Annual Report 2018 (IFRS/Group)

Hamburg Commercial Bank

~~Ready,~~ ~~steady,~~ go!

Annual Report 2018

In 2018, we became the first landesbank to complete a successful privatisation. This entails an in-depth transformation – we are becoming a more efficient, more responsive and more profitable bank with a clear focus on its clients.

"Privatisation is only the start for us. Through a systematic transformation we are becoming a successful private commercial bank."

Stefan Ermisch, Chief Executive Officer

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Group overview

Positive results, solid new business and strong capital ratios. Plus further cuts in administrative costs and the reduction of legacy assets to virtually zero. We can certainly be pleased with our performance in 2018. Above all, with these successes we have created an excellent basis for our future as a private bank.

Income statement (€ million)

Net income before restructuring and privatisation 31.12.2018
(cf. 31.12.2017: -238)

↗ **621**

Net income before taxes 31.12.2018
(cf. 31.12.2017: -453)

↗ **97**

Group net result 31.12.2018
(cf. 31.12.2017: -528)

↗ **77**

Balance sheet (€ billion)

Reported equity 31.12.2018
(cf. 31.12.2017: 4.4)

→ **4.4**

Total assets 31.12.2018
(cf. 31.12.2017: 70.4)

↘ **55.1**

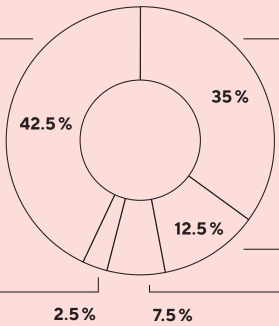
Business volume 31.12.2018
(cf. 31.12.2017: 78.6)

↘ **64.5**

Group structure

Several funds initiated by **Cerberus Capital Management, L.P.**

Promontoria Holding 221 B.V. ↓ **9.89%**	Promontoria Holding 231 B.V. ↓ **13.88%**	Promontoria Holding 233 B.V. ↓ **18.73%**



A fund advised by **J.C. Flowers & Co. LLC**
→ JCF IV Neptun Holdings S.à r.l.

A fund initiated by **GoldenTree Asset Management LLP**
→ GoldenTree Asset Management Lux S.à r.l.

BAWAG P.S.K. Bank für Arbeit und Wirtschaft und Österreichische Postsparkasse Aktiengesellschaft

Centaurus Capital LP
→ Chi Centauri LLC

Capital ratios & RWA

CET1 ratio (%)[1] 31.12.2018
(cf. 31.12.2017: 15.4)

↗ **18.5**

Total capital ratio (%) 31.12.2018
(cf. 31.12.2017: 25.8)

↘ **23.4**

Risk weighted assets (RWA) (€ billion) (cf. 31.12.2017: 26.2)

↘ **22.1**

Employees (computed on full-time equivalent basis)

Total 31.12.2018
(cf. 31.12.2017: 1,926)

↘ **1,716**

Germany 31.12.2018
(cf. 31.12.2017: 1,838)

↘ **1,648**

Abroad 31.12.2018
(cf. 31.12.2017: 88)

↘ **68**

[1] Pursuant to same-period calculation under the rules of the Capital Requirements Regulation (CRR).

New business in 2018 (excl. syndication)

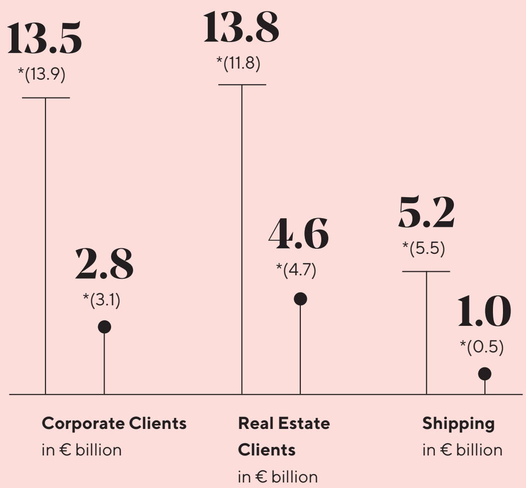
The Bank recorded a positive development in its client business: new business including syndications reached a volume of € 8.4 billion (2017: € 8.6 bn), driven by Real Estate Clients and by the Renewable Energies, Infrastructure and Shipping segments. In the traditional Corporate Clients business, the Bank has deliberately curtailed its new exposures due to the competition-related pressure on margins.

