct their excessive deficits by the recommended deadline". Indeed, Spain clearly missed its budget deficit goal of 4.2% of GDP for 2015 and 3% for 2016. Its actual figures were 5.1% (2015) and 4.7% (2016). Portugal also missed the target figure of 2.5% for 2015 (actual figure: 4.4%), but with a result of 2.3% it met the revised target in the current year, which remained at 2.5%.

For failure to meet the 2015 deficit goals, fines of up to 0.2% of GDP could have been imposed under the rules of the Stability and Growth Pact, totalling more than EUR 2 billion for Spain and around EUR 200 million for Portugal. However, the European Commission waived these fines, pointing to the two countries' successful consolidation measures over the past few years and their readiness to implement additional deficit-cutting measures.

Overall, the euro area's public finances improved slightly in the year under review. The Eurozone's aggregate budget deficit fell to 1.8% (previous year: 2.1%), while its gross debt volume decreased to 91.6% (previous year: 92.6%). In mid-February 2017, for the year 2017 as a whole the European Commission announced a further decrease in the Eurozone's budget deficit, to 1.4%, and in its gross debt volume to 90.4%.

At the end of the year under review, Eurozone inflation finally picked up some momentum after long months of hovering sluggishly around the 0% mark. The Eurozone's Harmonised Index of Consumer Prices (HICP) leapt from 0.6% (November 2016) to 1.1% (December 2016), even reaching 1.8% one month later and thus roughly matching the ECB's target level of "below, but close to, 2%", a good two years after the launch of its Asset Purchase Programme (APP). The ECB's preferred indicator measuring the medium-term inflation outlook, the 5Y plus 5Y Forward Inflation Swap Rate (five-year inflation-indexed forward swap rate in five years' time) – which had fallen to an all-time low of 1.25% on July 11, 2016 – had climbed to 1.74% by the end of 2016. This burst of inflation was mainly driven by base effects on account of the huge rise in energy prices year-on-year (+8.1%). In a press conference held on January 19, 2017, the ECB's president, Draghi, clarified that he did not yet see the higher level of inflation as sustained and that pressure on the core inflation rate adjusted for energy and food price effects remained "subdued".

As an important measure to combat deflation, at its meeting held on March 10, 2016 the ECB's Governing Council had resolved an extensive set of measures cutting key interest rates and expanding quantitative easing with the following measures:

- The interest rate on main refinancing operations was reduced to 0.00% (previously 0.05%) and the rate on the marginal lending facility to 0.25% (previously 0.30%), while the rate on the deposit facility was lowered to −0.40% (previously −0.30%).
- The volume of monthly asset purchases under the APP was expanded from EUR 60 to 80 billion.
- Investment-grade euro-denominated bonds issued by non-bank corporations established in the euro area were included in the list of assets eligible for purchasing under the APP.
- Launch of a new series of four targeted longer-term refinancing operations (TLTRO II), each of which has a term of four years. Borrowing conditions in these operations can be as low as the interest rate on the deposit facility.

In early December 2016, the ECB's Governing Council decided to extend the term of the APP for a further nine months up to December 31, 2017, and to expand the pool of bonds eligible for purchase by including securities with a remaining term of at least one year (previously at least two years) and securities yielding a return below the ECB's deposit rate. Draghi also announced that the volume of the ECB's monthly asset purchases would be cut from EUR 80 billion to EUR 60 billion from April 2017 onwards. However, he was visibly at pains to emphasise that this step would not in any way entail an end to the policy of quantitative easing (tapering) and that the duration and size of the APP might once again be extended if necessary on account of the inflation trend.

As of the end of 2016, the securities portfolios purchased by the ECB under the APP totalled EUR 1,532.1 billion (previous year: EUR 649.9 billion), comprising the following four sub-programmes:

- PSPP: EUR 1,254.6 billion,
- CBPP3: EUR 203.5 billion,
- CSPP: EUR 51.1 billion,
- ABSPP: EUR 22.8 billion.

In sticking to its expansionary monetary policy, which has been increasingly criticised by politicians and economists, the ECB considered that this had been borne out by the significant rise in lending in the Eurozone. The rate of growth in lending to the corporate sector reached 2.3% over the course of the year, its strongest rise since 2009. The monetary aggregate M1 – which is monitored as an economic indicator – also reached a significant, 8.8% rate of growth.

Ten-year Bund bonds, the benchmark for European government bonds, were providing a yield of 0.21% on December 31, 2016 – still very close to the all-time yield low of −0.19% reached on July 8, 2016 – while two-year German government securities ended the year under review with a yield of −0.77%.

On the other hand, despite huge ECB purchases in the year under review the ten-year yields on government bonds issued by peripheral Eurozone countries were trading in very broad bands of 1.04% to 2.13% (Italy), 0.88% to 1.83% (Spain) and 2.51% to 4.11% (Portugal). At the end of 2016, they had reached 1.82% (Italy), 1.38% (Spain) and 3.76% (Portugal).

Apart from the comparatively weak performance of Portuguese government bonds, the widening of the spread between French government securities (OATs) and German Bund bonds, which began in December 2016, was a notable development. In February, the premium on ten-year OAT yields as compared with that of German securities reached over 75 bp, a level last seen in the crisis year 2012. This was due to concerns over a possible victory for the nationalist opponent of the EU, Marine Le Pen, in the impending French presidential election. With a forecasted share of the vote in excess of 25%, she led opinion polls for the first round of the election which is due to be held on April 23, 2017. However, in the run-off vote which will take place two weeks later she is likely to have only a marginal chance of victory against either of her two likely opponents – the former economics minister Emmanuel Macron or the conservative Francois Fillon.

Unlike in the case of government bonds, interest rates on the euro money market were calmer and continuously headed south. Yields on the 3-month Euribor fell from −0.13% at the start of the year to −0.32% on December 31, 2016, not least due to the ECB's key interestrate cut in March 2016.

The British pound reacted to the decision for the United Kingdom to leave the EU with a steep fall from USD 1.49 to USD 1.23 by the end of the year. The euro also fell continuously, following its annual high of USD 1.15 in February 2016, and at the end of the year at USD 1.05 it had only slightly recovered from the low of USD 1.03 reached shortly after Trump's election.

While on the stock markets the Euro Stoxx 50 index and Germany's DAX index had virtually made up for their Brexit-driven losses in the space of just a few days and registered annual performances of 0.7% (Euro Stoxx 50 index) and 6.9% (DAX) at the end of the year, banking stocks experienced stronger losses and staged a weaker recovery. The Stoxx Europe 600 banking index suffered considerable peak losses of 22.3%, and the markdowns on Italian bank equities – which were particularly badly affected – were even significantly higher at times.

For some time now, Italy's banks have been suffering due to the burden of non-performing loans whose overall volume is estimated at approximately EUR 360 billion, around 16.4% of all Italian bank loans. The bank resolution fund Atlante was established in April 2016 on the Italian government's initiative in order to support banks in difficulty. However, its resources and those of the follow-up fund Atlante 2 soon proved insufficient to resolve the problems. Banca Monte dei Paschi di Siena (MPS), the country's third-largest credit institution, is at the heart of the Italian banking crisis. In December 2016, the ECB estimated its capital requirements to amount to EUR 8.8 billion. Shortly thereafter, the European Commission authorised the Italian government to provide temporary liquidity assistance for the institution and also permitted Italy to provide banks with liquidity for a further six months if necessary, subject to compliance with the EU's provisions on state aid. It seems certain that the government will acquire a majority of the interests in MPS and underwrite most of the required capital increase.

Brexit and the Italian banking crisis had an impact on the risk premiums for bank refinancing. The average premium on five-year credit default swaps calculated by the iTraxx Senior Financials Europe Index for 25 European financial institutions on senior unsecured liabilities peaked at 135 bp in June 2016, before falling back to 94 bp by December 31, 2016.

At just short of EUR 126 billion (previous year: EUR 145 billion), the volume of new issues of covered bonds placed in the year under review with a euro benchmark format (issue volume of EUR 500 million or more including increases) was significantly lower than in the previous year. In the country ranking, Germany led the way with a 19% share of issues, ahead of France (17%) and Spain (11%).

Due to continuing demand from the ECB within the scope of its CBPP3 programme, the spread on German Public Pfandbriefe over the swap curve remained almost unchanged. According to the iBoxx Public Pfandbriefe index, at the end of 2016 the average asset swap spread was pricing at −8.0 bp (December 31, 2015: −7.3 bp).

As of December 31, 2016, sales of Public Pfandbriefe had increased by 41.3% year-on-year to EUR 15.6 billion, while the volume outstanding fell from EUR 180.5 billion (December 31, 2015) to EUR 155.2 billion (−14.0%).

BUSINESS PERFORMANCE

In accordance with the plan approved by the European Commission in late December 2012 for the orderly restructuring of the Dexia Group, Dexia Kommunalbank Deutschland did not pursue any new lending business in the year under review. Only in a few cases where the Bank was contractually obliged to submit a renewal offer were existing loans extended with a total volume of EUR 15.4 million (previous year: EUR 68.2 million). All of these loans are guaranteed by German regional or local authorities and are therefore eligible as cover for Public Pfandbriefe.

As of June 30, 2016, the Bank held certificates of deposits of Dexia Crédit Local with a volume of EUR 300 million, which are guaranteed by the governments of Belgium (51.4%), France (45.6%) and Luxembourg (3.0%). This portfolio was completely eliminated through sales in the second half of the year under review.

Moreover, in the 4th quarter of the year under review the Bank sold the Kärntner Ausgleichszahlungs-Fonds zero-coupon bonds which it had received within the scope of Tender Offer II for federal state-backed Heta debt securities for a nominal amount of EUR 399.8 million (see Business performance section – Claims against Heta Asset Resolution AG).

The Bank also disposed of securities with a nominal value of EUR 608.4 million (previous year: EUR 2,073.0 million) in the reporting period, including Japanese government bonds for a nominal amount equivalent to EUR 428.2 million.

To fund its lending operations, issues with a total volume of EUR 1,564.3 million (previous year: EUR 1,555.7 million) were launched within the framework of new issue business. Of this figure

- EUR 503.0 million related to Public Pfandbriefe and
- EUR 1,061.3 million to loans taken out.

A Pfandbrief issue with a volume of EUR 500 million and a period to maturity of 5.25 years was launched on June 8, 2016, as the largest individual transaction in these issuing operations. This bond was priced at a re-offer spread of +6 bp over the swap curve. 87% of the investors were from Germany, and the remainder from Scandinavia (7%), the United Kingdom and Ireland (3%) and other countries (3%).

The Bank did not issue any unsecured bearer notes in the reporting period. › 6

6 Development of new issue business (bearer and registered instruments)

in EUR million	2016	2015
Public Pfandbriefe	503.0	528.0
Loans taken out	1,061.3	1,027.7
Total	**1,564.3**	**1,555.7**

The Bank uses derivative transactions to hedge interest rate risks and currency risks. In the year under review, new derivative transactions were entered into with a nominal volume of EUR 1,381.4 million (previous year: EUR 1,252.9 million).

Table › 7 shows the volume of interest-rate and cross-currency interest-rate swaps and options as of December 31, 2016.

7 Derivative transactions

Nominal value in EUR million	31.12.2016	31.12.2015
Interest-rate swaps and cross-currency interest-rate swaps	51,348.4	56,291.1
Options	0.0	30.0
Total	**51,348.4**	**56,321.1**

At 178.2% (previous year: 179.4%), the ratio of the volume of derivatives to the balance sheet total was at the same level as in the previous year.

As of the balance sheet date, the credit equivalent amounts of the interest-rate and cross-currency interest-rate swaps determined according to the mark-to-market method pursuant to Article 274 of the Capital Requirements Regulation (CRR) amounted to EUR 1,547.0 million (previous year: EUR 1,532.9 million). On balance, collateral for derivatives exposures totalled EUR 3.8 billion (previous year: EUR 3.6 billion).

Claims against Heta Asset Resolution AG

At the start of 2016, the portfolio of Dexia Kommunalbank Deutschland included claims with a volume of EUR 395 million against Austria's Heta Asset Resolution AG (Heta), the successor company of Hypo Alpe Adria Bank International AG (HAA). These claims were secured by a deficiency guarantee issued by the Austrian federal state of Carinthia and Kärntner Landesholding.

On January 21, 2016, Kärntner Ausgleichszahlungs-Fonds (KAF) published a "Tender Offer I" pursuant to Section 2a of the Austrian Financial Market Stabilisation Act (Finanzmarktstabilisierungsgesetz, FinStaG) for the creditors of Heta claims which were secured through the statutory liability of the Austrian federal state of Carinthia and Kärntner Landesholding.

In early March 2016, this offer was extended and non-junior Heta creditors wishing to accept the tender offer with a term expiring on March 11, 2016 were offered the opportunity to subscribe for a zero-coupon bearer bond issued by the Republic of Austria with an 18-year period to maturity in return for payment of their 75% proceeds. In a joint press release, a large group of Heta creditors (including Dexia Kommunalbank Deutschland) announced that it would not accept the tender offer, which it considered inadequate.

On March 14, 2016, Kärntner Ausgleichszahlungs-Fonds announced that the necessary quorum for acceptance of at least two thirds of the creditors granting their approval had not been reached, and that the tender offer had therefore failed.

On May 18, 2016, the Republic of Austria and 72 Heta creditors (including Dexia Kommunalbank Deutschland) holding federal state-backed Heta debt securities with a volume of approximately EUR 4.9 billion signed a memorandum of understanding in order to resolve the Heta dispute.

The subject matter of this memorandum of understanding was a public tender offer for federal state-backed Heta debt securities (Tender Offer II) to be resubmitted by Kärntner Ausgleichszahlungs-Fonds, but on significantly better terms than in Tender Offer I which had failed in March 2016. Section 2a FinStaG once again served as the statutory basis for Tender Offer II.

Over the next few months, the statutory, contractual and technical preconditions for Tender Offer II were fulfilled, and on September 6, 2016 Kärntner Ausgleichszahlungs-Fonds published its new offer. This offer was submitted to non-junior Heta creditors with claims totalling EUR 10.0 billion and junior Heta creditors with claims in the amount of EUR 0.9 billion. In order to become legally valid, this required the consent of at least two thirds of all creditors and of 25% of the non-junior creditor group and 25% of the junior creditor group. The deadline for acceptance expired on October 7, 2016.

For non-junior Heta creditors, such as Dexia Kommunalbank Deutschland, Tender Offer II comprised the offer of a cash payment of 75% of the nominal value of their Heta claims plus interest for the period up to March 1, 2015. The cash payment received was exchangeable at a ratio of 1:1 for zero-coupon bonds issued by Kärntner Ausgleichszahlungs-Fonds and guaranteed by the Republic of Austria, with a term of 15.3 years and a market value of 90% of their nominal value.

Moreover, a six-month "stabilisation period" was envisaged beginning on December 1, 2016, during which time Kärntner Ausgleichszahlungs-Fonds undertakes to repurchase the zero-coupon bonds at a prescribed yield markup over the swap curve. This was intended to ensure that the holders of zero-coupon bonds were actually able to realise the value of the offer, 90% less hedge costs.

On October 10, 2016, Kärntner Ausgleichszahlungs-Fonds announced that Tender Offer II had been accepted by an overwhelming majority of the Heta creditors. The total approval rate was 98.71%. 99.55% of non-junior creditors (including Dexia Kommunalbank Deutschland) participated and 89.42% of junior creditors.

By participating in Tender Offer II, Dexia Kommunalbank Deutschland was able to reduce its existing risk provisioning on Heta claims by EUR 139.6 million. The same amount of extraordinary income thus accrued to the Bank.

The Bank disposed of the Kärntner Ausgleichszahlungs-Fonds zero-coupon bond which it had received, with a nominal amount of EUR 399.8 million, in the 4th quarter of the year under review.

POSITION

RESULTS OF OPERATIONS

Net interest income and net commission income

Net interest income for 2016 amounted to EUR – 67.4 million (previous year: EUR 80.8 million), and was thus EUR 148.2 million lower than in the previous year.

This significant decrease was mainly attributable to the negative earnings contributions in the amount of EUR – 106.4 million (previous year: EUR + 29.6 million) which resulted from the early termination of derivative transactions and were included in net interest income. Dexia Kommunalbank Deutschland had announced its termination of this volume of derivatives transactions in its ad hoc announcement of May 18, 2016 and in its 2016 semi annual report (see Business performance section – Summary of business performance).

Excluding the negative earnings contributions from the early termination of derivative transactions, net interest income amounted to EUR 38.2 million. Net interest income includes the commitment commission reduced to EUR 1.1 million (previous year: EUR 3.1 million) for the liquidity facility provided by Dexia Crédit Local. This was due to a decrease in the volume of the liquidity facility in October 2016, from EUR 1 billion to EUR 500 million, as well as improved terms.

Moreover, use of securities repurchase agreements on the interbank market and via the Eurex Repo trading platform once again helped to reduce funding costs. Funding of securities was thus possible on significantly more favourable terms than via open market operations with Deutsche Bundesbank.

As in the previous year, no trading-book business was entered into in the year under review.

The Bank has reported a negative profit for the financial year 2016. Accordingly, in line with its terms of issue, servicing of the profit participation rights capital was not possible for the financial year 2016. As in the previous year, net interest income therefore does not include expenses for servicing of the Bank's profit participation rights capital.

Net commission income in the amount of EUR – 2.2 million (previous year: EUR – 2.6 million) mainly comprises expenses for pro rata management fees for guaranteed loans, custody charges paid and commission for brokerage of customer deposits.

Overall, net interest and commission income totalled EUR – 69.6 million (previous year: EUR 78.2 million). › 8

Administrative expenses

The Bank's number of employees had increased to 81 by the end of 2016 (previous year: 78 employees), while personnel expenses rose by 2.9% to EUR 7.0 million.

On July 12, 2016, the parties to the wage agreement for the private and public banking sector concluded a new wage agreement with a term of 33 months (expiring on January 31, 2019). Salaries covered by the wage agreement are to rise by 3.7% in three steps from October 2016. This is proportionately reflected in the increase in personnel costs for 2016.

Non-compensation expenses with a volume of EUR 27.1 million (previous year: EUR 28.3 million) decreased by 4.2% on the previous year.

The decline is mainly due to the contribution made to the restructuring fund (bank levy) of the German Financial Market Stabilisation Agency (Bundesanstalt für Finanzmarktstabilisierung, FMSA). This increased to EUR 16.4 million (previous year: EUR 15.8 million), but the Bank made use of the opportunity to cover 15% (EUR 2.5 million) of the payment amount by submitting an irrevocable payment commitment to the FMSA and to capitalise this as an other asset. Only the remaining EUR 13.9 million was thus registered as non-compensation expenses.

Allowing for the impairment of fixed assets (depreciation) of EUR 0.5 million (previous year: EUR 0.5 million), overall administrative expenses decreased to EUR 34.6 million (previous year: EUR 35.6 million).

Due to the high negative net interest income, the ratio of administrative expenses to net interest income (cost-income ratio) deteriorated to – 49.7% (previous year: 45.6%).

8 Development of key profit and loss account positions

	2016 in EUR million	2015 in EUR million	Change as %
Interest income	2,156.8	2,310.3	–6.6
Interest expense	–2,224.2	–2,229.5	–0.2
Net interest income	–67.4	80.8	> –100.0
Net commission income	–2.2	–2.6	–18.6
Net interest and commission income	**–69.6**	**78.2**	**> –100.0**
Personnel expenses	–7.0	–6.8	2.4
Other administrative expenses (non-compensation expenses)	–27.1	–28.3	–4.2
Depreciation, amortisation and valuation adjustments on intangible assets and property, plant and equipment	–0.5	–0.5	0.3
Administrative expenses	–34.6	–35.6	–2.9
Partial operating result	**–104.2**	**42.6**	**> –100.0**
Other operating income and expenses	0.1	0.3	–63.0
Risk provisioning	32.8	–50.8	> –100.0
Result of financial investments	71.1	–91.5	> –100.0
Operating result	**–0.2**	**–99.5**	**–99.8**
Tax expense	0.0	0.0	0.0
Profit/loss for the year	**–0.2**	**–99.5**	**–99.8**

Risk provisioning

Risk provisioning in the past financial year was shaped by the release of a specific valuation allowance in the amount of EUR 68.4 million for the loan claims guaranteed by the Austrian federal state of Carinthia against Heta Asset Resolution AG (see Business performance section – Claims against Heta Asset Resolution AG).

The one-off income from the receipt of an already written-off repayment claim of EUR 9.4 million on the participation certificate of a German credit institution which the Bank had purchased in 2002 was a further positive factor.

Risk provisioning was adversely affected by losses in the amount of EUR 3.9 million from the sale of securities. In addition, a contingency reserve in accordance with Section 340f of the German Commercial Code (Handelsgesetzbuch, HGB) was added with a further volume of EUR 27.6 million.

In overall terms, net risk provisioning amounted to EUR 32.8 million (previous year: EUR –50.8 million).

No excess liability resulted from the loss-free valuation of the banking book.

Result of financial investments

The result of financial investments in the amount of EUR 71.1 million (previous year: EUR –91.5 million) includes write-ups of EUR 71.2 million on the debt securities of Heta Asset Resolution AG guaranteed by the Austrian federal state of Carinthia (see Business performance section – Claims against Heta Asset Resolution AG).

Operating result before tax

The operating result before tax amounted to EUR –0.2 million (previous year: EUR –99.5 million).

Taxes

Deferred tax assets resulting from temporary differences between the commercial and tax balance sheets were not recognised since it is not possible to predict the time of settlement of these differences with a sufficient degree of probability.

Net loss for the year

The net loss for the year amounts to EUR –0.2 million (previous year: EUR –99.5 million). This was thus significantly better than the forecast range of EUR –15 million to EUR –25 million that was published in the Bank's 2015 Annual Report.

Accumulated losses

Allowing for drawings on the profit participation rights capital, accumulated losses decreased by EUR 5.2 million to EUR –168.9 million (previous year: EUR –174.1 million).

FINANCIAL AND LIQUIDITY POSITION

In the year under review, the registered Public Pfandbriefe item decreased by EUR 1.4 billion to EUR 13.5 billion (previous year: EUR 14.9 billion). This decline reflected scheduled maturities and debtors' exercise of termination rights.

The bearer Pfandbriefe item decreased by EUR 0.3 billion to EUR 4.5 billion (previous year: EUR 4.8 billion).

The overall Pfandbriefe item thus reached EUR 18.0 billion (previous year: EUR 19.7 billion), which represented 62.4% (previous year: 62.7%) of the balance sheet total.

At EUR 4.3 billion, other liabilities to banks remained at the previous year's level (previous year: EUR 4.3 billion). › 9

Securities repurchase agreements declined to EUR 0.9 billion (previous year: EUR 1.2 billion), of which EUR 0.5 billion related to business with Dexia Crédit Local and its Dublin branch.

The Bank's use of open-market loans provided by Deutsche Bundesbank continued to decline. As of December 31, 2016, the Bank had taken out open-market loans with a volume of only EUR 0.1 billion (previous year: EUR 1.6 billion). On this date, Dexia Kommunalbank Deutschland's available credit line with Deutsche Bundesbank on the basis of pledged securities amounted to EUR 1,532 million. The Bank also held further unencumbered securities eligible for central bank borrowings with a loan value of EUR 1.0 billion.

As of the end of the reporting year, the Bank's portfolio of secured refinancing funds in the form of Public Pfandbriefe and other secured borrowings totalled EUR 19.0 billion, which amounted to 66.0% (previous year: 70.1%) of the balance sheet total.

As of December 31, 2016, the Bank held unsecured liabilities to its parent company, Dexia Crédit Local, in the amount of EUR 1.7 billion (previous year: EUR 0.0 billion).

Other liabilities to non-bank customers decreased to EUR 5.3 billion (previous year: EUR 6.1 billion). This mainly comprised non-banks' demand and fixed-term deposits, which have decreased to EUR 4.9 billion (previous year: EUR 5.7 billion). Customers have a broad range of deposit products in line with market conditions in this business segment.

Please see the Notes for details of the maturity breakdown of the liabilities to banks and non-bank customers outstanding as of December 31, 2016.

Please refer to Table › 10 for details of the development of the Bank's overall funding structure.

Overall, the liquidity situation of Dexia Kommunalbank Deutschland remained adequate due to its high volume of claims which have solid credit ratings and are eligible for cover and for central bank borrowings, together with its active deposit business.

The Bank remains integrated within the Dexia Group's central liquidity management system. The revolving liquidity facility granted by Dexia Crédit Local was extended for a

9 Development of key balance sheet equity and liabilities

	31.12.2016 in EUR million	31.12.2015 in EUR million	Veränderung as %
Registered Pfandbriefe	381.8	526.7	−27.5
Other liabilities	4,301.9	4,329.0	−0.6
Liabilities to banks	**4,683.7**	**4,855.7**	**−3.5**
Registered Pfandbriefe	13,085.1	14,354.7	−8.8
Other liabilities	5,311.2	6,104.0	−13.0
Liabilities to non-bank customers	**18,396.3**	**20,458.7**	**−10.1**
Public Pfandbriefe	4,498.4	4,797.1	−6.2
Other debt securities	30.5	30.5	0.0
Securitised liabilities	**4,528.9**	**4,827.6**	**−6.2**
Subordinated liabilities	**20.0**	**60.0**	**−66.7**
Profit participation rights capital	**43.9**	**49.3**	**−11.0**
Subscribed capital	432.5	432.5	0.0
Reserves	399.4	399.4	0.0
Accumulated losses	−168.9	−174.1	−3.0
Equity	**663.0**	**657.7**	**0.8**
Other liabilities	**474.1**	**486.2**	**−2.5**
Balance sheet total	**28,809.8**	**31,395.4**	**−8.2**

10 **Development of funding structure**

	31.12.2016 in EUR million	31.12.2016 as %	31.12.2015 in EUR million	31.12.2015 as %
Public Pfandbriefe	17,596.3	64.1	19,270.0	64.5
Funding transactions with Deutsche Bundesbank	130.0	0.5	1,600.0	5.3
Securities repurchase agreements with banks	493.2	1.8	592.3	2.0
Securities repurchase agreements (Eurex Repo)	425.0	1.5	570.0	1.9
Liabilities to banks	2,741.4	10.0	1,012.5	3.4
of which to Dexia Group (repo transactions & other liabilities)	2,155.2	7.9	432.7	1.4
Liabilities to non-bank customers	4,938.4	18.0	5,729.1	19.1
Other (including own funds)	1,115.9	4.1	1,147.9	3.8
Total	**27,440.2**	**100.0**	**29,921.8**	**100.0**

further year in October 2016, with its volume reduced from EUR 1 billion to EUR 500 million. As in previous years, the Bank did not draw upon this facility in the year under review.

In this respect, it should be noted that the letter of support issued by Dexia Crédit Local on February 28, 2011 includes a legally binding commitment to make up any liquidity shortfalls of Dexia Kommunalbank Deutschland.

The liquidity coverage ratio (LCR) is calculated pursuant to the CRR in conjunction with the Delegated Regulation on the LCR. This indicator represents the ratio of available qualifying liquid assets to the net liquidity outflows determined according to prescribed rules in the one-month period following the reporting date. The minimum ratio in the year under review was 0.7; the liquidity coverage ratio of Dexia Kommunalbank Deutschland fluctuated between 0.99 and 1.46.

The Bank's liquidity ratio under German regulatory requirements continues to be determined in accordance with the German Liquidity Regulation (Liquiditätsverordnung, LiqV). The ratio of the funds available in the first maturity band (due daily or within a period of up to one month) and the payment commitments which may fall due within this period may not fall below a figure of 1.

In the reporting period, the liquidity ratio according to Section 2 LiqV fluctuated between 1.08 (minimum) and 1.46 (maximum) and averaged 1.30. › 11

11 **Liquidity position**

	Minimum	Maximum	Average
Liquidity ratio	1.08	1.46	1.30

In addition, the Bank calculates the non-risk-dependent leverage ratio (LR) pursuant to the CRR in conjunction with the Delegated Regulation on the LR. In simple terms, this indicator represents the ratio of an institution's regulatory capital to its volume of business. As of December 31, 2016, it amounted to 2.7%.

No binding minimum limit is currently applicable for the leverage ratio. As things currently stand, a minimum limit of 3% will come into effect from 2019 at the earliest. The Bank expects to comply with this minimum limit at the time of its introduction.

Volume of Pfandbriefe outstanding and Pfandbriefe cover

The total volume of Public Pfandbriefe outstanding had decreased to EUR 17.6 billion as of December 31, 2016 (previous year: EUR 19.3 billion). At the same time, the volume of cover pool assets used for cover declined to EUR 19.1 billion (previous year: EUR 21.0 billion).

Dexia Kommunalbank Deutschland has long maintained a nominal overcollateralisation ratio (ratio of the cover pool's nominal value to the nominal value of the Pfandbriefe outstanding) of at least 8.15%, without being statutorily or contractually obliged to do so. At the end of 2016, its nominal overcollateralisation ratio amounted to 8.40% (previous year: 8.59%) and its present-value overcollateralisation ratio (ratio of the cover pool's present value to the present value of the volume of Pfandbriefe outstanding) was 17.30% (previous year: 16.46%).

Dexia Kommunalbank Deutschland complies with the recommendation of the Association of German Pfandbrief Banks (Verband deutscher Pfandbriefbanken, vdp) to apply the rules prescribed by the vdp credit differentiation model. With the vdp credit differentiation model, the vdp has developed a method which limits the inclusion of non-investment grade government debt in the cover calculation by means of rating-dependent markdowns. Allowing for these markdowns, as of December 31, 2016 the nominal overcollateralisation ratio decreased slightly to 8.14% (previous year: 8.14%) and the present-value overcollateralisation ratio to 17.03% (previous year: 16.01%).

The structure of the cover pool thus changed only slightly. The proportion of exposures to central governments decreased to 12.1% (previous year: 13.1%), while the proportion of exposures to regional authorities rose to 58.8% (previous year: 57.1%) and the proportion of exposures to local authorities remained almost unchanged at 26.0% (previous year: 26.4%). Exposures to other debtors accounted for 3.1% (previous year: 3.4%) of the cover pool. Cover claims from Germany amounted to 67.9% (previous year: 65.3%) of the total cover pool and were thus slightly higher than in the previous year. Claims from Italy (12.8%), Belgium (6.3%) and Austria (5.5%) followed.

Please see the Notes for details of the maturity breakdown of the Pfandbriefe outstanding as of December 31, 2016.

The rating agency Standard & Poor's continues to assign the Public Pfandbriefe held by Dexia Kommunalbank Deutschland AG an A rating (outlook stable).

In the first half of 2016, Dexia Kommunalbank Deutschland commissioned the rating agency Scope Ratings with the very first rating of its Public Pfandbriefe. On May 4, 2016, the rating agency announced the rating of the Public Pfandbriefe issued by Dexia Kommunalbank Deutschland at AA– (outlook stable). According to Scope Ratings, the main bases of this valuation are the solid credit quality of the cover assets, which is expressed in the low default rates as well as the available nominal overcollateralisation.

In determining the set-up of its cover pool for Public Pfandbriefe, Dexia Kommunalbank Deutschland traditionally maintains a steady-handed approach emphasising continuity. For many years now, its nominal overcollateralisation ratio has exceeded the target figure of 8.15% of its Pfandbriefe outstanding, with only slight changes in its debtor structure.

NET ASSETS POSITION

The balance sheet total of Dexia Kommunalbank Deutschland decreased by EUR 2.6 billion (or –8.2%) by comparison with the end of the previous year to EUR 28.8 billion (previous year: EUR 31.4 billion).

In the loans and advances to banks item, loans to public sector entities fell slightly, on account of maturities, to EUR 0.4 billion. Other loans and advances to banks increased, mainly due to a rise in cash collateral to secure derivative exposures and securities repurchase agreements. › 12

Largely scheduled maturities resulted in a EUR 1.1 billion decline in loans and advances to non-bank customers to EUR 14.4 billion (previous year: EUR 15.5 billion).

Please see the Notes for details of the maturity breakdown of the loans and advances to banks and non-bank customers outstanding as of December 31, 2016.

The Bank's portfolio of bonds and debt securities declined – mainly due to scheduled maturities – by EUR 1.6 billion to EUR 7.8 billion (previous year: EUR 9.4 billion).

Bonds and debt securities amounted to 26.9% (previous year: 29.8%) of the balance sheet total, while loans represented 51.1% (previous year: 51.0%).

Total domestic and foreign exposures to public-sector debtors (public sector lending) decreased by EUR 2.2 billion to EUR 20.5 billion (previous year: EUR 22.7 billion). This corresponded to a 71.0% (previous year: 72.4%) share of the balance sheet total.

12 Development of key balance sheet assets

	31.12.2016 in EUR million	31.12.2015 in EUR million	Veränderung as %
Loans to public sector entities	352.0	533.1	–34.0
Other loans and advances	5,824.4	5,694.5	2.3
Loans and advances to banks	**6,176.4**	**6,227.6**	**–0.8**
Mortgage loans	37.5	40.6	–7.6
Loans to public sector entities	14,159.0	15,197.1	–6.8
Other loans and advances	187.7	232.1	–19.1
Loans and advances to non-bank customers	**14,384.2**	**15,469.7**	**–7.0**
From public sector issuers	5,942.7	7,000.8	–15.1
From other issuers	1,802.0	2,340.7	–23.0
Own debt securities	5.5	11.6	–52.9
Bonds and debt securities	**7,750.2**	**9,353.0**	**–17.1**
Other assets	**499.1**	**345.0**	**44.7**
Balance sheet total	**28,809.8**	**31,395.4**	**–8.2**

Own funds

The net loss reported for the financial year 2015 amounted to EUR – 99.5 million. Within the scope of offsetting of losses, the profit participation rights capital was called upon with a volume of EUR 9.4 million in accordance with the applicable contractual terms. The accumulated losses for 2015 thus decreased to EUR – 174.1 million. This figure was approved on March 24, 2016 and carried forward to new account.

The following Table › 13 shows the development of own funds, as notified by the Bank to the banking supervisory authorities on December 31, 2016, within the framework of the common reporting (CoRep). Since the annual financial statements had not yet been adopted as of this date, these figures have been calculated according to a Tier 1 capital amount which was determined in view of an intra-year loss of EUR – 3.9 million.

On this basis, as of December 31, 2016 the Bank had a significantly increased Common Equity Tier 1 (CET1) capital of EUR 653.5 million (previous year: EUR 588.8 million).

In the 4th quarter of 2015 the ECB notified the Bank that, within the framework of the Supervisory Review and Evaluation Process (SREP), it is obliged in future to comply with a Common Equity Tier 1 capital ratio (CET1 ratio) of at least 8%, plus the required capital conservation buffer (jointly 8.625% as of December 31, 2016).

The CET1 ratio notified according to the CRR reached 22.2% (previous year: 17.3%), while the total capital ratio rose to 23.2% (previous year: 18.7%). Both of these capital ratios continue to significantly exceed the statutory requirements as well as the ECB's supplementary SREP requirements.