The foundations of Hamburg Commercial Bank

— Segment assets (EAD) 2018 (incl. Syndication)

● New business 2018

*(cf. 31.12.2017)



Administrative expenses 31.12.2018 (€ billion)
(cf. 31.12.2017: - 481)

↗ **-402**

At the start of a fundamental transformation spanning several years

Ladies and Gentlemen,

For our Bank the year 2018 was as decisive as it was groundbreaking: We are the first landesbank to have successfully privatised. This is an achievement of which we can certainly be proud. We would like to thank our colleagues for their great commitment and the federal states of Hamburg and Schleswig-Holstein, which did pioneering work through the sale of HSH Nordbank that was closed on 28 November 2018.

For the Bank, this privatisation marks the beginning of a completely new era. We now have the opportunity to take Hamburg Commercial Bank to success with our new, internationally experienced shareholders: they are the independent funds of Cerberus Capital Management, L.P., J.C. Flowers & Co. LLC, GoldenTree Asset Management LP as well as an Acquisition Company of Centaurus Capital LP and BAWAG P.S.K. We are at the start of a fundamental transformation spanning several years, during which we will be developing from a moderately profitable landesbank to an appropriately profitable bank in private ownership. In doing so we will increase our profitability substantially and raise the value of the company.

The potential of Hamburg Commercial Bank is also evidenced by the fact that we achieved quite a satisfactory result in 2018, despite all the uncertainties in the wake of privatisation. Net income before taxes came to € 97 million, at € 8.4 billion our new business was roughly at the previous year's level. Our Common Equity Tier 1 ratio stands at more than 18 percent and is clearly in green territory. The non-performing exposure ratio, which measures how many loans are at risk of defaulting, comes to around two percent and meets our target. As expected, non-recurring effects in connection with the privatisation, the transformation and the liabilities side, which needs to be restructured, had a major impact on our income statement.

Even though we have reached an important milestone with privatisation, there is still a considerable way to go. We are only at the beginning of the change. We must make major progress regarding profitability, in particular. We are still a long way off our goals: we are aiming for a cost/income ratio of no more than 40 percent and a return on equity of at least eight percent. These goals are important to us in several respects: we want to generate sustained commercial success, offer our shareholders an appropriate return and be certain of being accepted in the guarantee system of the Association of German Banks. This, in turn, is linked with capital and profitability ratios.

We are making huge changes to increase our profitability. We will streamline our internal structures, increase our speed and continue to reduce our costs systematically. In future, we will invest our capital in Germany and abroad only where it really pays off. At the same time, we are planning to expand our activity by including some more business areas. For example, we will extend commercial real estate finance to France, Austria and the Benelux countries. We also want to carefully expand our international radius when it comes to financing projects in the renewable energy and infrastructure sectors. Above all, what is important to us is that we focus on the client more than ever. We want to distinguish ourselves through our expertise and responsiveness.

The future for Hamburg Commercial Bank starts now – we will shape it with momentum, clarity and consistency.

Yours sincerely,
The Management Board

Nicolas Blanchard is Chief Clients and Products Officer. He has been with the Bank since December 2018 and has responsibility for the client segments.

Stefan Ermisch is the Chief Executive Officer. He joined the Bank as Chief Financial Officer in 2012 and took over as Chief Executive Officer in June 2016.

Oliver Gatzke is the Chief Financial Officer. He has been with the Bank since 2013 and was appointed Chief Financial Officer in July 2016.

Ulrik Lackschewitz is the Chief Risk Officer and Deputy CEO. He has been with the Bank since October 2015.


Hamburg
Commercial
Bank

~~And so~~ forth.

Stefan Ermisch
Chief Executive Officer

What is your assessment of the year 2018?
Stefan Ermisch → The past year was as decisive for our Bank as it was ground-breaking. The signing on 28 February and the closing of our sale on 28 November 2018 achieved something that hasn't been seen in Germany before: the privatisation of a landesbank. We can be proud of this achievement. I would like to thank all my colleagues for their great commitment, as well as our previous owners, the federal states of Hamburg and Schleswig-Holstein. We now have the opportunity to take Hamburg Commercial Bank to success with our new, internationally experienced shareholders: they are the independent funds of Cerberus Capital Management, L.P., J.C. Flowers & Co. LLC, GoldenTree Asset Management LP as well as an Acquisition Company of Centaurus Capital LP and BAWAG P.S.K.

Even though privatisation was a decisive project in 2018 – how was business?
SE → All told, quite satisfactory. The Bank closed out the 2018 financial year with net income before taxes of 97 million euros. A respectable operating performance contributed to this result, as did having achieved major savings. Our Common Equity Tier 1 ratio stands at more than 18 percent and is strong. As expected, the results were weighed down very heavily by non-recurring effects in connection with the privatisation, the profound transformation spanning several years and the liabilities side of the balance sheet having to be restructured.