On December 31, 2016, the capital yield of Dexia Kommunalbank Deutschland amounted to – 0.01% (previous year: – 0.3%).

The overall net loss reported for the financial year 2016 amounts to EUR – 0.2 million. Following the approval of the annual financial statements by the Management Board and the Supervisory Board, within the scope of offsetting of losses the profit participation rights capital will be called upon with a volume of EUR 5.4 million in accordance with the applicable contractual provisions. Accumulated losses will thus decrease from EUR – 174.1 million to EUR – 168.9 million as of December 31, 2016.

If these effects are taken into consideration, on December 31, 2016 Common Equity Tier 1 capital (CET1) amounts to EUR 662.7 million (previous year: 657.5 million). The Bank does not have any Additional Tier 1 capital. Tier 2 capital decreases to EUR 27.4 million (previous year: EUR 46.3 million). Due to the eligibility rules, the profit participation rights capital recognised by the regulatory authorities declines to EUR 4.9 million and subordinated loans decrease to EUR 6.0 million. Regulatory acknowledged general credit risk adjustments in accordance with Section 340f HGB and an internal rating based excess over expected losses are further elements of the Tier 2 capital and jointly amount to EUR 16.5 million.

The Bank's CET1 ratio calculated according to the CRR is 22.5% (previous year: 19.3%), and its total capital ratio 23.5% (previous year: 20.6%).

SUMMARY OF BUSINESS PERFORMANCE

In summary, the following comments are in order regarding the net assets, financial position and results of operations of Dexia Kommunalbank Deutschland:

- As planned, the balance sheet total decreased by 8.3% to EUR 28.8 billion (previous year: EUR 31.4 billion).
- New lending business was only entered into in the form of a marginal volume of loan extensions (EUR 15.4 million).

13 Development of own funds

in EUR million	31.12.2016	31.12.2015
Subscribed capital	432.5	432.5
Reserves	399.4	399.4
Accumulated balance sheet loss	– 174.1	– 84.1
Intra-year loss	– 3.9	– 158.8
Intangible assets	– 0.4	– 0.2
Tier 1 capital	**653.5**	**588.8**
Profit participation rights capital	4.9	17.2
Subordinated liabilities	6.0	14.6
Regulatory acknowledged general credit risk adjustments acc. Section 340f HGB	5.0	6.1
IRB excess of provisions over expected losses	11.5	10.3
Tier 2 capital	**27.4**	**48.2**
Total	**680.9**	**637.0**

- The profit and loss account ended the year with a net loss of EUR – 0.2 million (previous year: EUR – 99.5 million).
- Tier 1 capital shown in the balance sheet increased to EUR 662.7 million. The Tier 1 capital ratio amounted to 22.5% (previous year: 19.3%).
- Dexia Kommunalbank Deutschland maintained an adequate liquidity position, with active deposit business.
- As of December 31, 2016, the Bank's number of employees had increased to 81 (previous year: 78).

In the year under review, the results of operations of the Bank were shaped by extraordinary income with a volume of EUR 139.6 million due to the acceptance of Tender Offer II for the federal state-backed Heta debt securities (see Business performance section – Claims against Heta Asset Resolution AG). This extraordinary income fell within the predicted range of EUR 130 million to EUR 140 million.

In its ad hoc announcement of May 18, 2016 and its 2016 semi annual report, the Bank had announced that – subject to completion of the Heta exchange transaction with the envisaged outcome – it intends to cancel pending financial transactions and possibly implement further measures which will jointly result in earnings of between EUR – 15 million and EUR – 25 million.

In actual fact, in the financial year 2016 Dexia Kommunalbank Deutschland realised negative earnings contributions in the amount of EUR – 106.4 million from the early termination of derivatives transactions. Moreover, a contingency reserve in accordance with Section 340f HGB was established with a volume of EUR 27.6 million. These measures together resulted in a negative impact on earnings with a volume of EUR 134.0 million.

The Management Board considered itself obliged to strengthen the Bank's present-value capital base in the interests of ongoing compliance with the standards required under banking supervision law as well as accounting standards.

The result for the year thus represented a significant improvement on the forecast result.

In summary, in the period under review,
- the Bank strengthened its net assets position and
- its results of operations were balanced,
- while its financial position was stable.

The Management Board would like to express its thanks and appreciation to all of the Bank's employees for their considerable dedication. We would also like to thank the works council and the representative body for senior executives for our constructive working relationships.

OTHER DISCLOSURES

RELATIONSHIPS WITH AFFILIATED COMPANIES

The Management Board's report on relationships with affiliated companies pursuant to Section 312 AktG ends with the following declaration:

"Our Company received suitable consideration for each of the legal transactions indicated in the report on relationships with affiliated companies and was not disadvantaged on account of the measures listed in this report which were either taken or not taken. This assessment is based on the circumstances known to us at the time of the notifiable transactions."

EMPLOYEES

On December 31, 2016, Dexia Kommunalbank Deutschland had 81 employees (previous year: 78 employees). › 14. Overall, in the period under review eight employees left the Bank while eleven new employees were hired.

14 Personnel information

	Male	Female	Total
Total employees	**43**	**38**	**81**
Part-time employees	**1**	**17**	**18**
1. Age			
Under 29 years old	3	1	4
30 – 39 years old	17	11	28
40 – 49 years old	11	12	23
50 – 59 years old	11	12	23
60 years old or older	1	2	3
2. Period of service			
Less than 5 years	17	9	26
5 – 10 years	11	10	21
11 – 20 years	12	14	26
More than 20 years	3	5	8

Remuneration policy

The remuneration policy of Dexia Kommunalbank Deutschland provides an important contribution to the achievement of the Bank's business goals. The Bank fosters its employees' motivation and loyalty through an attractive and competitive remuneration system. Due to its adoption of the Dexia Group's Group Remuneration Policy, the Bank has ensured that its remuneration system complies with uniform Group standards.

The Bank's overall remuneration package consists of fixed and variable remuneration components. On December 31, 2016, the Bank had 40 employees whose fixed salaries are determined in accordance with the wage agreement for the private banking sector, as amended. The Bank's 41 employees not covered by a wage agreement receive individually negotiated fixed salaries.

On the basis of the collective bargaining agreement for performance-related variable remuneration which was already concluded with the works council on December 2, 2015, an essentially identical agreement was signed with the representative body for senior executives with effect as of February 1, 2016.

The Bank's variable remuneration rewards employees' commitment and their outstanding performance in the past financial year and thus serves as an incentive system. Variable remuneration is determined on the basis of a target bonus adjusted in line with the employee's position, according to an individual assessment of specific competences as well as fulfilment of qualitative and quantitative goals. The Management Board determines the overall budget for variable remuneration through a formalised process, and its scope reflects the Bank's risk-bearing capacity, results of operations and long-term planning. The volume of the overall budget is subject to approval by the Supervisory Board. Payments will only be made if the results of operations of the Bank permit this, subject to due consideration of Section 7 of the German Ordinance on the Supervisory Requirements for Institutions' Remuneration Systems (Institutsvergütungsverordnung, InstitutsVergV) and Section 45 (2) Clause 1 No. 6 of the German Banking Act (Kreditwesengesetz, KWG). Variable remuneration is paid out in full, in the form of a cash payment. The Bank does not have any share-based remuneration model.

The volume of variable remuneration for the Management Board for the past financial year and the terms of its payment are decided at the first meeting of the Supervisory Board each year, on the basis of agreed goals, individual performance levels and the Bank's business development.

While complying with the Remuneration Policy of the Dexia Group – according to which an employee's variable remuneration may not exceed 30% of his fixed salary – for the financial year 2015 in May 2016 the Bank paid overall variable remuneration of EUR 388,000 to a total of 69 persons (including the members of the Management Board).

Investing in the future

In the 2nd half of 2016, the Bank commissioned an extensive employee survey in order to measure its employees' levels of loyalty and satisfaction. This confidential survey was carried out by an external consulting firm and included questions covering employees' satisfaction, their level of identification and affinity with the Bank, remuneration and other outline conditions, corporate communications, management culture and each employee's working relationship with his own manager and with the Management Board. The results of the survey were generally positive.

On a scale of 1 (lowest score) to 10 (highest score), employees' level of general satisfaction averaged 7.03. The results and comments gained from the survey – both positive and critical – were presented at an employee meeting, reviewed within the Bank's departments and discussed with the Bank's managers and its works council in order to develop meaningful follow-up measures.

The Bank offers all of its employees the possibility of pursuing individual development measures. This includes internal and external courses covering professional, methodological and management skills.

The contents of the two-year specialist trainee programme launched in February 2013 have been revised, and this programme has been shortened to a period of 18 months. The programme continued in April 2017 with two new trainees in the Back Office and Regulation & Portfolio Management departments.

Social issues

The duration of employees' illness-related absence has decreased and averaged 15.8 days per employee (previous year: 18.7 days per employee).

Extensive minimum standards were laid down in the area of health in the year under review. These include internal training as well as prophylactic measures in the areas of stress prevention, time management and work organisation. Further precautionary measures include a regular ergonomics and occupational safety-based workplace review as well as a health day.

The Supervisory Board of Dexia Kommunalbank Deutschland has specified the following gender ratios, which it aims to achieve by June 30, 2017:

- Proportion of female (male) members of the Supervisory Board: 33% (67%),
- Proportion of female (male) members of the Management Board: 50% (50%).

The Management Board has resolved that the proportion of female employees at the management level which reports directly to the Management Board (department heads and their deputies) should not fall below 30% in 2016 and 2017. At the end of 2016, this ratio amounted to 36.8% (previous year: 40.0%) and was thus slightly lower than in the previous year.

FORECAST REPORT

The Bank envisages the following trends for the financial year 2017:

- The balance sheet total will decrease to approximately EUR 23.9 billion as of December 31, 2017.
- As of December 31, 2017, the Bank's Tier 1 capital is expected to reach a level of around EUR 664.6 million.

- The Bank's Tier 1 capital ratio will likely amount to approximately 24.1% at the end of 2017 and will thus continue to significantly exceed the statutory requirements.
- The Bank expects to report at most a seven-digit figure as its net loss for the year.
- Dexia Kommunalbank Deutschland will maintain an adequate liquidity position.

In summary, for Dexia Kommunalbank Deutschland's financial year 2017 we thus expect that the Bank's net assets, financial position and results of operations will remain stable in overall terms.

In the 4th quarter of 2016, the Bank was notified by the ECB that, within the framework of the SREP, it is obliged in future to comply with a CET1 ratio of at least 5.125% plus the required capital conservation buffer (jointly 6.375% as of December 31, 2017).

This forecast is based on the following assumptions:

Since we expect that the rate of interest on the capital markets will remain low, we have assumed that the creditors' termination rights which are embedded in the Bank's asset positions will not be exercised, while the creditors' termination rights embedded in its liability positions will always be exercised.

With the exception of a marginal volume of loan extensions, the Bank is no longer pursuing any new lending business. Due to the expected net loss for the year, in line with the terms of issue servicing of the profit participation rights capital is not possible.

We expect personnel expenses to be stable overall, at the same level as in the financial year 2016. On the other hand, non-compensation expenses will once again be materially affected by the bank levy, whose value will likely not fall significantly short of the previous year's level.

By way of risk costs, standard costs have been assumed on the basis of average past defaults.

We do not envisage any significant changes in relation to the Bank's financial position. The assets held in the cover pool and the Bank's securities which are eligible for central bank borrowings outside the scope of its cover – which together account for almost all of its assets – continue to be funded by means of Public Pfandbriefe, securities repurchase agreements and also a marginal volume of open-market loans from Deutsche Bundesbank.

Since the start of 2017, the Bank has deliberately gradually reduced the volume of unsecured refinancing funds, which mainly encompasses promissory note loans taken out as well as deposits of municipal customers and other investors. On February 17, 2017, this amounted to EUR 4.1 billion. This trend was due to the decision to replace a significant portion of deposit business with deposits of the parent company, Dexia Crédit Local. However, the Bank intends to remain active on the money market with its various deposit products.

In addition, it intends to once again extend by one more year the term of the EUR 500 million revolving liquidity facility provided by Dexia Crédit Local, which is due to expire in October 2017. The Bank continues to assume that it will not need to draw upon this liquidity facility.

Moreover, we expect that Standard & Poor's A rating (stable outlook) and Scope Ratings' AA– rating (stable outlook) for our Public Pfandbriefe will remain intact in the current financial year. We continue to aim for a nominal overcollateralisation ratio of at least 8.15%, without being statutorily or contractually obliged to do so.

In regard to the Bank's credit exposures, we do not envisage any burdens resulting from the default of borrowers in the government and banking sectors. Nor do we expect our current residual portfolio of financing for semi-public enterprises and our residual volume of project financing to have any negative impact.

The leading indicators for the Eurozone's economic development point to a continuation of its solid overall level of economic growth. In its winter forecast published in February of the current year, for 2017 the European Commission predicts GDP growth of 1.6% in the euro area, combined with a further rise in employment and a declining, albeit still comparably high level of unemployment. The European Commission continues to see private consumption and moderate investment growth as the key factors driving this trend. The consequences of the United Kingdom's withdrawal from the EU, more rapid monetary tightening in the United States and the potential consequences of China's high (and still growing) debt burden are cited as risk factors.

We do not envisage any changes in the legal and organisational structure of Dexia Kommunalbank Deutschland.

In its press release of February 23, 2017 the Dexia Group announced that its consolidated financial statements as of December 31, 2016 had been prepared in accordance with the accounting rules based on the going concern principle. This requires a series of assumptions which form the basis for the business plan for the Dexia Group's restructuring and are outlined below.

- The business plan is based upon market data as of late September 2012. The underlying macroeconomic assumptions are revised every six months, within the scope of a review of the overall plan.
- In particular, the updates implemented on the basis of the data as of late September 2012 which the Management Board of the Dexia Group resolved on November 16, 2016 reflect a refinancing plan which is in line with current

market conditions. They also cover the effects of regulatory changes, such as those resulting from the final wording of the Capital Requirements Directive IV (CRD IV), and implementation of the International Financial Reporting Standard 9 (IFRS 9) which is valid from 2018.
- The revised business plan includes changes to the original business plan which will result in significant adjustments by comparison with the originally assumed process for the resolution of assets, without currently calling into question its basis.
- The business plan assumes that the various units will maintain their banking licences and that Dexia Crédit Local S. A. will maintain its rating.
- The plan moreover relies on a stable funding programme which is dependent on the level of investor demand for debt securities guaranteed by the Belgian, French and Luxembourg governments and on the capacity of the Dexia Group to raise secured funds.
- In this context, following the approval of the restructuring plan in December 2012 the Group's funding structure benefited from an increased secured and guaranteed funding volume, with considerably lower costs and longer maturities than those stipulated in the business plan. This enabled the Group to reduce its refinancing via central banks and to eliminate entirely the extraordinary refinancing mechanisms introduced in 2012. Through prudent liquidity management, the Group has developed liquidity reserves so as to be prepared for rising cash collateral requirements to secure derivative exposures. These reserves amounted to EUR 18.2 billion as of December 31, 2016.

However, uncertainties will continue to apply in terms of the implementation of this business plan, for the duration of the orderly resolution of its assets.
- In particular, its implementation is subject to uncertainties associated with developments in the fields of accounting and regulation.
- Due to the financing structure of the Dexia Group which has been in place since it embarked upon the orderly resolution of its assets, it may not be possible to comply with certain regulatory indicators over time.
- Moreover, the Group remains sensitive to the development of the macroeconomic environment and in relation to market parameters, including exchange rates, interest rates and credit spreads whose fluctuations may influence the business plan. An adverse trend for these parameters might, over the course of time, adversely affect the liquidity position of the Group and its solvency, in particular:
  - due to rising cash collateral requirements to secure derivative exposures (a 10 bp decline in long-term interest rates will result in an increase of approximately EUR 1 billion in cash collateral requirements) or
  - due to effects on valuations of assets, liabilities and OTC derivatives whose fluctuations in value are recognised in the profit and loss account and may result in changes in the AFS reserve as well as the Group's regulatory capital.
- If the level of demand for government-guaranteed bonds were to decline, the Dexia Group might ultimately be forced to use more expensive funding sources, which would directly influence the level of profitability assumed in its original business plan.

Due to the Bank's membership of the Dexia Group, these comments on the Dexia Group are also indirectly applicable for Dexia Kommunalbank Deutschland.

REPORT ON RISKS AND OPPORTUNITIES

RISK MANAGEMENT SYSTEM

Dexia Kommunalbank Deutschland maintains a risk management and risk controlling system for identification, assessment, management, monitoring and notification of key risks and associated risk concentrations. This system is continuously refined.

As part of the Dexia Group, where appropriate and expedient Dexia Kommunalbank Deutschland applies the Dexia Group's standard risk measurement definitions, guidelines and methods. This enables the Bank's consistent inclusion in the Dexia Group's risk management framework.

Within the scope of its annual risk inventory process, all quantifiable and non-quantifiable risks associated with the Bank's business are identified and subsequently assessed in terms of their potential impact on the Bank's net assets, financial and liquidity position and results of operations. Possible effects on Pfandbrief business are also analysed. All of the Bank's relevant organisational units are included in this regular process, which is performed once a year. The following risk types have been classified as significant:
- credit risks (including country risks),
- market risks (including interest rate risks and spread risks),
- liquidity risks and funding risks as well as
- operational risks (including legal risks)

On the basis of the Bank's business strategy and the results of its risk inventory, the Management Board has defined a risk strategy which is consistent with its business strategy, both for the Bank as a whole and for its Pfandbrief business. This risk strategy specifies its risk policy guidelines (risk culture, risk appetite and risk propensity) and defines risk management goals and the relevant risk limitation measures.

Risk policy guidelines and structures are laid down in the organisational manual which all of the Bank's employees have access to via its intranet. This serves as the basis for uniform management of all significant types of risk for Dexia Kommunalbank Deutschland.

The Risk Controlling department provides the relevant decision-makers with the necessary information for management of these risks. It implements the risk strategy prescribed by the Management Board and monitors, in particular, general credit risks, market risks, liquidity risks and operational risks. Risk Controlling is also responsible for the ongoing development of the Bank's risk measurement and valuation methods. In line with the Bank's schedule of responsibilities, the Risk Controlling department reports to the member of the Management Board with responsibility for back office functions.

Internal Audit reviews the appropriateness of the Bank's risk control and risk management system on an ad hoc basis and within the scope of the annual audit plan.

The risk-bearing capacity concept (one-year horizon), the capital planning process (four-year horizon) in accordance with the Minimum Requirements for Risk Management (Mindestanforderungen an das Risikomanagement, MaRisk) issued by the German Federal Financial Supervisory Authority (Bundesanstalt für Finanzdienstleistungsaufsicht, BaFin), the portfolio present value and the portfolio market value indicators are core elements of the Bank's overall risk management system.

In addition, material individual risks are separately registered, analysed, valued and limited.

Risk-bearing capacity concept

Risk-bearing capacity is determined on a standalone basis, according to the going-concern approach and also the liquidation approach. Existing support measures – such as Dexia Crédit Local's letter of support and revolving liquidity facility – are not included in this calculation.

The Bank uses different levels of confidence for each approach: It applies a confidence level of 95.0% for the going-concern approach and a level of 99.9% for the liquidation approach. As a rule, a (rolling) assessment period of twelve months is the reference timeframe. Risk-reducing diversification effects between the individual risk types are only taken into consideration for the market risks risk type. The going-concern approach provides the primary perspective from the point of view of internal risk management. The liquidation approach serves as an additional perspective.

The risk-covering potential is determined on the basis of regulatory capital and the planned outcome for the defined assessment period. The portion of regulatory capital which is necessary for fulfilment of the minimum capital requirements under banking supervision law is deducted from the risk-covering potential.

The calculation of the assignable risk amounts includes in the risk-bearing capacity calculation any risks which have been characterised as material in the risk inventory and may be meaningfully assigned risk-covering potential. If a new, quantifiable material risk is identified in the risk inventory, this will be considered within the scope of the determination of the Bank's risk-bearing capacity. In principle, there is no obligation for non-material risks to be included in the risk-bearing capacity calculation, but they are included in individual cases. Risk amounts are currently determined for credit risk (general credit risk and CVA), market risk (interest rate risk, basis risk and spread risk), funding risk and operational risk. For all of these risk types, a Value at Risk method is applied in order to determine the risk amount, on the basis of various assumptions. Model risks are also considered.

Further latent risks are considered by assigning only part of the overall risk-covering potential to the above-mentioned risk types. › 15

Even though they have been identified as material risks in the risk inventory, the Bank's risk-bearing capacity concept does not include liquidity risks in the narrowly defined sense, since this risk cannot be meaningfully assigned own funds. Dexia Kommunalbank Deutschland has separate procedures for management of liquidity risk.

Since operational risks cannot be managed by means of short-term measures, no separate limit is assigned for them. The limit thus matches the risk contribution and is deducted from the available risk-covering potential.

15 Assumptions for the calculation of risk-bearing capacity

	Risk type	Comments on the risk measurement methods
General credit risk	Non-specific general credit risk	Calculation of a Value at Risk using the Gordy model with a granularity adjustment (Hirschman-Herfindahl index).
	CVA charge	Calculation in accordance with the standardised method in compliance with regulatory requirements (Article 384 of the CRR).
Market risk		Comprises interest rate risk, basis risk and spread risk. Value at Risk on the basis of a historical simulation for all current assets positions and subject to trustee dual control.
Funding risk		Conservative estimate of the accumulated liquidity gap for the one-year horizon and closure subject to increased refinancing premiums.
Operational risk		Statistical approach on the basis of a historical simulation of all loss events since recording of losses began.

16 Risk-bearing capacity according to a going-concern perspective in the normal scenario

Risk-covering potential	Available Risk-covering potential		Provided risk-covering potential	
in EUR million	31.12.2016	31.12.2015	31.12.2016	31.12.2015
Eligible capital	680.9	637.0	90% of the available risk-covering potential	
Own funds requirements	−253.7	−277.5		
Free eligible capital	**427.2**	**359.5**		
Horizon Δ eligible capital	4.2	29.1		
Horizon Δ own funds requirements	−36.8	−21.7		
Further elements of risk-covering potential	−25.0	30.4		
Total	**369.6**	**397.3**	**332,6**	**357,6**

Risk potential

	Limit on provided risk-covering potential		Utilisation	
	in EUR million		as %	
	31.12.2016	31.12.2015	31.12.2016	31.12.2015
General credit risk & CVA charge	125.5	83.9	70.3	102.5
Market risk	78.4	117.4	38.5	79.1
Funding risk	109.8	134.2	91.6	71.0
Operational risk	18.9	22.1		
Total	**332.6**	**357.6**	**71.5**	**82.8**

Within the scope of the ongoing methodological development of the Bank's risk-bearing capacity system, in the financial year 2016 the following significant changes to the risk-bearing capacity concept were implemented:

› ongoing development of the integrated market risk measurement tool,
› limitation of the assignment of market risk to positions which are subject to a level of market risk which is relevant under commercial law,
› expansion of the LGD methodology for determination of the credit risk contribution,
› reallocation of the risk limits (increase for credit risks, reduction of market risk and funding risk) and
› adjustments due to validation results (e. g. adjustment of the model risk premium).

On the basis of the going-concern approach, the Bank's risk-bearing capacity is intact as of December 31, 2016. › 16 Due to the methodological changes outlined above, the previous year's figures are not fully comparable.

In addition, the Bank uses risk management instruments in the form of individual reports on all relevant risk types which provide detailed information on the key risk drivers and changes to these risk drivers over time. They thus provide important information for internal risk management purposes, both at the level of the overall Bank and at the level of individual risks.

Moreover, the Bank regularly conducts stress tests for all key risk types – including all relevant positions – within the scope of its risk-bearing capacity calculation.

Portfolio present value and portfolio market value

Another key control parameter is the portfolio present value (PPV), which is calculated every day and reported to the Bank's decision-makers. For this purpose, the present values of all interest-bearing balance-sheet and off-balance sheet positions are pooled and supplemented with other assets as well as associated balance-sheet positions. The PPV provides an indication of the development of the portfolio value, subject to a going concern assumption. At the end of the year, the PPV to Tier 1 capital ratio amounted to 1.54. The PPV is supplemented by the portfolio market value (PMV) – which also considers the credit spreads of asset and liability positions and thus reflects a liquidation scenario – and by the scenario PPV, which also includes the assumption of increased costs, in order to close funding gaps.

Stress tests

Stress scenarios are an important component of the Bank's risk management process, in order to identify risk concentrations and possible equity capital shortfalls. They provide transparency regarding the effects of extraordinary but plausible events.

For the market risk and liquidity risk types, the Bank calculates the stress tests required by MaRisk on a daily basis.

In addition, quarterly historical stress tests are implemented for all individual risk types (general credit risk, market risk, funding risk and operational risk). Moreover, a core area of focus is the hypothetical overall bank stress tests, which are based upon the "sovereign debt crisis" scenario and also the "serious economic downturn" scenario.

The results of these stress tests are considered in the overall assessment of risk-bearing capacity, and they may thus serve as a basis for implementation of enhanced risk monitoring measures.

Risk management for Pfandbrief business

As a Pfandbrief bank, Dexia Kommunalbank Deutschland falls under the scope of the German Pfandbrief Act (Pfandbriefgesetz, PfandBG). This requires a suitable risk management system (Section 27 PfandBG) for monitoring of all risks associated with Pfandbrief business.

As well as safeguarding compliance with the statutory requirements in regard to overcollateralisation for Pfandbriefe, in line with the dynamic approach pursuant to Section 5 (1) and Section 6 (2) of the German Pfandbrief Present Value Regulation (Pfandbrief-Barwertverordnung, PfandBarwertV) the Bank calculates stress scenarios for interest-rate and currency risks. In case of an impending fall below a present-value overcollateralisation level of 2%, measures must be implemented immediately to ensure compliance with the statutory requirements. For some time now, the Bank has maintained a nominal overcollateralisation ratio (ratio of the nominal value of the cover pool to the nominal value of the Pfandbriefe outstanding) of at least 8.15%, without being statutorily or contractually obliged to do so.

Credit risk for the cover pool is restricted by means of a limit system. The cover portfolio focuses on high-quality assets with ratings within the rating interval of AAA to A+. In addition, the proportion of cover assets with a non-investment grade rating is limited.

While at the overall bank level foreign-currency risk is hedged by means of derivative transactions, as a rule, the derivatives incorporated in the foreign-currency positions are not included in the cover pool. Open foreign currency positions thus exist at the level of the cover pool, but are restricted by means of limits. In addition, various cash flow analyses are implemented for monitoring of liquidity risk, and risk concentration is monitored at the borrower level.

RISKS

CREDIT RISKS

Credit risk is the risk of a borrower or a contracting party being unable to meet its obligations to Dexia Kommunalbank Deutschland, either in whole or in part.

To limit credit risks, subject to consultation with the Dexia Group the Management Board specifies credit lines and lending authority rules for all contracting parties. The same applies for clearing houses and central counterparties.

Dexia Kommunalbank Deutschland has frozen all credit lines (except for money market and derivative limits) for new risk exposures. Moreover, all contracting parties entered on the Bank's monitoring list due to defined criteria (including a downgrade of four notches/a rating which reaches the non-investment grade segment) are separately monitored.

Market-independent credit analysis and loan processing is ensured through an appropriate operational structure for management of credit risks.

The following measures are implemented in order to limit credit risk and the related concentrations of risk:

- credit line monitoring,
- monitoring of credit default risk,
- early risk-detection methods,
- reporting on external and internal rating changes and
- portfolio management and monitoring on the basis of the general credit risk report and the results of the risk-bearing capacity calculation, including stress scenarios.

The Management Board and the Supervisory Board are regularly notified of the credit risk and the measures implemented to limit this risk.

Derivative transactions may only be entered into subject to the legally binding conclusion of a German Framework Agreement or an ISDA Framework Agreement with the contracting party. A further precondition is the legally binding conclusion of a credit support annex (CSA) in accordance with the Bank's standards. The value of the collateral exchanged is monitored on a daily basis. Detailed information regarding the value and structure of the collateral granted is provided every week at the Management Board's meeting. As of December 31, 2016, the Bank had a net contributor position of EUR 3.8 billion (previous year: EUR 3.6 billion).

The Risk Controlling department provides and monitors the calculation for levels of credit line utilisation on a daily basis. The Management Board is immediately notified of any overruns of credit lines and is obliged to decide on appropriate measures. In the period under review, due to fair value fluctuations 65 overruns occurred for individual borrowers in the derivatives portfolio. These overruns were immediately eliminated.

German debtors account for approximately 61.3% (previous year: 59.1%) of the Bank's credit exposures, followed by debtors in Italy (15.2%) and Belgium (6.5%).

Moreover, around 92.4% of the Bank's assets are eligible for cover and some of them are also eligible for central bank borrowings and for repo transactions. As of December 31, 2016, 96.4% of all assets have an internal rating of BBB– (investment grade) or higher. Adequate risk classification systems (ratings) are in place for all of the Bank's customer groups. Due to the structure of existing business, portfolio management focuses on regionally diversifying and credit rating class-related management. Foreign claims resulting from loans and securities especially undergo a regular review covering existing risks and opportunities and the resulting strategic options.

The Bank's volume of assets (including credit risk mitigation techniques) is shown for each specific asset class in Tables › 17 and › 18, with a breakdown of external and internal ratings on the basis of the CoRep reporting as of December 31, 2016.

17 Total exposure by external rating

Asset class	External rating	Risk position		Average risk weight
		31.12.2016	31.12.2015	
		in EUR million	in EUR million	as %
Central governments or central banks	AAA to AA–	14,331.4	15,528.4	0.0
	A+ to A–	245.2	232.1	20.0
	BBB+ to BBB–	–	–	–
	BB+ to BB–	326.9	–	0.0
	B+ to B–	–	–	–
	No rating	–	–	–
Regional or local authorities	AAA to AA–	–	–	–
	A+ to A–	–	–	–
	BBB+ to BBB–	61.8	64.9	20.0
	BB+ to BB–	–	–	–
	B+ to B–	–	–	–
	No rating	–	–	–
Public sector entities	AAA to AA–	343.5	448.5	20.0
	A+ to A–	–	–	–
	BBB+ to BBB–	–	–	–
	BB+ to BB–	–	–	–
	B+ to B–	–	–	–
	No rating	108.5	117.8	100.0
Multilateral development banks	AAA to AA–	267.0	265.2	0.0
	A+ to A–	–	–	–
	BBB+ to BBB–	–	–	–
	BB+ to BB–	–	–	–
	B+ to B–	–	–	–
	No rating	–	–	–
Institutions	AAA to AA–	24.5	–	0.3
	A+ to A–	40.4	17.1	50.0
	BBB+ to BBB–	–	–	–
	BB+ to BB–	–	–	–
	B+ to B–	–	–	–
	kein Rating	119.9	96.2	2.0
Corporates	AAA to AA–	14.1	3.5	20.0
	A+ to A–	–	–	–
	BBB+ to BBB–	–	–	–
	BB+ to BB–	–	–	–
	B+ to B–	–	–	–
	No rating	157.1	182.8	100.0
Defaulted positions	CCC+ or lower	0.0	220.2	100.0
Others	AAA to AA–	85.4	90.1	0.0
	A+ to A–	92.8	92.8	0.0
	BBB+ to BBB–	–	–	–
	BB+ to BB–	25.1	25.1	0.0
	B+ to B–	–	–	–
	No rating	219.8	578.8	100.0
Total		**16,463.2**	**17,963.4**	–

18 Total exposure by internal rating

Asset class	Internal rating	Risk position 31.12.2016 in EUR million	Risk position 31.12.2015 in EUR million	Average default probability as %	Average loss given default as %	Average risk weight as %	Average expected loss as %
Central governments and central banks	AAA to AA–	1,487.5	1,652.5	–	5.1	–	–
	A+ to A–	109.8	638.7	0.1	20.0	16.8	0.0
	BBB+ to BBB–	3,505.1	3,168.9	0.2	26.8	42.4	0.1
	BB+ to BB–	–	421.4	–	–	–	–
	B+ to B–	–	–	–	–	–	–
Institutions	AAA to AA–	231.3	377.3	0.0	3.0	1.8	0.0
	A+ to A–	626.6	773.5	0.1	14.3	13.9	0.0
	BBB+ to BBB–	807.1	683.6	0.3	15.6	31.3	0.0
	BB+ to BB–	238.1	413.7	1.4	6.1	20.3	0.1
	B+ to B–	25.9	67.0	4.6	0.5	1.6	0.0
Corporates	AAA to AA–	–	–	–	–	–	–
	A+ to A–	–	7.5	–	–	–	–
	BBB+ to BBB–	36.7	32.9	0.4	27.9	45.4	0.1
	BB+ to BB–	–	–	–	–	–	–
	B+ to B–	–	–	–	–	–	–
Other non credit-obligation assets	AAA to AA–	2.5	0.1	–	5.0	–	–
	A+ to A–	50.3	57.5	0.1	30.3	20.1	–
	BBB+ to BBB–	4.1	0.3	0.2	33.3	27.6	–
	BB+ to BB–	–	–	–	–	–	–
	B+ to B–	–	–	–	–	–	–
Total		**7,125.1**	**8,295.0**	**–**	**–**	**–**	**–**

As well as the Internal Rating Based Approach (IRB Approach) pursuant to Articles 142ff of the CRR, the Bank also uses the Credit Risk Standard Approach pursuant to Articles 111ff of the CRR for determination of the total capital charge for credit risks. Exposure values under the IRB Approach are determined for loans to central governments and central banks, institutions and corporates. If the Bank has not implemented any independent rating systems for borrowers for which the usage requirements for the IRB Approach are fulfilled, the Credit Risk Standard Approach is applied for these credit risk positions in accordance with the CRR. In particular, this comprises loans to German and foreign municipal and semi-public enterprises. German federal states and their municipalities are permanently excluded from application of the IRB Approach under Article 150 of the CRR.

As a company belonging to the Dexia Group, the Bank applies the standard rating methods of the Dexia Group. This includes regular validation of the methods and models applied. Please refer to the annual risk report of the Dexia Group for further information regarding the rating models used, the model assumptions and the premises for the methods applied.

The ratings determined on the basis of the internal risk classification methods and the associated probabilities of default (PD) and loss given defaults (LGDs) are an integral part of the Bank's approval, monitoring and control processes.

Within the scope of the risk-bearing capacity calculation, credit risks are quantified by means of a credit default model (CVaR, Gordy model). These results undergo a detailed plausibility and development analysis.

Credit exposure to public-sector entities and financial institutions

Table › 19 shows Dexia Kommunalbank Deutschland's nominal credit exposure and credit risk equivalence amounts in relation to borrowers, with a breakdown by country.

The Bank is not subject to any significant risks in connection with the United Kingdom's decision to leave the EU (Brexit). At the end of the year, Dexia Kommunalbank Deutschland's book of business included claims against banks or subsidiaries domiciled in the United Kingdom with a volume of EUR 129.0 million and against branch offices of international financial institutions domiciled in the United Kingdom with a volume of EUR 42.6 million. The Bank also holds European government bonds denominated in British pounds with a volume of 80.0 million British pounds, for which the exchange risk is fully hedged through currency swaps.