How was new business?
SE → Our new business including syndications reached a volume of 8.4 billion euros and was thus just below the previous year's level. In view of our privatisation and all the hopes and risks it entailed, this is a good performance by our sales teams.

What were the most important business areas in 2018?
SE → Our new business was once again supported by the Real Estate Clients division, where we signed 4.4 billion euros in new business, after 4.7 billion in the previous year. In the Corporate Clients division, which also includes project financings in Renewable Energies and Infrastructure, we signed 2.6 billion euros in new business, after 3.1 billion euros in 2017. Given the fierce competition in the domestic corporate client business, we deliberately exercised some restraint here. The new Hamburg Commercial Bank will not participate in the price war currently waging on the market in the traditional corporate clients business; it will, instead, take care to ensure a balanced risk/return ratio. This may also mean a further decline in volumes for the benefit of enterprise value. In Shipping, we increased new business from 0.5 billion to 0.9 billion euros and kept the risk and return requirements firmly in our sights. For the Bank as a whole, there were also around 400 million euros in syndications.

Will these areas remain the most important ones in future?
SE → Yes, the financing of commercial real estate, business with corporate clients including project finance in renewable energies and infrastructure as well as shipping will remain the main pillars of Hamburg Commercial Bank going forward. We will, however, increase the percentage of international business gradually in order to diversify our balance sheet better and increase the return on equity. This will be rounded off by a capital markets offering that is focused on the needs of clients.

What role did loan loss provisions play in 2018?
SE → Last year we set aside loan loss provisions of -367 million euros. This reflects the fact that our risk approach remains conservative. Given the increasingly uncertain underlying macroeconomic conditions, the keywords being Brexit, the possibility of a deterioration in the trade conflict, resulting in lower growth rates, we have increased portfolio risk provisioning, in particular. It is very important to note that we were freed almost completely from legacy assets in 2018 in the wake of privatisation. Our portfolio quality has improved substantially as a result: in all, our non-performing exposure (NPE) ratio – which measures how many loans are at risk of default – fell to around two percent. This is a respectable figure compared with other banks, which we want to maintain.

The results of Hamburg Commercial Bank are positive, the portfolio has been adjusted – has most of the work been done?
SE → No. But it is true that we have already achieved much through our privatisation. At the same time, we know that a long way still lies ahead of us, at the end of which we will be a successful private bank. The foundations are in place, but the restructuring work has only just begun.

Why is this major restructuring work necessary?
SE → We want to develop from a moderately profitable landesbank into an appropriately profitable bank in private hands. To achieve this, we must increase our profitability substantially. We aim to raise our enterprise value. This requires a major operational and financial transformation. All told, we must meet clear requirements regarding capital, expenses and income by the end of 2021. We are already meeting two goals: at more than 18 percent, our Common Equity Tier 1 ratio is easily in green territory, and our NPE ratio of around two percent matches the target figure. But we are currently not managing a cost/income ratio of no more than 40 percent or a return on equity of at least eight percent. We are still a long way off that.

Why are these indicators so important?
SE → As a rule, companies are only viable if they are profitable on a sustained basis. And the cost of capital, in particular, is a yardstick of profitability. We also need to achieve these goals to be accepted into the guarantee system of the Association of German Banks (BdB). It stipulates clear requirements, linked among other things to capital ratios and profitability.

"We want to develop from a moderately profitable landesbank into an appropriately profitable bank in private hands. To achieve this, we must raise our profitability substantially. We aim to increase our enterprise value. This requires a major operational and financial transformation."

Stefan Ermisch, Chief Executive Officer

Stefan Ermisch and Ulrik Lackschewitz hoist the flag of Hamburg Commercial Bank.

How does Hamburg Commercial Bank aim to achieve these targets?
SE → We will streamline our internal structures and increase the speed of both decision-making and implementation. In future, we will invest our capital in Germany and abroad only where it really pays off. We must assert ourselves on the market with our structuring expertise and skills and we want to place the clients at the centre of all we do even more than before, and convince them with our services. At the same time, we are planning to expand our activity by including some more business areas.

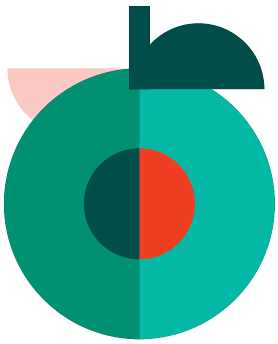
Can you give an example?
SE → Among other things, we will extend commercial real estate finance to France, Austria and the Benelux countries. We also want to carefully expand our radius when it comes to financing projects in renewable energies and infrastructure – in particular, we are considering becoming more active in the Asia-Pacific region. When it comes to internationalisation, I see particular opportunities in areas where we can score with our credit and structuring expertise.