Risk provisioning

The fair value of existing repayment and interest claims held within the loan book is reviewed within the scope of regular (at least quarterly) and also ad hoc loan monitoring. An ad hoc review is implemented in case of negative information (early warning indicators) regarding the borrower, which may result in this borrower's inclusion on the Bank's monitoring list, for instance. Credit-related default or default on interest or redemption payments of more than 90 days are objective indications that may also necessitate a valuation adjustment.

MARKET RISKS

Market risk comprises the following key sub-categories:

- interest rate risks (including basis risks),
- credit spread risks and
- foreign currency risks.

Interest rate risk refers to the loss potential on interest-related positions which result from a change in the interest rate level or the interest rate structure for the Bank's portfolio value.

As a rule, interest rate risks are hedged by entering into interest rate swaps. Limits restrict the residual interest rate risk. Interest rate risk is managed and monitored at the portfolio level and at the overall bank level.

The management has at its disposal two risk-related indicators which are calculated on the basis of the fair value method as key management parameters for interest rate risks: the Basis Point Value (BPV or PV01) and Value at Risk (VaR).

The BPV describes the potential present-value change in the overall portfolio in case of a parallel change in the interest rates for the full range of maturities by 100 basis points, while PV01 describes this in case of a 1 basis point increase per defined maturity band.

The Value at Risk (VaR) calculates the maximum expected loss within a defined holding period, with a defined degree of probability. The Bank calculates the VaR every day, on the basis of a confidence level of 99.0% and a holding period of ten days. The Bank has created various sub-portfolios: the long-term sub-portfolio Balance Sheet Management (BSM) and the short-term sub-portfolio Cash & Liquidity Management (CLM).

For short-term and long-term interest rate risks, various +/– 100 BPV and VaR limits apply. In addition, the interest rate risk (PV01) maturity ranges specified for the BSM are limited. The interest sensitivity of the credit spreads is measured daily. No separate limit is imposed.

19 Credit exposure to public-sector entities and financial institutions as of December 31, 2016*

Country	Sovereign	Sub-sovereign entities	Others	Total	as part of cover pool for Public Pfandbriefe (nominal)	loans	securities	average weighted residual maturity
	in EUR million	in EUR million	in EUR million	in EUR million	in EUR million	in EUR million	in EUR million	in years
Belgium	–	1,304.7	213.6	1,518.4	1,196.3	1,438.3	45.0	8.8
Germany	128.4	13,397.4	816.4	14,342.3	12,967.5	12,273.7	1,821.2	10.8
France	–	14.4	159.7	174.0	12.0	–	48.7	6.0
United Kingdom	–	–	129.0	129.0	–	–	84.8	4.3
Italy	3,133.5	301.0	126.3	3,560.7	2,452.3	–	3,488.4	12.1
Japan	–	245.2	–	245.2	232.7	–	245.2	20.3
Austria	69.5	1,016.0	–	1,085.5	1,047.4	1,032.8	52.7	6.1
Poland	109.8	–	–	109.8	–	–	109.8	3.3
Portugal	463.1	50.0	313.5	826.6	522.5	225.3	601.4	9.4
Spain	18.8	–	430.7	449.5	78.8	–	449.4	6.7
USA	–	373.8	42.6	416.4	226.5	–	373.8	11.8
Supranational	–	–	267.1	267.1	191.2	–	267.1	7.6
Others	90.5	101.2	67.5	259.2	183.3	101.2	157.4	2.1
Total	**4,013.5**	**16,803.7**	**2,566.6**	**23,383.7**	**19,110.5**	**15,071.2**	**7,744.9**	

* Repo and derivatives transactions have been recognised at their credit equivalent amount; loans and securities at their carrying amount; not including cover pool assets.

As of December 31, 2016, these limits are as follows: › 20

20 Limits for management of interest rate risks

in EUR million	Value at Risk (99%, 10 days)	+/−100 bp
Cash & liquidity management	1.5	15.0
Balance sheet management	–	5.0
Total	**2.5**	**–**

The following figures resulted on the basis of these assumptions: › 21 and › 22

21 Limit utilisation for cash & liquidity management

in EUR million	Value at Risk (99%, 10 days)	+100 bp	−100 bp
Average	0.3	6.2	−6.2
Minimum	0.1	−1.0	−12.7
Maximum	1.1	12.7	1.0
Last trading day	0.2	5.6	−5.6

22 Limit utilisation for balance sheet management

in EUR million	Value at Risk (99%, 10 days)	+100 bp	−100 bp
Average	0.3	−2.2	2.3
Minimum	0.1	−4.4	−0.2
Maximum	1.0	0.2	4.7
Last trading day	0.3	−2.6	2.8

The Treasury department which is responsible for the management of interest rate risks is notified daily of the development of interest rate risk and the level of limit utilisation. The Bank's Asset Liability Management Committee – which meets on a monthly basis – is responsible for strategic interest rate risk management.

Credit spreads reflect the yield markup on bonds subject to a risk of default. The Bank regularly measures the valuation effects of changes in credit spreads. Credit spread risks are not limited at the portfolio level. Credit spread risk is restricted within the scope of the risk-bearing capacity system.

The Bank holds a large volume of European government bonds, some of which were subject to heightened spread risks over the past few years. Risk premiums widened slightly in the year under review, particularly for claims against government entities of the peripheral Eurozone countries Italy, Portugal and Spain. A widening of the risk premiums for these bonds will generally have a negative impact on the Bank's risk situation.

Foreign-currency risk results from negative changes in value due to exchange-rate fluctuations of foreign currencies. As a rule, the Bank hedges foreign-currency risks by means of cross-currency swaps. As of December 31, 2016, it did not have any non-hedged foreign currency positions. Applicable currency basis risks are regularly monitored, but are not limited.

LIQUIDITY RISKS

Liquidity risks consist of the following sub-categories:
- liquidity risk (more narrowly defined),
- funding risk and
- market liquidity risk.

Liquidity risk refers to the risk of the Bank being unable to fulfil its present and future payment commitments in a timely manner or of being unable to fulfil them in full.

As an important liquidity control instrument, a liquidity forecast is produced every day and provides an overview of liquidity movements. Moreover, the Risk Controlling department determines the short-term liquidity risks by comparing the defined liquidity reserve with the accumulated liquidity requirements for the following month (liquidity position). This liquidity position is determined on a daily basis, subject to various stress scenarios (idiosyncratic stress, market-wide stress, combined stress) in accordance with MaRisk section BTR 3.2. These calculations refer to the following periods: "spot-next" (for the next-but-one working day), one week and one month.

As well as the absolute liquidity position, Table › 23 shows the ratio of the reserve to the liquidity gap in the various liquidity scenarios.

Securities eligible for Eurex Repo and ECB borrowings which are classified as highly liquid investments and are not used within the first week are recognised as a liquidity reserve. Beyond the scope of this one-week period, free securities eligible for Eurex Repo or ECB borrowings are included in the reserve. In addition, in determining its overall reserve to cover any liquidity gaps arising, the Bank considers various haircuts (ECB and stress haircuts) as well as Pfandbrief overcollateralisation assumptions.

The tightest liquidity position (reserve plus liquidity gap) for the spot-next, one week and one month periods is reported daily.

To determine the liquidity gap, maturity assumptions (holding periods) for unsecured deposits of municipal customers and other investors are included in the scenarios. In addition, pro rata drawing on the guarantees and liquidity lines provided by Dexia Kommunalbank Deutschland and liquidity outflows resulting from the increased payment of cash collateral are simulated.

23 Liquidity scenarios according to MaRisk, section BTR 3.2, as of December 31, 2016

	Horizon	Date	Reserve	Liquidity gap	Liquidity position	Reserve / liquidity gap
			in EUR million	in EUR million	in EUR million	as %
Normal scenario	Spot/next	03.01.2017	2,812.8	−314.0	2,498.8	895.7
	1 week	07.01.2017	2,812.5	−495.5	2,317.0	567.6
	1 month	31.01.2017	3,902.2	−2,108.9	1,793.4	185.0
Institution-specific stress scenario	Spot/next	03.01.2017	3,773.6	−983.2	2,790.4	383.8
	1 week	07.01.2017	3,773.2	−1,138.8	2,634.4	331.3
	1 month	31.01.2017	4,864.6	−2,907.6	1,957.0	167.3
Market-wide stress scenario	Spot/next	03.01.2017	3,126.2	−407.3	2,718.9	767.5
	1 week	07.01.2017	3,125.8	−722.2	2,403.6	432.8
	1 month	31.01.2017	4,172.3	−2,593.1	1,579.2	160.9
Combined stress scenario	Spot/next	03.01.2017	4,046.1	−1,076.5	2,969.7	375.9
	1 week	07.01.2017	4,045.8	−1,365.5	2,680.3	296.3
	1 month	31.01.2017	4,997.2	−3,391.9	1,605.3	147.3

The long-term liquidity risk is measured on a monthly basis by comparing the liquidity requirements and the liquidity surplus (gap) with the liquidity reserves for the various maturity bands within a period of five working days following the last day of the month, for a period of up to 50 years. In addition, a short-term (90 days) and a long-term (ten years) liquidity fore-cast is produced on a monthly basis. Moreover, the Bank has implemented scenarios for forecast periods of up to twelve months, which are based on the scenarios used for liquidity measurement of up to one month.

Funding risk refers to the risk of only being able to obtain the necessary liquid funds at increased funding costs.

The Bank measures the risk of increased strain on its future results of operations due to structural liquidity mismatches (liquidity gaps) by regularly analysing the maturity mismatches between asset and liability positions, at the level of the overall bank and at the level of the cover pool. The simulations based on these analyses illustrate the likely effects on future results of operations in case of an increase in the funding costs. No limit applies for the maturity mismatch at the level of the overall portfolio. The Bank's Asset Liability Management Committee measures maturity mismatches and analyses any necessary measures on a monthly basis.

Funding risk is also restricted by means of a limit in the risk-bearing capacity concept. On the development of the Bank's funding structure, please also refer to the financial and liquidity position section.

The Bank's liquidity situation remained adequate and it maintained a high volume of claims which have solid credit ratings and are eligible for cover and for central bank borrowings, together with active deposit business. It will thus remain possible to exploit the resulting opportunities, in order to achieve a balanced funding mix subject to advantageous funding terms.

Market liquidity risks refer to the risk of being unable to unwind transactions due to insufficient market depth or in case of market disruptions or of only being able to do so subject to losses.

The going-concern/held-to-maturity approach of Dexia Kommunalbank Deutschland assumes that positions will be held up to their final maturity – unless permanent impairment is apparent – and that market liquidity risks will thus not be relevant for valuation purposes. All of the Bank's securities have therefore been entered on its banking book. It does not have any positions in its trading book.

Dexia Kommunalbank Deutschland considers market liquidity risks to be non-material. However, the realisability and refinancing capacity of its assets (in particular, of the securities held) are monitored daily within the scope of its liquidity risk management and are assessed in appropriate stress scenarios.

OPERATIONAL RISKS

The Bank defines operational risk as the risk of direct or indirect losses which arise due to the inappropriateness or the failure of internal processes and systems or personnel or due to external events and which have financial or non-financial effects. This definition includes, in particular, legal risks, personnel risks, IT-related systemic risks and also reputational risks and risks associated with outsourcing and projects.

The ultimate goal for management of operational risks is to minimise losses which may result from operational loss events, to avoid risks jeopardising the Bank's existence and to identify and monitor material operational risks within the scope of the Risk Control and Self Assessment (RCSA) which must be performed at least annually. This also includes the continuous improvement of existing procedures and the review of possible measures to reduce the level of complexity and for automation of existing processes and controls.

Operational events which have resulted in an unexpected loss or a profit of more than EUR 1,000 are notifiable incidents. Cases with significant non-financial effects are also included and classified by means of a rating scale.

The Bank uses a Group-wide IT application for registration, valuation, monitoring and historicisation of operational risks. In case of losses, the departments involved are required to analyse the relevant business processes, estimate the loss and produce proposals on how to avoid this in future. Through an escalation process, the overall Management Board and Internal Audit are immediately notified of any loss events.

The Operational Risk & Information Security Committee, which meets on a quarterly basis, discusses losses and risks with the Management Board, representatives of the IT department, the IT and information security officer, the compliance officer and the Bank's Internal Audit department. The Operational Risk Management system (Risk Controlling) registers notified losses. Overall, eight cases were reported in 2016.

The annual RCSA identifies and analyses the operational risks in the various processes by means of risk inventories and reviews the control systems for risk limitation. Possible measures enabling a reduction in the level of risk are discussed and, where expedient, action plans are agreed whose implementation is monitored by the Operational Risk Management system. Following completion of the RCSA process, the results of the individual RCSAs are presented to the Management Board.

For its implementation of projects, the Bank uses an appropriate project risk management system in order to identify possible events or situations with a negative impact (damage) on the project's outcome as a whole or on individual planning factors – such as its scope, the costs and the volume of time required – and to prevent, or at least minimise, these events or situations by initiating appropriate measures. The Bank's Project Management Office Committee, which meets on a monthly basis, monitors the overall project risks.

The Bank has also established processes through which it is able to manage and monitor outsourcing activities pursuant to Section 25b KWG as well as changes relating to new processes or new products or markets. No material risks have been identified.

The IT infrastructure and the operational structure include contingency plans and packages of measures for the purposes of risk limitation and risk avoidance. In addition, within the scope of its contingency planning the Bank maintains an emergency data centre in order to ensure business continuity in case of crisis situations.

In regard to the Bank's currently applicable legal risks, it should be pointed out that legal proceedings are pending in four cases that relate to variable-rate loans which Dexia Kommunalbank Deutschland granted in 2006 and 2007 and whose interest rate is tied to the development of the Swiss franc's exchange rate against the euro. This entails a loan volume with an outstanding principal balance of EUR 9.4 million as of December 31, 2016. This volume is divided up between a small number of borrowers. Dexia Kommunalbank Deutschland has rejected the claims brought against it in these proceedings. In three of these four cases, the court of first instance found entirely in favour of Dexia Kommunalbank Deutschland, while in the fourth case its ruling was only partially in favour of the Bank. Two of these four legal disputes are currently subject to appeal proceedings. In the other two cases, the appeal proceedings have already been completed; the court of appeal has ruled in the Bank's favour in one case and against it in another. Appeal proceedings on points of law have been initiated against both of these appeal decisions. In two further cases, complaints of profit participation certificate creditors are pending versus Dexia Kommunalbank Deutschland whose amounts in dispute represent a low seven-digit figure overall. The two plaintiffs are an investment company and its managing partner. In relation to the complaint involving the far larger amount in dispute, in March 2017 a first partial ruling (which is not yet non-appealable) was issued in favour of Dexia Kommunalbank Deutschland for almost all of the matter in controversy. Only in relation to a low-value partial claim was the case not yet ready for a decision. This decision will be made at a later date. In view of the court rulings already issued in similar cases, the Bank is confident that the complaints will be dismissed outright and with final effect.

SUMMARY OF RISK SITUATION

Through the implementation of the revised plan for the restructuring of the Dexia Group of December 28, 2012, a stable long-term framework was established for the future business activities of the Group and thus also for Dexia Kommunalbank Deutschland.

In the year under review, the Bank's risk situation was significantly improved through an agreement reached on the repayment of the Bank's overall claim against Heta Asset Resolution AG (see Business performance section – Claims against Heta Asset Resolution AG).

On the other hand, credit spreads on claims against government entities of the peripheral Eurozone countries Italy, Portugal and Spain have increased slightly, which has generally had a negative impact on the Bank's risk situation. In the reporting period, the Bank's total nominal credit exposure to these countries decreased from EUR 5,036 million to EUR 4,837 million.

Besides natural amortisation of its loan and securities portfolio, the sale of various bank and German federal state bonds reduced the volume of risk assets. Overall, the Bank's volume of assets with a non-investment grade rating has decreased to 3.6% of its credit portfolio (previous year: 5.1%).

The level of utilisation of risk-bearing capacity, within the scope of the going-concern approach, has decreased to 71.5% (previous year: 82.8%). This is mainly attributable to the reduction in market risk. The volume of further risks changed only slightly in the year under review. The risk-covering potential provided decreased slightly, by EUR 24.9 million, mainly due to the increasing minimum capital requirements and the shrinkage of Tier 2 capital.

The Bank's liquidity situation remained adequate and it maintained a high volume of claims which have solid credit ratings and are eligible for cover and for central bank borrowings, together with active deposit business.

The Bank's own funds increased to EUR 680.9 million (previous year: EUR 637.0 million). This is chiefly attributable to the portion of the valuation allowance released by the Bank for its overall claim against Heta Asset Resolution AG. The Bank's CET1 ratio increased to 22.2% (previous year: 17.3%), and its total capital ratio to 23.2% (previous year: 18.7%). Both of these capital ratios significantly exceed the regulatory requirements.

Accumulated losses will decrease upon approval of the annual financial statements by the Management Board and the Supervisory Board, due to calling upon the profit participation rights capital. Allowing for these effects, on December 31, 2016 the CET1 ratio will increase to EUR 662.7 million (previous year: 657.5 million). The CET1 ratio calculated according to the CRR will then reach 22.5%, and the total capital ratio 23.5%.

No events occurred after the balance sheet date which would necessitate a different assessment of the risk situation.

CHANGES IN REGULATORY REQUIREMENTS

The EU regulation on transparency of securities financing transactions and of reuse of financial instruments received as collateral (SFTR) came into effect on January 12, 2016. In 2016, this Regulation initially only gave rise to notification obligations for the Bank.