Does transformation also mean staff reductions?
SE → Yes, unfortunately there is no other way because we need to cut our high costs. It is important to remember that many tasks within the Bank are no long needed due to the disappearance of the state guarantee, the end of the EU proceedings and the run-down of legacy assets. IT is due to be repositioned. Our product portfolio in Treasury & Markets has been significantly streamlined, we are spinning off less profitable, marginal activities. In order to work more efficiently and more effectively, we are reducing our management structure by one level and are thus also simplifying our internal processes. We presented the relevant plans to all employees immediately.

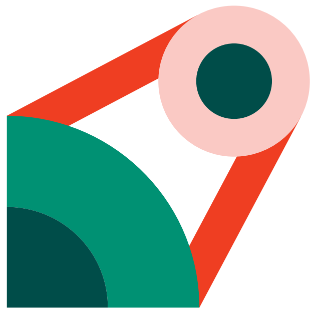
The bank is now named Hamburg Commercial Bank. Is the new name an advantage?
SE → Yes, because it stands for a new start. We are taking advantage of this opportunity to present ourselves on the market and win over new clients. We will create value.

Our strength: great know-how in selected sectors

We have a profound understanding of the markets in which we have specialised. We are therefore able to provide our clients with optimum support. As a banking partner, we help them achieve their goals quickly.



Food Industry

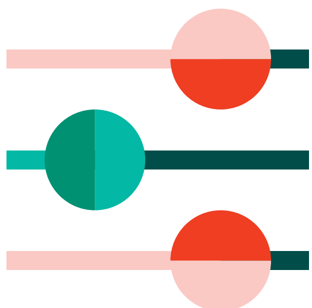


Industry & Services

Trade

M&A Advisory

Health Care



Structured Finance

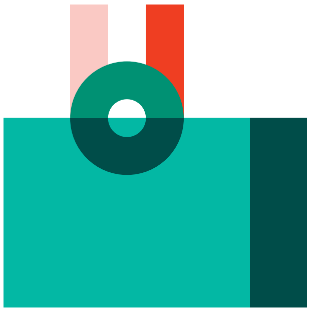
Shipping

Real Estate

Capital Markets & Products

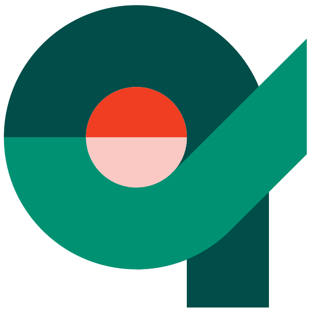
Wealth Management

Institutional Clients



Infrastructure & Logistics

Energy & Utilities



Transaction Banking

~~One~~

~~should~~

change

a lot.

"Re-imagining the way we work"

Dan Roth, Chief Transformation Officer

Only those who change are successful – Hamburg Commercial Bank is the first landesbank to be successfully privatised. Chief Transformation Officer Dan Roth explains how the bank wants to develop further.

Why is transformation important for the Bank?
Dan Roth → The privatisation is a historic event. It is the first privatisation of a landesbank. We are now at the point where we need to be able to compete according to international standards. We need to become a more profitable bank that generates higher returns and meets the needs of our German and selected international customers.

What does transformation mean exactly?
DR → Transformation involves all aspects of the bank, covering all areas necessary to create a more profitable bank. Transformation includes the way we go to market, our growth strategies, our funding strategy, our asset allocation, and everything around creating efficient customer facing and internal processes. The transformation workstreams reflect this, including the five principal transformation areas of Go to Market, Portfolio Management, Liability Optimisation, Operating Efficiency, and Organisational Vitality. It's critical that every employee understands how she or he can contribute to the transformation of the bank. We need to take advantage of the creative energy of every person to create a dynamic, flexible organisation that can compete in the rapidly evolving and highly competitive banking industry.

Will the new bank be different to HSH Nordbank?
DR → Transformation is about re-imagining the way we work to better serve our customers and to create a profitable bank with returns on equity that meet global banking standards. Transformation is about challenging the way that we did things historically, keeping and expanding what makes us stand out for our customers and eliminating or dramatically simplifying activities that our customers don't value. The transformation agenda will also include adjustments to the organisational structure. We are putting our top talent in positions where they can best influence the speed and impact of the transformation.

Does transformation involve a change of mindset?
DR → Yes, it does. We have to take the best of our environment and align it with a much more dynamic, agile, faster paced organisation that can quickly make decisions and be more competitive. We have to challenge ourselves to streamline or eliminate activities that are unnecessarily slow, internally focused or do not meet the needs of our customers. The mindset change will be rooted in a clear prioritisation of increasing profitability and meeting the needs of our customers.

How long will the transformation of this bank take?
DR → Much of the transformation, especially internal processes that we control, will take place in 2019, with certain areas like the IT transformation taking 2 to 3 years. Our go-to-market strategies are also sure to evolve over the next 1 to 2 years, with immediate focus on improving our cost of funding and allocating capital to asset classes and customers that meet our return-on-equity-objectives. It is important to realise that transformation is a process and it will ultimately be embedded in the way we work and think. Transformation never stops. There is no "status quo".

~~To~~ do:

Renewable Energy

“Support customers anywhere they go to implement new projects”

Nils Driemeyer, Head of Origination International

For more than 25 years we have been the strategic financing partner for the growth industry of renewable energies, and are among the leading providers of finance across Europe. Nils Driemeyer describes the new markets the Bank wants to tap and explains why power purchase agreements are becoming increasingly important.

Which markets are of interest to Hamburg Commercial Bank outside of Europe?
Nils Driemeyer → We grew up with our clients in Europe and we want to support them anywhere they go to implement new projects. For example, in Asia this may be Vietnam or Taiwan. These markets are promising because the expansion of renewable energies is in its infancy and the annual growth rates of expansion are substantially higher than in Europe. When implementing their projects locally, our clients want a partner at their side with considerable expertise and a wealth of experience in the sector.

How important is Europe and the German home market specifically?
ND → Of course, we are not overlooking the markets in Europe, quite the opposite! Europe is and remains our core market. We have successfully supported and financed projects in many countries, including the Netherlands, France, Germany, Scandinavia and Ireland. We will continue in this vein in 2019 and also strengthen our presence in Southern Europe again. Our home market also plays an important role for us. But at present it is uncertain how many projects can actually be implemented because of the lack of approvals for new projects.

What criteria do the transactions have to meet for us to sign them?
ND → One thing is quite clear: we don’t transact business at any price; we take care to ensure that the projects match with our risk/return profile. In 2018, we thus underwrote around 671 million euros in new business and acquired many new clients in the process.

There has been a growing trend of power purchase agreements (PPA), which allow wind and solar park operators to sell power directly to businesses they supply. Is this set to continue?
ND → This is a topic we discussed in depth in our sector study “Corporate PPA – Going Green”. Thanks to these power purchase agreements, which are concluded directly, operators of wind and solar plants are able to secure their revenues over the long term without state-regulated compensation – which is a clear advantage. We have delved deeply into the subject and were able to assist our customers early on with financing in Scandinavia. We expect PPAs to be used with increasing frequency in new renewable energy projects in Europe. At present, PPAs are primarily being signed in Sweden, Norway, Finland, the Netherlands and the UK.

Work is currently underway to find ways of storing wind or solar power. Is this already a topic for financing?
ND → We looked at a number of projects in 2018. At present, we are assisting our clients in conceptual terms in an exciting “power to gas” project, i.e. the production and storage of hydrogen from power generated using wind or solar power. But the statutory framework conditions in this area will need to be clarified. I expect to see very interesting developments over the coming two years.

671

€ 671 million of new project business done in the renewable energy sector.

4.6

€ 4.6 billion is our existing volume in energy and utilities.

58 %

The wind energy segment accounts for 58 percent of our overall volume in this sector.

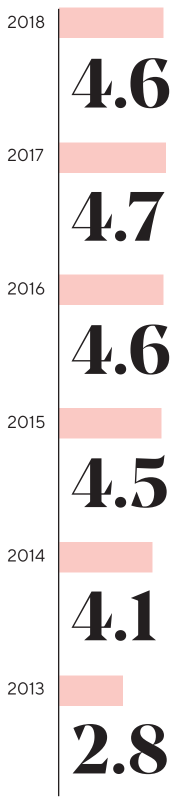
Real Estate Clients

“Attractive opportunities outside Germany”

For years, Hamburg Commercial Bank has ranked among the most significant institutions when it comes to financing commercial real estate in Germany. In future, the Bank will return to financing such activities outside Germany. Michael Windoffer explains how the Bank uses the new opportunities.