The basis for the Additional Liquidity Monitoring Metrics (ALMM) notification was established through publication of the implementing technical standard for the liquidity reporting pursuant to Article 415 of the CRR. This notification requires additional parameters for liquidity monitoring and has been reported monthly since April 2016.

On June 30, 2016, the Bank was required for the first time to provide quarterly financial reporting (FinRep) in compliance with regulatory requirements, in accordance with the simplified approach. The FinRep notification requires granular information on the balance sheet, profit and loss account, off-balance sheet transactions, collateral received, valuation adjustments and on risk provisioning.

New market abuse legislation came into effect in Germany (and Europe) on July 3, 2016. Since this time, the First German Act Amending Financial Market Regulations due to European Legal Instruments (Erstes Gesetz zur Novellierung von Finanzmarktvorschriften aufgrund europäischer Rechtsakte, 1. FiMaNoG) and the Market Abuse Regulation (MAR, Regulation (EU) No 596/2014) have served as the legal framework for insider dealing, unlawful disclosure of insider information, market manipulation and market abuse. The EU has prescribed this legal framework in response to the financial crisis in the field of capital market law, so as to improve the markets' stability and protection for investors. The Bank has adjusted its internal rules and regulations and procedures in line with the requirements of this new market abuse legislation.

The Common Reporting Standard (CRS) requires financial institutions to report accounts which are held, directly or indirectly, by accountholders resident for tax purposes in a CRS state. The Bank has implemented all necessary measures so as to be able to provide these reports from 2017.

The Delegated Regulation on collateralisation of non-cleared OTC derivatives (EMIR collateralisation RTS) was published on December 15, 2016. From March 1, 2017, new collateralisation obligations will thus apply for OTC derivatives newly entered into which are not subject to clearing.

On February 19, 2016, BaFin published its consultation paper (02/2016) on the fifth amendment of its MaRisk standards.

Final publication is expected in the 1st quarter of 2017. Following publication, the Bank will identify and implement concrete measures by means of a gap analysis.

The requirements for remuneration systems are subject to ongoing development, above all in the context of the sound remuneration policy guidelines published by the European Banking Authority (EBA) on December 21, 2015 (the EBA guidelines). The revised version of InstitutsVergV of January 19, 2017 takes into consideration the practical feedback resulting from the consultation procedure. InstitutsVergV will come into effect on March 1, 2017.

INTERNAL CONTROL SYSTEM AND RISK MANAGEMENT SYSTEM

Information management

All risk-related information is centrally registered in the Bank's risk management system, systemically processed within the framework of its reporting and provided to the Bank's decision-makers every day, or more frequently if necessary. The IT system also provides the competent employees with access to analysis results. A functional and targeted flow of information which is tailored to its specific recipients ensures a high level of risk awareness on the part of the employees of Dexia Kommunalbank Deutschland.

Accounting-related internal control and risk management system

The goal of the accounting-related internal control and risk management system is to ensure compliance with accounting standards and regulations and to ensure the orderliness of the accounting, including correct information in financial statements.

The Accounting department is responsible for the general ledger and for regular monitoring of the accounting and its adjustment in line with statutory and regulatory changes. The Back Office department handles inventory management of banking business in the subsidiary ledgers as well as technical implementation. The Risk Controlling department values financial instruments, while the Credit department values general credit risks. This information is followed up on in accordance with the process for the preparation of financial statements. The relevant responsibilities are defined in the organisational manual. Job descriptions have been specified for all of the employees entrusted with the accounting process. They are assigned to the Back Office. The accounting process is documented in a form which expert third parties are able to follow.

The control system of Dexia Kommunalbank Deutschland consists of organisational arrangements and integrated IT-based controls. As well as these IT-based controls, the Bank has also installed further regular and ad hoc control procedures.

Dexia Kommunalbank Deutschland uses the software SAP ERP and SAP-compatible modules as an integrated Bank-wide solution. This ensures an uninterrupted flow of data and largely avoids transfers to other IT applications or manual interference. A competence-based access and authorisation concept establishes controls so as to prevent unauthorised interference with the accounting process. In addition, the functions for registration of the transactions of the divisions involved in the accounting process are clearly segregated from one another. The market departments enter transactions in the subsidiary ledger, while the Back Office subsequently reviews and authorises these transactions in accordance with the dual control principle (deal certainty policy). Further interim and final results following processing of the inputted data are analysed by means of checks against time-series analyses and target/actual comparisons, their plausibility is reviewed by means of close consultation between Risk Controlling and Accounting and, where appropriate, these results are assessed on a case-by-case basis.

The Accounting department is integrated in the new products process. This ensures rule-compliant and proper accounting for new, non-routine business transactions.

Internal Audit monitors the functional capacity of the accounting-related internal control and risk management system by means of regular process-independent audits, with changing audit focuses.

The management information system provides the management with timely reporting in the form of monthly financial statements under commercial law. The Management Board provides the Supervisory Board and its committees with regular reports, at least once per quarter, on the Bank's current business development. It also provides prompt information in case of specific events.

Berlin, March 13, 2017

Dexia Kommunalbank Deutschland AG

The Management Board

Munsberg **Fritsch**

ANNUAL FINANCIAL STATEMENTS 2016 OF DEXIA KOMMUNALBANK DEUTSCHLAND AG

ANNUAL BALANCE SHEET OF DEXIA KOMMUNALBANK DEUTSCHLAND AG AS OF DECEMBER 31, 2016

24 Assets

	in EUR	in EUR	31.12.2016 in EUR	31.12.2015 in KEUR
1. Cash reserve assets				
a) Cash on hand		861.06		2
b) Balances with central banks		246,055,805.52		60,466
of which: Deutsche Bundesbank	246,055,805.52			(60,466)
c) Balances with post office giro institutions		0.00	246,056,666.58	0
2. Debt securities of public sector entities and bills permitted for funding at central banks				
a) Treasury bills and non-interest-bearing Treasury financing papers and similar debt securities issued by public sector entities		0.00		0
of which: eligible for refinancing at Deutsche Bundesbank	0.00			0
b) Bills		0.00	0.00	0
3. Loans and advances to banks				
a) Mortgage loans		0.00		0
b) Loans to public sector entities		351,955,410.15		533,144
c) Other loans and advances		5,824,463,037.88	6,176,418,448.03	5,694,492
of which: due daily	5,079,109,095.44			(4,594,931)
collateralised by securities	0.00			(0)
4. Loans and advances to non-bank customers				
a) Mortgage loans		37,520,720.01		40,597
b) Loans to public sector entities		14,158,961,286.57		15,197,067
c) Other loans and advances		187,692,421.51	14,384,174,428.09	232,057
of which: collateralised by securities	0.00			(0)
5. Debt securities and other fixed income securities				
a) Money market securities				
aa) from public sector issuers	0.00			0
of which: eligible as collateral at Deutsche Bundesbank	0.00			(0)
ab) from other issuers	0.00			0
of which: eligible as collateral at Deutsche Bundesbank	0.00	0.00		(0)
b) Bonds and debt securities				
ba) from public sector issuers	5,942,750,323.82			7,000,752
of which: eligible as collateral at Deutsche Bundesbank	4,451,527,859.62			(4,947,053)
bb) from other issuers	1,802,002,224.07	7,744,752,547.89		2,340,672
of which: eligible as collateral at Deutsche Bundesbank	976,411,183.79			(1,503,431)
c) Own debt securities		5,450,563.07	7,750,203,110.96	11,574
Nominal amount	5,419,000.00			(11,350)
6. Shares and other non-fixed income securities			0.00	0
6a. Trading portfolio			0.00	0
7. Equity investments			0.00	0
of which: in banks	0.00			(0)
of which: in financial services institutions	0.00			(0)
8. Shares in affiliated companies			0.00	0
of which: in banks	0.00			(0)
of which: in financial services institutions	0.00			(0)
9. Trust assets			0.00	0
of which: trust loans	0.00			(0)
10. Equalisation claims against the public sector. including debt securities resulting from their conversionh			0.00	0
11. Intangible assets				
a) Self-generated industrial property rights and similar rights and assets		0.00		0
b) Licences. industrial property rights and similar acquired for consideration Rights and assets and licences to such rights and assets		281,541.01		156
c) Goodwill		0.00		0
d) Advance payments to suppliers		0.00	281,541.01	0
12. Property, plant and equipment			4,653,528.03	4,970
13. Capital called in but not yet paid in			0.00	0
14. Other assets			2,641,179.43	8,401
15. Prepayments				
a) From issuing and lending business		174,429,120.24		194,157
b) Other		70,927,935.38	245,357,055.62	76,852
16. Deferred tax assets			0.00	0
17. Surplus from offsetting			0.00	0
18. Deficit not covered by equity			0.00	0
Total assets			**28,809,785,957.75**	**31,395,360**

25 Equity and liabilities

	in EUR	in EUR	31.12.2016 in EUR	31.12.2015 in KEUR
1. Liabilities to banks				
a) Registered Mortgage Pfandbriefe issued		0.00		0
b) Registered Public Pfandbriefe issued		381,786,139.65		526,734
c) Other liabilities		4,301,906,478.09	4,683,692,617.74	4,329,013
of which: due daily	893,745,526.55			(873,917)
handed over to the lender as collateral for loans taken out: registered Mortgage Pfandbriefe	0.00			(0)
and registered Public Pfandbriefe	0.00			(0)
2. Liabilities to non-bank customers				
a) Registered Mortgage Pfandbriefe issued		0.00		0
b) Registered Public Pfandbriefe issued		13,085,052,105.57		14,354,739
c) Savings deposits				
ca) with an agreed notice period of three months	0.00			0
cb) with an agreed notice period of more than three months	0.00	0.00		0
d) Other liabilities		5,311,236,044.97	18,396,288,150.54	6,104,004
of which: due daily	1,052,719,816.78			(1,347,979)
handed over to the lender as collateral for loans taken out: registered Mortgage Pfandbriefe	0.00			(0)
and registered Public Pfandbriefe	0.00			(0)
3. Securitised liabilities				
a) Debt securities issued				
aa) Mortgage Pfandbriefe	0.00			0
ab) Public Pfandbriefe	4,498,421,416.89			4,797,143
ac) other debt securities	30,465,901.36	4,528,887,318.25		30,465
b) Other securitised liabilities		0.00	4,528,887,318.25	0
of which: money market securities	0.00			(0)
3a. Trading portfolio			0.00	0
4. Trust liabilities			0.00	0
of which: trust loans	0.00			(0)
5. Other liabilities			283,848,513.80	276,283
6. Deferred income				
a) From issuing and lending business		13,647,648.01		16,151
b) Other		163,498,002.80	177,145,650.81	187,972
6a. Deferred tax liabilities			0.00	0
7. Accruals				
a) Accruals for pensions and similar obligations		0.00		0
b) Tax accruals		276,801.42		277
c) Other accruals		12,783,085.27	13,059,886.69	5,496
8.			0.00	0
9. Subordinated liabilities			20,000,000.00	60,000
10. Profit participation rights capital			43,897,260.85	49,338
of which: due in less than two years	43,897,260.85			(22,371)
11. Fund for general banking risks			0.00	0
12. Equity				
a) Called-in capital				
Subscribed capital	432,500,000.00			432,500
less outstanding deposits not called in	0.00	432,500,000.00		0
b) Capital reserve		348,684,911.98		348,685
c) Revenue reserves				0
ca) legal reserve	0.00			0
cb) reserve for shares in a controlling undertaking or an undertaking with a majority interest	0.00			0
cc) statutory reserves	0.00			0
cd) other revenue reserves	50,702,270.07	50,702,270.07		50,702
d) Accumulated losses		–168,920,622.98	662,966,559.07	–174,142
Total equity and liabilities			**28,809,785,957.75**	**31,395,360**
1. Contingent liabilities				
a) Contingent liabilities from rediscounted bills		0.00		0
b) Liabilities from guarantees and warranty agreements		43,051,797.79		47,333
c) Liability from the provision of collateral for third-party liabilities		0.00	43,051,797.79	0
2. Other obligations				
a) Repurchase obligations resulting from non-genuine repurchase transactions		0.00		0
b) Placement and underwriting commitments		0.00		0
c) Irrevocable lending commitments		–	–	8,077

PROFIT AND LOSS ACCOUNT OF DEXIA KOMMUNALBANK DEUTSCHLAND AG FOR THE PERIOD FROM JANUARY 1 TO DECEMBER 31, 2016

26 **Expenses**

			01.01.–31.12.2016	01.01.–31.12.2015
	in EUR	in EUR	in EUR	in KEUR
1. Interest expense			2,224,195,961.11	2,229,516
2. Commission expenses			2,676,382.81	3,117
3. Net expense for trading portfolio			0.00	0
4. General administrative expenses				
a) Personnel expenses				
aa) wages and salaries	6,014,024.99			5,856
ab) social security contributions and expenses for old-age pensions and support	1,028,027.53	7,042,052.52		979
of which: for old-age pensions	180,875.10			(172)
b) Other administrative expenses		27,114,740.08	34,156,792.60	28,316
of which: annual contribution to restructuring fund	13,909,144.57			(15,805)
5. Depreciation, amortisation and valuation adjustments on intangible assets and property, plant and equipment			454,272.81	453
6. Other operating expenses			8,306.47	8
7. Depreciation, amortisation and valuation adjustments on receivables and specific types of securities and allocations to accruals in lending business			–	50,761
8. Depreciation, amortisation and valuation adjustments on equity investments, shares in affiliated companies and securities treated as fixed assets			–	91,510
9. Expenses from assumption of losses			0.00	0
10.			0.00	0
11. Extraordinary expenses			0.00	0
12. Taxes on income and earnings			0.00	0
13. Other taxes not shown under Item 6n			15,148.72	15
14. Profits transferred under a profit pool, a profit transfer agreement or a partial profit transfer agreemente			0.00	0
15. Net income for the year			0.00	0
Total			**2,261,506,864.52**	**2,410,531**

27 Income

	in EUR	in EUR	01.01.–31.12.2016 in EUR	01.01.–31.12.2015 in KEUR
1. Interest income from				
a) Loan and money market business		1,861,150,306.84		1,982,628
b) Fixed income securities and book-entry securities		295,616,215.05	2,156,766,521.89	327,696
2. Current income from				
a) Shares and other non-fixed income securities		0.00		0
b) Equity investments		0.00		0
c) Shares in affiliated companies		0.00	0.00	0
3. Income from profit pools, profit transfer agreements or partial profit transfer agreements			0.00	0
4. Commission income			522,924.18	473
5. Net income from trading portfolio			0.00	0
6. Income from write-ups of receivables and specific types of securities and from the release of accruals in lending business			32,815,825.20	0
7. Income from write-ups of equity investments, shares in affiliated companies and securities treated as fixed assets			71,080,618.99	–
8. Other operating income			101,021.27	259
9.			0.00	0
10. Extraordinary income			0.00	0
11. Income from assumption of losses			0.00	0
12. Net loss for the year			219,952.99	99,475
Total			**2,261,506,864.52**	**2,410,531**
1. Net income/net loss for the year			–219,952.99	–99,475
2. Profit carryforward/loss carryforward from previous year			–174,141,801.86	–84,113
			–174,361,754.85	–183,587
3. Capital reserve drawings			0.00	0
			–174,361,754.85	–183,587
4. Revenue reserves drawings				
a) from the legal reserve		0.00		
b) from the reserve for shares in a controlling undertaking or an undertaking with a majority interest		0.00		
c) from statutory reserves		0.00		
d) from other revenue reserves		0.00	0.00	0
			–174,361,754.85	–183,587
5. Drawing on profit participation rights capital			5,441,131.87	9,446
			–168,920,622.98	–174,141
6. Allocations to revenue reserves				
a) to the legal reserve				
b) to the reserve for shares in a controlling undertaking or an undertaking with a majority interest				
c) to statutory reserves				
d) to other revenue reserves			0.00	0
			–168,920,622.98	–174,141
7. Replenishment of profit participation rights capital			0.00	0
Accumulated losses			**–168,920,622.98**	**–174,141**

STATEMENT OF CHANGES IN EQUITY

28 Change in equity

in EUR million	Subscribed capital	Capital reserves	Revenue reserves	Net income for the year/accumulated losses	Equity
As of December 31, 2014	**432.5**	**348.7**	**50.7**	**–84.1**	**747.8**
Issuance of shares	0.0	0.0	0.0	0.0	0.0
Paid dividends	0.0	0.0	0.0	0.0	0.0
Other changes	0.0	0.0	0.0	0.0	0.0
Net income/net loss for the year	0.0	0.0	0.0	–99.5	–99.5
Drawing on profit participation rights capital	0.0	0.0	0.0	9.4	9.4
As of December 31, 2015	**432.5**	**348.7**	**50.7**	**–174.1**	**657.7**
Issuance of shares	0.0	0.0	0.0	0.0	0.0
Paid dividends	0.0	0.0	0.0	0.0	0.0
Other changes	0.0	0.0	0.0	0.0	0.0
Net income/net loss for the year	0.0	0.0	0.0	–0.2	–0.2
Drawing on profit participation rights capital	0.0	0.0	0.0	5.4	5.4
As of December 31, 2016	**432.5**	**348.7**	**50.7**	**–168.9**	**663.0**

CASH FLOW STATEMENT

29 Cash flow statement

in EUR million	2016	2015
Profit/loss for the period	**–0.2**	**–99.5**
Non-cash items from operating activity included in profit/loss for the period		
Depreciation, amortisation, valuation adjustments and write-ups on receivables, property, plant and equipment and financial assets	–110.9	155.4
Increase/decrease in accruals	7.3	1.1
Other non-cash expenses/income	7.9	0.0
Profit/loss from disposal of financial assets and property, plant and equipment	0.1	–0.3
Other adjustments	67.4	–80.8
Subtotal	**–28.5**	**–24.1**
Changes in assets and liabilities from current operations		
Loans and advances to non-bank customers	1,117.3	1,041.4
Loans and advances to banks	–75.0	–387.9
Securities (if not financial assets)	532.6	210.6
Other assets from current operations	–5.8	–10.6
Liabilities to non-bank customers	–2,018.8	–1,7
Liabilities to banks	–126.6	–4,963.2
Securitised liabilities	–289.4	–230.8
Other liabilities from current operations	–3.1	15.9
Interest received	2,209.5	2,347.6
Interest paid	–2,281.1	–2,266.8
Income tax payments	0.0	–0.2
Cash flow from current operations	**–968.8**	**–4,269.7**
Cash proceeds of disposals of financial assets	1,801.5	5,575.5
Cash proceeds of disposals of property, plant and equipment	0.0	0.0
Payments for investments in financial assets	–606.9	–1,300.1
Payments for investments in property, plant and equipment	–0.3	–0.3
Cash flow from investing activities	**1,194.4**	**4,275.2**
Cash proceeds of capital increases	0.0	0.0
Changes in cash flow due to other capital	–40.0	0.0
Cash flow from financing activities	**–40.0**	**0.0**
Change in cash and cash equivalents	185.6	5.5
Cash and cash equivalents at start of period	60.5	55.0
Cash and cash equivalents at end of period	**246.1**	**60.5**

NOTES

ACCOUNTING, VALUATION AND TRANSLATION PRINCIPLES

The annual financial statements have been prepared in accordance with the relevant provisions of the German Commercial Code, the German Stock Corporation Act and the German Pfandbrief Act as well as the German Regulation on the Accounting of Banks and Financial Services Institutions (Verordnung über die Rechnungslegung der Kreditinstitute und Finanzdienstleistungsinstitute, RechKredV). The annual balance sheet (balance sheet) and the profit and loss account (P&L) have been structured in accordance with the RechKredV forms and include the items required for Pfandbrief banks.

As a rule, the same accounting and valuation methods have been applied in the annual financial statements as of December 31, 2016 as in the annual financial statements as of December 31, 2015.

Assets and liabilities are valued in line with the general valuation provisions laid down in Section 252ff HGB, while complying with the special rules applicable for credit institutions (Section 340ff HGB).

Receivables and other assets are reported at their nominal value plus pro rata interest. The difference between the issue amount and the nominal amount is shown as an accrual or deferral. All discernible individual risks in lending business are accounted for by establishing specific valuation allowances.

The securities holdings included in financial assets are valued according to the diluted lower of cost or market principle. Premium and discount amounts are offset in the net interest income over the securities' period to maturity.

Securities held in the liquidity reserve are valued at the strict lower of cost or market principle – allowing for currency hedging instruments – at the continuously calculated average value or the lower current rate on the balance sheet date, while complying with the write-up requirement. Where liquid prices were not available for securities through external market data providers as of the balance sheet date, securities' fair values have been determined using internal valuation models. These valuation models involve standard discounted cash flow methods. Issuer- and asset class-specific yield curves and risk premiums (credit spreads) are explicitly included.

Where derivative financial instruments with underlying transactions are pooled in a separate valuation unit (micro-hedge) for hedging of interest rate risks, the effectiveness of this hedging relationship is determined both prospectively and retrospectively. This is done in the form of a sensitivity analysis (prospectively) and using the cumulative dollar offset method (retro-spectively). The method for measurement of retrospective effectiveness was changed over from a regression analysis to the cumulative dollar offset method in the previous year. The changeover of the method for measurement of effectiveness has not had any effect on the separate valuation units. In accordance with Section 254 HGB, opposite changes in the values of the underlying transaction and the hedge transaction are not considered (net hedge presentation method). Further changes in value are subject to the principle of imparity regarding the establishment of accruals, while complying with the write-up requirement.

The net interest income and expense for the swap transactions hedged in separate valuation units are offset against the net interest income and expense for each hedged position. Net interest income for the specific overall valuation unit is thus reported in the relevant item of the profit and loss account. Interest expense in the amount of EUR 50.2 million (previous year: EUR 60.2 million) was offset against the net interest income with a volume of EUR 0.5 million (EUR 2.2 million) in the year under review.

As a rule, close-out netting payments are entered in net interest income. In case of the simultaneous disposal or premature repayment of an underlying transaction within the scope of a close economic relationship, the netting payments are offset against the disposal or repayment amount within the framework of risk provisioning.

Intangible assets and property, plant and equipment are recognised in accordance with the period of their useful life at historical cost less scheduled straight-line depreciation and amortisation. As well as scheduled depreciation and amortisation, the simplification rule under Section 6 (2a) of the German Income Tax Act (Einkommensteuergesetz, EStG) has been used for low-value assets.

Deferred taxes are calculated pursuant to Section 274 HGB in accordance with the balance sheet item-oriented temporary concept, as a comparison between the carrying value according to the commercial value sheet and the tax balance sheet. The balance-sheet option for recognition of deferred tax assets is not used.

The securities transferred in connection with genuine repurchase transactions are accounted for and valued according to their originally assigned category, including the economic outcomes. At the same time, a liability is carried in the value of the agreed amount which is received for the transfer. The difference between the agreed repurchase amount and the amount received is allocated to the accrued and deferred items and is included in net interest income pro rata temporis. Securities purchased under agreements to resell are not shown in the balance sheet. The amount paid for the assumed securities is recognised as a claim against the pledger. The markups and markdowns on the repurchase transactions are accrued/deferred pro rata temporis over the period to maturity of the repurchase transaction.

Liabilities are carried at their settlement value plus pro rata interest. The difference between the nominal amount and the issue amount is allocated to the accrued and deferred items. Accruals are established for taxes, contingent liabilities and contingent losses from pending transactions on the basis of the settlement value deemed necessary according to a prudent commercial assessment.

Pension accruals are recognised in accordance with actuarial principles pursuant to Section 253 (2) HGB in conjunction with the German Regulation on the Discounting of Provisions (Rückstellungsabzinsungsverordnung, RückAbzinsV). The 2005 G mortality tables prepared by Prof. Klaus Heubeck are used for the purpose of the calculation, with an actuarial interest rate of 4.01% p.a. The pension commitment is covered by means of an appropriate employer's pension liability insurance policy. The relevant amounts are offset in accordance with Section 246 (2) Clause 2 HGB. The actual assumptions for the salary trend, fluctuation and the pension trend were not relevant, since the pension commitments (capital commitments) were fulfilled through the conversion of salary entitlements into pension entitlements, in the form of a one-off payment. The difference between the carrying amount for pension accruals calculated according to the average market interest rate over the past ten financial years and the carrying amount for accruals determined according to the average market interest rate over the past seven financial years amounts to EUR 0.0 million in the financial year 2016.

Received and paid upfront payments from swaps are reported under deferred income and prepayments and recognised pro rata temporis in the net interest income and expense.

Foreign-currency assets and liabilities and off-balance sheet transactions are valued on the basis of Section 256a HGB in conjunction with Section 340h HGB. Foreign-currency amounts are translated at the spot exchange middle rate as of the balance sheet date. The same applies for the valuation of additions. All foreign-currency items are exchange rate-hedged positions for which no exchange risk applies (special coverage). Expenses and income from currency translation are recognised net in other operating profit/loss.

The Bank implements a loss-free valuation of its banking book on the basis of the opinion of August 30, 2012 issued by the banking committee of the Institute of Public Auditors in Germany (Institut der Wirtschaftsprüfer in Deutschland e.V., IDW RS BFA 3). This banking book comprises all balance-sheet and off-balance sheet interest-driven financial transactions out-side the trading portfolio (including securities held in the liquidity reserve and securities held in the banking book). The Bank does not maintain a trading book. The banking book is valued by means of a periodic (P&L-oriented) assessment, including appropriate future administrative and risk costs. The risk costs are derived from the regulatory requirements for reporting (standard risk costs). Future funding through fixed-term deposits, borrowings from the ECB and repurchase transactions is assumed on the basis of the current funding mix. Amount and maturity mismatches are notionally closed out using matching money and capital market interest rates as of the reporting date, while considering the financing effect of equity capital. In case of excess liability, this is considered in accordance with the principle of imparity – by way of an accrual for contingent losses – and recognised in income under risk provisioning.

NOTES ON THE BALANCE SHEET

Assets transferred as collateral

Liabilities to banks are secured within the scope of open market operations and genuine repurchase transactions, by means of securities and loans with a volume of EUR 813.8 million.

Securities eligible for stock market listing

Securities with a nominal volume of EUR 6,620.5 million are valued as fixed assets, since they do not serve as a liquidity reserve and in some cases serve as cover for Public Pfandbriefe issued. Investment securities with a carrying amount of EUR 708.2 million and a fair value of EUR 667.1 million have not been written down to the lower of cost or market value. No permanent impairment in value is applicable, since this relates to price fluctuations and it is expected that these fluctuations will be made up for prior to the maturity of the security in question and that these securities can be held to maturity. › 33

Development of fixed assets

Property, plant and equipment comprise land and buildings used for the Bank's own activities, in the amount of EUR 3.9 million, and operating and office equipment in the amount of EUR 0.7 million. › 34

Other assets

Other assets include as a key position irrevocable payment commitments in connection with the bank levy (EUR 2.5 million).

Deferred tax assets

Different carrying values for debt securities and other fixed income securities and for loans and accruals give rise to temporary differences between the commercial and tax balance sheet and thus deferred taxes. These deferred tax assets are valued at a tax rate of 30.2%. Exercising the option under Section 274 (1) Clause 2 HGB, Dexia Kommunalbank Deutschland has waived recognition of this amount, since the prospective settlement of these differences is not foreseeable with a sufficient degree of probability.

30 Maturity breakdown by residual maturity

in EUR million	Loans and advances to banks	Loans and advances to non-bank customers	Liabilities to banks	Liabilities to non-bank customers
Up to 3 months	5,277.2	99.9	2,558.0	3,268.4
More than 3 months and up to 1 year	115.7	816.8	1,251.5	2,164.3
More than 1 year and up to 5 years	165.2	2,163.9	190.4	3,692.6
More than 5 years	130.5	11,072.5	166.5	8,974.8
Interest	487.8	231.1	517.3	296.2
Total	**6,176.4**	**14,384.2**	**4,683.7**	**18,396.3**

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in EUR million	Maturing in following year
Debt securities and other fixed income securities	**585.8**
Debt securities issued	**1,011.7**

32 Loans and advances to/liabilities to affiliated companies/equity investments

in EUR million	Total	Of which affiliated companies	Of which companies in which an equity interest is held
Loans and advances to banks	**6,176.4**	1,332.1*	–
Loans and advances to non-bank customers	**14,384.2**	–	–
Debt securities and other fixed income securities	**7,750.2**	53.9	–
Liabilities to banks	**4,683.7**	2,211.5*	–
Liabilities to non-bank customers	**18,396.3**	–	–
Securitised liabilities	**4,528.9**	–	–
Subordinated liabilities	**20.0**	20.0*	–

* exclusively comprises non-securitised receivables/liabilities. .

33 Securities eligible for stock market listing

in EUR million	Total	Eligible for stock market listing	Stock market-listed	Non-stock market-listed	Amount of securities eligible for stock market listing and not valued according to the lower of cost or market principle
Debt securities and other fixed income securities	**7,750.2**	7,750.2	6,270.1	1,480.2	708.2

34 Fixed assets movement schedule

	Historical cost				Accumulated depreciation/amortisation				Residual book value	
in EUR million	01.01.2016	Additions in financial year	Disposals in financial year	31.12.2016	01.01.2016	Additions in financial year	Disposals in financial year	31.12.2016	01.01.2016	31.12.2016
Intangible assets	23.0	0.2	0.0	23.2	−22.9	−0.1	0.0	−23.0	0.2	**0.3**
Property, plant and equipment	16.2	0.1	−0.8	15.5	−11.2	−0.4	0.8	−10.9	5.0	**4.7**
Investment securities	7,770.0	Net changes		6,604.5	91.8	Net changes		0.0	7,678.2	**6,604.5**

Accrued and deferred items

35 Prepayments

in EUR million	31.12.2016	31.12.2015
Issuing discount on debt securities	8.2	10.3
Premium on receivables	166.2	183.8
Total amount from issuing and lending business	**174.4**	**194.2**

36 Deferred income

in EUR million	31.12.2016	31.12.2015
Discount on receivables	8.2	9.1
Premium on debt securities	5.5	7.0
Total amount from issuing and lending business	**13.6**	**16.2**

Foreign-currency receivables/liabilities

The Bank's assets include foreign-currency items with an equivalent value of EUR 1,493.8 million, while its liabilities include foreign-currency items with an equivalent value of EUR 25.1 million.

Separate valuation units

The Bank has established separate valuation units in the form of micro-hedge relationships exclusively for hedging of interest rate risks and has included the following items and transactions in these valuation units. › 37 Since interest-rate swaps have been entered into, these underlying transactions are converted into variable transactions. The separate valuation unit is established on the basis of almost complete congruency between the key parameters for the underlying transaction and the hedge transaction. Since the changes in value for the corresponding transactions almost entirely offset one another over the period to maturity, an accrual need only be established in the value of the non-hedged portion. As of the balance sheet date, this amounts to EUR 9.0 million. For monitoring of the effectiveness of the micro-hedge relationships established, within the scope of the non-interest rate-structured products sensitivity analyses and the cumulative dollar offset method are applied. The changes in value for the underlying transaction and the hedge transaction are compared with one another here.

Other liabilities

Other liabilities mainly comprise unrealised losses on specially covered forward exchange transactions (EUR 275.3 million).

Pension accruals

Pursuant to Section 246 (2) Clause 2 HGB, pension accruals in the amount of EUR 0.0 million have been offset against claims under employer's pension liability insurance policies with a volume of EUR 0.0 million.

Subordinated liabilities

In the event of the Bank's bankruptcy or liquidation, subordinated liabilities are only reimbursable upon satisfaction of all of the non-junior creditors. Premature repayment is excluded. Interest expense for all subordinated liabilities amounts to EUR 2.3 million.

Table › 38 shows the subordinated liabilities which exceed 10% of the total amount reported.

38 Subordinated liabilities

in EUR million	Interest rate as %	Maturity
10.0	4.7	30.05.2018
10.0	4.7	26.09.2018

Of the portfolio with a volume of EUR 20.0 million, EUR 6.0 million must be counted towards own funds, as Tier 2 capital, due to the transitional provisions laid down in Article 484 (5) of the CRR. The terms for subordinated promissory note loans apply. Conversion into capital or another form of debt is not contractually stipulated.

Profit participation rights capital

After a reduction for the repayment claims, the profit participation rights capital consists of bearer profit participation rights in the amount of EUR 17.2 million and registered profit participation rights in the amount of EUR 26.7 million. Of this figure, as of the balance sheet date EUR 4.9 million must

37 Separate valuation units

in EUR million	Underlying transaction	Type of separate valuation unit	Secured risk	Hedged risk
Assets	1,003.8	Micro-hedge	Interest rate risk	292.6

be counted towards own funds, as Tier 2 capital, due to the transitional provisions laid down in Article 484 (5) of the CRR.

On account of its terms of issue, in case of accumulated losses the profit participation rights capital will not attract interest. Accordingly, no expenses were incurred in the past financial year. The participation certificate creditors' share of the losses is determined according to the various participation right terms, on the basis of different calculation methods. The registered participation certificate holders' share of the net loss for the year is calculated according to the ratio of the repayment claim to the total amount of the subscribed capital, the reserves and the overall profit participation rights capital. For the bearer participation certificates, the share of the accumulated losses, including the loss carryforward, is calculated according to the ratio of the respective repayment claims to the total equity according to Section 10 KWG. This calculation is based on the nominal capital amounts and, for recognition of the profit participation rights capital, the amounts less the previous year's loss share. The net loss for the year/the accumulated losses were determined before the loss share was included. The ratios as of the balance sheet date, December 31, 2016, were applied for the calculation. The repayment claims of participation certificate creditors decreased by EUR 5.4 million to EUR 43.9 million in the financial year 2016. › 39

Subscribed capital
The subscribed capital amounts to EUR 432.5 million. It is divided up into 432,500,000 registered shares with restricted transferability, each with a value of EUR 1.00.

Capital/revenue reserves
The capital reserve amounts to EUR 348.7 million. At the end of 2016, the revenue reserves amount to EUR 50.7 million.

Freely available reserves
Accumulated losses as of December 31, 2016 amount to EUR – 168.9 million. No bans on distributions applied in the year under review either by law, according to the Bank's articles of association or pursuant to its company agreement.

Repurchase transactions
The carrying amount of the assets sold under agreements to repurchase is EUR 427.8 million.

NOTES ON THE PROFIT AND LOSS ACCOUNT

Negative interest
The net interest income includes negative interest on claims in the amount of EUR 35.5 million (previous year: EUR 2.5 million), while interest expense includes negative interest on liabilities in the amount of EUR 45.8 million (previous year: EUR 6.3 million).

Remuneration of the members of the executive bodies
In the year under review, the total remuneration of the members of the Management Board amounted to EUR 0.7 million. The members of the Supervisory Board were paid EUR 0.05 million in the financial year 2016.

Auditors' fees
Table › 40 shows the auditors' fees included in the other administrative expenses.