Michael Windoffer, Head of Cross-Border Business in the Real Estate division

New business in € billion (incl. Syndication)



Hamburg Commercial Bank is a fixture in the real estate sector in Germany, and in future it will be able once again to pursue business outside Germany. How will the Real Estate unit be positioned in future?
Michael Windoffer → In recent decades we have established a strong market position in northern Germany, and we are well-embedded in the metropolitan regions. We intend to expand these positions. That’s why we are represented throughout Germany by capable real estate teams who know their regions very well. A new development for us is that we are once again able to transact business outside Germany — and we intend to take this opportunity! The start of the international commercial real estate finance business is an important building block in the Bank’s transformation.

How does the Bank go about establishing its foreign business?
MW → Our initial focus is on clients with whom we already have a business relationship. We have worked together very well with many global players in the sector in the past and supported them with their investments in Germany. In future, we will support exactly these clients — who have great experience of the international real estate business and a good track record – in their undertakings outside Germany. A number of business partners, having worked with us successfully on projects in Germany, have signalled their willingness to broaden their partnership with us outside Germany.

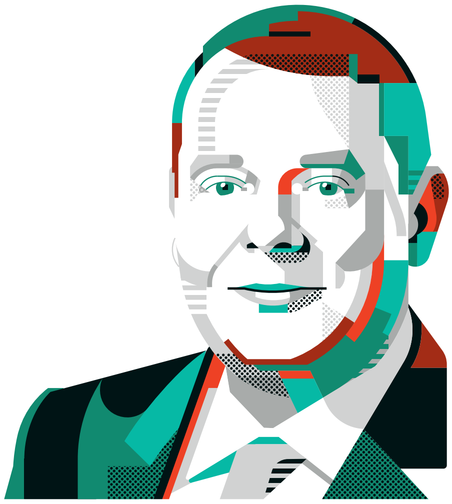
In Germany, clients particularly appreciate the Bank’s individually tailored financing for complex projects. What services is the Bank offering outside Germany?
MW → Of course, we also offer our international clients tailored financing geared to their specific business plans. We have a clear focus when it comes to selecting properties: during the start phase we concentrate on existing real estate where modernisations, for example, need to be financed. In addition, we participate in syndicate loans with other banks. Subsequently, project developments and more complex structuring will be added; these form part of our core expertise in Germany.

What countries will the Bank focus on?
MW → We will initially look at the markets in neighbouring European countries. They include Austria, France, Belgium, the Netherlands and Luxembourg as well as the UK. Every country has its particularities; every market is different. We see good opportunities in the Netherlands and already have a business relationship with a number of experienced and knowledgeable companies. The market in Austria is easy to survey, and the common language is an advantage. The UK faces the Brexit decision, and we need to watch how the situation develops, but we see medium-term opportunities for Greater London, in particular. We will manage our foreign business from Germany for the time being. The entire team is already looking forward to making the leap abroad, as we see attractive new opportunities there.

Shipping

“Extensive experience, in-depth understanding”

The Greek shipping market is the largest ship owning community in the world – Loukas Lagaras, Head of Shipping in Greece at Hamburg Commercial Bank in Piraeus, explains why this market is so resilient, even in turbulent times.



Loukas Lagaras, Head of Shipping Greece

What makes Greece such an attractive market for ship-financing banks?
Loukas Lagarars → At first it is important to point out that Greece is the biggest shipping nation in the world, controlling 17.3 percent of the world fleet capacity in terms of deadweight tonnage, ahead of Japan (11.7 percent) and China (9.6 percent). Approximately 600 registered owners operate a fleet of nearly 4,400 vessels. With a market value of about $ 105 billion as of end 2018, the Greeks control approximately 15 percent of the world’s trading fleet in terms of total value, followed by Japan at $ 95 billion and China at $ 91 billion. The Greeks are also very active players in both ship building and second hand markets. In 2018 they substantially increased their investment activity again, reaching a total of around $ 12.5 billion. The Greek owners have been working successfully for decades. For an international ship financier to be active in Greece is the natural choice, given the importance of this market.

Why are Greek shipowners so successful?
LL → Greek shipowners have extensive experience and deep understanding of the shipping markets. Greek shipping has traditionally been dominated by highly committed and financially strong families investing mainly their own funds. Over the last 20 years more owners have adopted a more corporate approach to the industry in order to create the necessary framework to exploit the international capital markets (mainly US and partly London and Oslo), as well as to develop joint ventures with private equity funds. Approximately 30 Greek-sponsored companies are currently listed on the US stock markets. However, the majority of the Greek-controlled fleet still remains under direct family ownership.

The shipping industry has suffered a major crisis in the last years. Have the Greek owners been heavily affected by the downturn?
LL → Greek shipping, once more, proved very resilient to the recent shipping crisis and actually took advantage of it to some extent. It is important to know that in Greece, due to the direct ownership structure, the owners of the shipping companies make the important investment decisions. This, along with their extensive experience and understanding of the market, allows an investment approach that is tailor made to the cyclical and volatile nature of the shipping industry. Traditionally the Greek owners take a counter-cyclical approach. In this way they are effectively taking advantage of the inherent volatility of the market, which enables them to grow even during periods of adverse market conditions. This approach provides more stability and better returns in the long run.

What can Hamburg Commercial Bank offer to Greek shipowners?
LL → I believe that our clients appreciate our international presence and expertise, our very good level of service and our long-term commitment to the industry and Greek shipping in particular. By continuing our successful operation and presence in the world’s largest shipping market, we have a strong chance of doing further attractive business here in the future.

1
€ 1 billion (incl. Syndication) of new business signed in 2018.

5.2
€ 5.2 billion is the total volume of our shipping business.

60 %
More than 60 percent of the portfolio is accounted for by financing outside Germany.

~~Im~~–

possible

Fritz Bedbur, Sales Team Treasury & Markets

Treasury & Markets

“The best of both worlds: low-cost funding and an individual structure”

The Treasury & Markets business unit supports clients in all market segments with individual capital market solutions in areas such as cash and risk management. Our specialists regularly develop new products to help our clients reach their goals. Sculpting swaps are one example of this. Fritz Bedbur explains how they work and why they make sense.

What are the benefits of sculpting swaps?
Fritz Bedbur → This type of swap individualises the interest rate over the entire term of the loan. It allows us not only to secure interest rates and optimise the entire cash flow, but also to tailor the structure of financing precisely to the wishes of our clients. As a result we are not only offering our clients their loan at favourable terms, but we can also sculpt it to meet their specific requirements.
How did the idea of a sculpting swap first emerge?
FB → We hit upon this idea when an increasing number of clients approached us with third-party loans, for example from development banks. The issue they had was that these loan agreements set out repayment structures and maturities that were strictly speaking unchangeable but did not fully correspond to their individual project requirements. As a first step, we secured the interest rate for our clients upon the expiry of the fixed-rate period. Then we discussed with our colleagues in the front office how we could sculpt these loans to the needs of our clients so as to give them the best of both worlds: secured, low-cost funding and an individual structure. This is how sculpting swaps were born.
Are sculpting swaps being well received by clients?
FB → The response has been very positive. In our new business we optimised around 70 percent of all transactions in 2018 using sculpting swaps. In our existing business, too, we have adjusted many finance deals to better suit the current market opportunities.
How difficult is the process of developing such new products?
FB → Of course, it’s not entirely straightforward, simply because many different areas are involved. From Risk to Finance, from Trading to the Legal department. But the cooperation has been consistently constructive and ultimately very fruitful. For us it is important that we constantly develop and improve. Such newly developed products demonstrate how that we can do precisely that.

“For us it is important that we constantly develop and improve. Such newly developed products demonstrate how we can do precisely that.”

Digitalisation

“Digitalisation is an important part of our transformation process”

Jan Sojka, Head of Digital Excellence Center

Better customer service, greater speed, more efficiency and fewer mistakes – digitalisation brings many benefits and is aiding the transformation of Hamburg Commercial Bank, as Jan Sojka from the Digital Excellence Center explains.

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Our Digital Excellence Center is working on four work streams simultaneously: Collaboration, Robotics Process Automation, Know Your Client and End to End Lending.

90%

The solutions developed in our Digital Excellence Center can accelerate our processes by up to 90 percent.

Why is digitalisation important for Hamburg Commercial Bank?
Jan Sojka → New technological possibilities accelerate and improve processes. Digitalisation is the technological foundation we need to be able to work more efficiently, faster and, above all, more profitably in the future. This saves us time and money. At the same time, digitalisation supports the cultural transformation within our Bank. For example, the use of new communication tools such as Office 365 automatically engenders a more direct, less complicated form of cooperation, both with our clients and within the Bank. This is what we seek to achieve. Digitalisation forms an important part of our entire transformation process.

What are the main opportunities that digitalisation brings?
JS → The biggest potential lies in direct contact with clients. Many of them expect their bank to digitalise their work processes more and more, and their message is clear: a bank unable to offer a good digital service will soon cease to be my bank. That’s why digitalisation is a strategic issue.

How does a digitalised client relationship work?
JS → First of all, the way it works is completely different from the analogue world. It is not about digitally replicating the current processes. Rather, digitalisation is an opportunity to completely redefine dialogue from a client’s perspective. This starts with credit initiation and runs through the entire lending process. Digitalisation will mark the development of the banking business over the coming years. Those who fall behind will struggle.