40 Auditors' fees

in EUR million	
Audit services	0.4
Other assurance services	0.0
Tax advisory services	0.0
Other services	0.0
Total	**0.4**

Risk provisioning
The full compensation option is exercised for risk provisioning (Section 340f (3) HGB). The balance shown results from offsetting the expense item "Depreciation, amortisation and valuation adjustments on receivables and specific types of securities and allocations to accruals in lending business" against the income item "Income from write-ups of receivables

39 Profit participation rights capital

	Interest rate	Capital repayment	Repayment claim after 2016 loss allocation	Repayment claim after 2015 loss allocation	Repayment claim before 2011 loss allocation
	as %		in EUR million	in EUR million	in EUR million
Year of issue 2006	5.1	2017	7.8	7.8	10.0
Year of issue 2006	5.1	2017	3.1	3.1	4.0
Year of issue 2006	4.9	2017	8.7	11.4	22.0
Year of issue 2007	5.6	2018	7.8	7.8	10.0
Year of issue 2007	5.6	2018	7.8	7.8	10.0
Year of issue 2007	5.6	2018	8.6	11.3	21.8
Total			**43.9**	**49.3**	**77.8**

and specific types of securities and from the release of accruals in lending business".

Depreciation, amortisation and valuation adjustments on equity investments, shares in affiliated companies and securities treated as fixed assets

The Bank exercises the option provided for in Section 340c (2) HGB of fully compensating for "Depreciation, amortisation and valuation adjustments on equity investments, shares in affiliated companies and securities treated as fixed assets" by means of "Income from write-ups on equity investments, shares in affiliated companies and securities treated as fixed assets".

Extraordinary expense and income items

Interest expense includes an amount of EUR 181.6 million and interest income an amount of EUR 75.0 million from the early termination of derivatives. The other administrative expenses include expenses with a volume of EUR 13.9 million resulting from the bank levy. Risk provisioning includes write-ups on the Bank's former Heta commitment in the amount of EUR 68.5 million, while income from write-ups of equity investments, shares in affiliated companies and securities treated as fixed assets include write-ups on the Bank's former Heta commitment with a volume of EUR 71.2 million.

OTHER DISCLOSURES

Supplementary disclosures concerning the cash flow statement

The cash flow statement has been prepared on the basis of the German accounting standard No. 21. It shows the change in cash and cash equivalents in terms of cash flows from operating, investing and financing activities. Cash flows are assigned to operating activities in accordance with the makeup of the operating result. Cash flows from investing activities mainly comprise cash flows from financial assets and from financing activities. The latter mainly derive from transactions with the Bank's shareholder. Cash and cash equivalents consist of cash on hand as well as balances with central banks. No changes were made to the relevant definition.

Contingent liabilities and other obligations

Contingent liabilities and other obligations comprise in sub-item 1b) other guarantees in their full amount.

The liabilities resulting from guarantees and contracts of indemnity shown as off-balance sheet items form part of our core lending business and are subject to the same conservative valuation criteria as all other claims involving credit risks. At the present time, no default risks are discernible which must be carried as liabilities in the balance sheet.

As of December 31, 2016, the irrevocable payment commitment submitted within the scope of the bank levy amounts to EUR 2.5 million. At the present time, this is not expected to be called upon.

Interest rate and foreign exchange forward transactions

As of the balance sheet date, the Bank has entered into the following interest rate and foreign exchange forward transactions which have not yet been settled and are not held for trading purposes: interest rate swaps, cross-currency interest rate swaps, promissory note loans with a creditor's right of termination, Pfandbrief issues with a debtor's right of termination. All of these cases involve OTC products. › 41

In each case, the Bank's swap partners are groups of credit institutions in OECD countries which are suitable credit institutions within the meaning of Section 4 (1) Clause 2 No. 3 PfandBG. The credit risk for the interest rate swaps is determined according to the mark-to-market method.

The derivatives' net negative fair values in the amount of EUR –3.8 billion (excluding pro rata interest) contrast with interest-driven hidden reserves of more than EUR 3.8 billion in the carrying amounts for the balance sheet items "Loans and advances to banks", "Loans and advances to non-bank customers", "Debt securities and other fixed income securities", "Liabilities to banks", "Liabilities to non-bank customers" and "Securitised liabilities".

The present values of these derivatives are calculated by means of zero bond discounting factors as well as the future cash flows, using the fair value method. The arbitrage-free zero bond discounting factors are calculated on each working day on the basis of the current swap mid yield curve. The overnight index swap curve is used for discounting.

41 Volume in derivatives business after residual maturities

	Nominal volume				Fair values		
in EUR million	Up to 1 year	1–5 years	Longer than 5 years	Total	Positive	Negative	Total
Interest-rate swaps	4,645.3	14,117.9	31,391.4	50,154.7	5,851.5	–8,885.2	–3,033.8
Cross-currency swaps	85.9	45.8	1,062.0	1,193.7	7.1	–812.1	–805.0
Total	**4,731.3**	**14,163.7**	**32,453.5**	**51,348.4**	**5,858.5**	**–9,697.3**	**–3,838.8**

The Bank does not enter into trading transactions with derivative products.

Other loans and advances to banks/non-bank customers include pro rata interest from derivative transactions in the amount of EUR 498.2 million and other liabilities to banks/non-bank customers pro rata interest from derivative transactions in the amount of EUR 513.1 million. Netting payments made are shown under "Prepayments" in the amount of EUR 66.3 million and netting payments received in the amount of EUR 163.0 million under "Deferred income". "Other liabilities" include a balancing item from the foreign-currency valuation of swaps with a volume of EUR 275.3 million.

Cover calculation

As on the reporting date for the previous year, no payments on the cover assets for Public Pfandbriefe are in arrears by more than 90 days. › 42 43 44 45 46 47 48

Loans to members of the Management Board or the Supervisory Board

As of the balance sheet date, no loans and advances had been granted to members of the Management Board and the Supervisory Board.

Number of employees

In the past financial year, the Bank had 81 employees on average. 40 of these employees were covered by a wage agreement, while 41 were not covered by a wage agreement. As of the end of 2016, the Bank had 81 (previous year: 78) employees.

Report on events after the balance sheet date

In relation to the Bank's existing legal risks, in February 2017 the court of appeal ruled in favour of the Bank in a legal dispute. This case involves a loan whose rate of interest is tied to the development of the exchange rate of the Swiss franc against the euro. The opposing party has initiated appeal proceedings on points of law. For full details of the legal risks, please see the Operational risks section.

No significant events occurred following the end of the financial year 2016 which would have altered the Bank's net assets, financial position and results of operations.

General information

Dexia Kommunalbank Deutschland AG, Berlin, is registered in the commercial register held by Local Court in Charlottenburg, No. HRB 36928.

Group membership

Dexia Crédit Local S. A., Paris, holds a 100% equity interest in the Bank. The Bank's parent company prepares annual sub-group accounts (smallest consolidated group) in accordance with the International Financial Reporting Standards, which include Dexia Kommunalbank Deutschland. The annual sub-group accounts are deposited with the commercial register in Paris. Dexia S. A., Brussels, holds a 100% equity interest in Dexia Crédit Local S. A., Paris. Dexia S. A., Brussels, prepares consolidated financial statements (largest consolidated group) in accordance with the International Financial Reporting Standards, which include Dexia Kommunalbank Deutschland. They are deposited with the commercial register in Brussels.

Some of the details which must be disclosed in accordance with Part 8 Articles 435 to 455 of the CRR are provided in the management report. In regard to the further disclosures, please refer to the disclosure report (risk report) issued by the Dexia Group. This report is published on the Dexia Group's website www.dexia.com.

42 Public Pfandbriefe

in EUR million	31.12.2016	31.12.2015
Ordinary cover		
Loans and advances to banks (loans to public sector entities)	343.3	430.1
Loans and advances to non-bank customers (loans to public sector entities)	13,671.6	14,576.5
Debt securities and other fixed income securities	4,578.2	4,913.6
Received as collateral for genuine repurchase transactions	517.4	947.2
Other cover		
Loans and advances to banks (loans to public sector entities)	–	92.1
Debt securities and other fixed income securities	–	–
Total	**19,110.5**	**20,959.5**

43 Cover assets in accordance with Section 20 (2) No. 2 PfandBG

	Nominal value	
in EUR million	31.12.2016	31.12.2015
Switzerland	–	92.1
Total	**–**	**92.1**

The total amount of the claims under Section 20 (2) No. 2 PfandBG is less than the limits stipulated in Section 20 (2) (details in accordance with Section 28 (1) No. 8 PfandBG). The cover assets in accordance with Section 20 (2) No. 2 PfandBG do not include any claims within the meaning of Article 129 of Regulation (EU) No 575/2013 (covered bonds).

44 Total amount of Pfandbriefe outstanding

		Nominal value		Present value		Risk-adjusted present value	
		31.12.2016	31.12.2015	31.12.2016	31.12.2015	31.12.2016	31.12.2015
Public Pfandbriefe	in EUR million	17,629.2	19,301.6	22,334.9	24,071.9	20,543.1	22,375.3
of which fixed income Pfandbriefe	as %	87.6	87.6	–	–	–	–
Cover pool	in EUR million	19,110.5	20,959.5	26,197.9	28,035.2	23,397.5	25,123.6
of which fixed income cover pool	as %	85.4	84.7	–	–	–	–
of which derivatives	in EUR million	–	–	–	–	–	–
Overcollateralisation	in EUR million	**1,481.3**	**1,657.9**	**3,863.0**	**3,963.3**	**2,854.4**	**2,748.3**

45 Maturity structure of Pfandbriefe outstanding and fixed-interest periods of the cover pool

	Public Pfandbriefe		Cover pool	
in EUR million	31.12.2016	31.12.2015	31.12.2016	31.12.2015
up to 6 months	1,190.9	1,166.5	855.1	675.0
more than 6 months and up to 12 months inclusive	524.8	583.5	1,015.8	576.4
more than 12 months and up to 18 months inclusive	1,328.6	1,170.3	717.4	726.9
more than 18 months and up to 2 years inclusive	195.8	524.8	489.9	1,000.5
more than 2 years and up to 3 years inclusive	1,999.0	1,524.0	749.5	1,165.6
more than 3 years and up to 4 years inclusive	1,295.6	1,999.0	1,055.0	785.3
more than 4 years and up to 5 years inclusive	1,439.1	1,295.0	491.8	1,107.0
more than 5 years and up to 10 years inclusive	4,888.3	4,986.8	4,869.6	3,849.6
more than 10 years	4,767.1	6,051.7	8,866.4	11,073.2
Total	**17,629.2**	**19,301.6**	**19,110.5**	**20,959.5**

46 Receivables serving as cover for Public Pfandbriefe

	Ordinary cover in accordance with Section 20 (1) PfandBG											
	Sum		of which									
			Guarantees due to the promotion of exports		Sovereign		Regional authorities		Local authorities		Other debtors	
in EUR million	31.12.2016	31.12.2015	31.12.2016	31.12.2015	31.12.2016	31.12.2015	31.12.2016	31.12.2015	31.12.2016	31.12.2015	31.12.2016	31.12.2015
Belgium	1,196.3	1,253.5	–	–	–	–	1,196.3	1,253.5	–	–	–	–
Germany	12,967.5	13,616.8	–	3.2	51.1	54.4	8,420.6	8,463.0	4,099.4	4,607.0	396.4	492.4
for which public sector entities liable	197.1	203.9	–	–	–	–	–	–	–	–	197.1	203.9
Finland	23.1	24.7	–	–	–	–	–	–	23.1	24.7	–	–
France	12.0	13.2	–	–	–	–	–	–	12.0	13.2	–	–
Italy	2,452.3	2,095.0	–	–	1,681.2	1,279.2	176.7	191.5	594.4	624.3	–	–
Japan	232.7	663.3	–	–	–	443.6	124.9	118.1	107.8	101.6	–	–
Austria	1,047.4	1,090.8	–	–	65.0	75.2	982.4	1,015.6	–	–	–	–
Poland	–	182.0	–	–	–	182.0	–	–	–	–	–	–
Portugal	522.5	625.0	–	–	422.5	525.0	100.0	100.0	–	–	–	–
Sweden	78.5	81.8	–	–	–	–	–	–	78.5	81.8	–	–
Spain	78.8	578.8	–	–	18.7	18.7	60.1	560.1	–	–	–	–
Hungary	81.7	155.6	–	–	81.7	155.6	–	–	–	–	–	–
USA	226.5	270.7	–	–	–	–	169.8	215.7	56.7	55.0	–	–
EU institutions	87.2	112.2	–	–	–	–	–	–	–	–	87.2	112.2
Other sovereigns/ institutions	104.0	104.0	–	–	–	–	–	–	–	–	104.0	104.0
Total	**19,110.5**	**20,867.4**	**–**	**3.2**	**2,320.2**	**2,733.7**	**11,230.8**	**11,917.5**	**4,971.9**	**5,507.6**	**587.6**	**708.6**

47 Net present value under Section 6 of PfandBarwertV per foreign currency

in EUR million	31.12.2016	31.12.2015
CHF	–	92.9
GBP	120.4	149.2
JPY	1,000.0	1,422.1
NOK	–11.5	–11.1
SEK	82.2	87.8
USD	268.7	317.1

48 Receivables serving as cover for Public Pfandbriefe, by size group

in EUR million	31.12.2016	31.12.2015
Up to and including EUR 10 million	1,070.8	1,190.6
More than EUR 10 million, up to and including EUR 100 million	3,484.3	3,833.5
More than EUR 100 million	14,555.4	15,935.4
Total	**19,110.5**	**20,959.5**

EXECUTIVE BODIES OF THE BANK

SUPERVISORY BOARD

Benoît Debroise
Member of the Management Board of
Dexia S. A. with responsibility for funding and markets
Member of the Management Board of
Dexia Crédit Local S. A. with responsibility
for funding and markets
Executive Vice President of Dexia Crédit Local S. A.
Chairman

Véronique Hugues
Chief Financial Officer and
Member of the Management Board of
Dexia S. A with responsibility for finance
Executive Vice President of Dexia Crédit Local S. A.
Deputy Chairman

Eric Bouthors
Bank employee of
Dexia Kommunalbank Deutschland AG

Isabelle Bouvet
Group Head of Market Risk of
Dexia S. A. and Dexia Crédit Local S. A.
(since November 1, 2016)

Stefanie Gregorius
Bank employee of
Dexia Kommunalbank Deutschland AG

Jürgen Jung
Consultant
(since July 1, 2016)

Dr. Dirk Hoffmann
Lawyer and consultant
(to June 30, 2016)

Claude Piret
Member of the Management Board of
Dexia S. A. with responsibility for asset management
Executive Vice President of Dexia Crédit Local S. A.
(to October 31, 2016)

MANAGEMENT BOARD

Friedrich Munsberg
Member of the Management Board
with responsibility for markets
Chairman

Laurent Fritsch
Member of the Management Board
with responsibility for back office functions

TRUSTEE

Victor von Bothmer
Lawyer

Josef Baiz
Independent consultant
for financial and economic issues
(since November 1, 2016)

Werner Graf
Retired Bundesbank director
(to November 30, 2016)

RESPONSIBILITY STATEMENT

We hereby provide an assurance that, to the best of our knowledge, the annual financial statements provide a true and fair view of the company's net assets, financial position and results of operations, while complying with the principles of orderly accounting. We also provide an assurance that, to the best of our knowledge, the company's business performance – including its business results – and its position have been presented in the management report so as to provide a true and fair view while describing the key risks and opportunities within the meaning of Section 289 (1) Clause 4 HGB.

Berlin, March 13, 2017

Dexia Kommunalbank Deutschland AG

The Management Board

Munsberg **Fritsch**

AUDITOR'S REPORT

We have audited the annual financial statements – consisting of the annual balance sheet, the profit and loss account, the cash flow statement, the statement of changes in equity capital and the notes – including the accounting and the management report for Dexia Kommunalbank Deutschland AG, Berlin, for the financial year from January 1 to December 31, 2016. The Bank's Management Board is responsible for the accounting and for the preparation of the annual financial statements and the management report in accordance with German commercial law provisions and the supplementary provisions of the Bank's articles of association. Our task is to provide an assessment of the annual financial statements – including the accounting – and the management report on the basis of our audit.

We have performed our audit of the annual financial statements in accordance with Section 317 HGB while complying with the German principles of proper auditing drawn up by the Institute of Public Auditors in Germany (Institut der Wirtschaftsprüfer in Deutschland e. V., IDW). These require us to plan and to conduct our audit so as to identify with a sufficient degree of certainty any inaccuracies and infringements which materially affect the picture of the Bank's net assets, financial position and results of operations provided by the annual financial statements – while complying with the principles of orderly accounting – and by the management report. In determining our audit activities, knowledge of the Bank's business activities and its economic and legal environment and likewise expectations of possible errors are considered. Within the scope of our audit, the effectiveness of the accounting-related internal control system and documentation of the disclosures provided in the accounting, the annual financial statements and the management report are mainly assessed on the basis of samples. Our audit includes an assessment of the accounting principles applied and the key evaluations made by the Management Board as well as an appraisal of the overall picture provided by the annual financial statements and the management report. In our view, our audit provides a sufficiently reliable basis for our assessment.

Our audit has not given rise to any objections.

In our assessment based on our audit findings, the annual financial statements of Dexia Kommunalbank Deutschland AG, Berlin, comply with the applicable statutory requirements and the supplementary provisions of its articles of association and provide a true and fair view of the Bank's net assets, financial position and results of operations, while complying with the principles of orderly accounting. The management report is consistent with the annual financial statements, complies with applicable statutory requirements, provides an accurate overall picture of the Bank's position and correctly presents the risks and opportunities associated with its future development.

Berlin, March 14, 2017

DELOITTE GMBH
Wirtschaftsprüfungsgesellschaft

gez. Björn Grüneberg	**gez. Maik Pehla**
Auditor	Auditor

DEXIA
KOMMUNALBANK
DEUTSCHLAND
DKD