What examples of digitalisation can we see within the Bank?
JS → We are working on several projects. We can already observe our first process-automating robot at work. It takes four minutes to complete a process that requires around 40 minutes if done manually. It opens systems independently, transfers data, closes the systems again, changes and compares data – this used to be a manual process with many sources of error. This process now runs securely and smoothly.

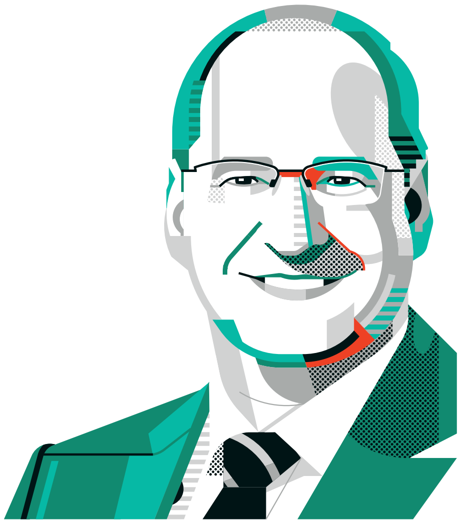
Is Hamburg Commercial Bank turning into a fintech?
JS → That’s going a bit too far. But we should seek to be guided by technology firms while at the same time maintaining our focus on our core business. In any case, technology firms are increasingly becoming rivals to financial service providers of all kinds.

“Digitalisation is the technological foundation we need to be able to work more efficiently, faster and, above all, more profitably in the future. This saves us time and money.”

IT

“Provide better, faster, more modern service”

Pushing ahead with digitalisation, improving customer service, speeding up operations in the back office – Ulrich Scheer on the importance of high-performance computers and how best to ensure they are state-of-the-art.



Ulrich Scheer, Head of IT

How important is the IT landscape for the success of Hamburg Commercial Bank?
Ulrich Scheer → It has become very important, primarily for the following two reasons. First, we need an efficient IT landscape in order to drive the Bank’s digitalisation, to accelerate internal processes and to deliver our clients an improved, faster and more modern service. Secondly, it is important to keep a very close eye on and reduce the cost of IT services. It is crucial to work as efficiently as possible. But this can only be achieved with modern systems that are tailored to what we do and what we need.
Banking has always been considered a people business. Is this changing due to the growing importance of IT?
US → Banking will, of course, remain a people business, especially when it comes to dealing with business clients. It is important to offer clients precisely tailored services. This means understanding what clients need, which requires a great deal of individual knowledge from our side. But of course, we support sales with our IT services and help ensure that operations in the back office run smoothly.
What are the criteria for a well-functioning IT service?
US → It must be fast, secure and inexpensive. At the same time, we have to reconcile two opposing demands: to maximise the standardisation and minimise the cost of business processes, while at the same time offering individual solutions for our clients. Such solutions are important because they are what set us apart from our rivals.

“We need an efficient IT landscape to drive the Bank’s digitalisation, to accelerate internal processes and deliver our clients an improved, faster and more modern service.”

Is an efficient IT service a prerequisite for success or a distinguishing feature?
US → In most cases efficient IT is essential in order to keep up with the competition. However, if we can offer clients particularly rapid, simple and smooth processes then this can prove to be an advantage. These are the distinguishing characteristics we are working on.
Is a bank that is getting smaller able to keep pace with the rapid developments in the IT sector, and what is the role of outsourcing in the midst of all of this?
US → It’s true that it’s difficult to remain aligned with all the current developments. For this reason, we have opted to outsource part of our operations to a partner. This means that our internal IT division will become substantially smaller going forward. By collaborating with a globally active IT specialist we will, in future, have access to a great deal of knowledge and considerable resources — and this is beneficial to us.

Human Resources

“Privatisation has made us a more attractive employer.”

Hamburg Commercial Bank is undergoing a transformation – Kaja Wilkniss explains why this heightens its appeal as an employer.

Katja Wilkniß, Head of Personnel Strategy

Young, well-qualified people are a sought-after commodity on the job market. What makes Hamburg Commercial Bank an attractive employer for them?
Kaja Wilkniss → One of our strengths is the fact that we are able to offer some very exciting challenges. We are the first landesbank to have successfully mastered privatisation, which has attracted new shareholders, and now we are forging ahead with the transformation we have initiated. We offer the most interesting story on the German banking market right now. Of course, a challenging path lies ahead of us. But pursuing it and, above all to help direct it is a great opportunity. Privatisation has made us a more attractive employer.

Will privatisation be enough of a strength to attract new employees?
KW → This is an important argument in conversations with applicants, but it is not the only one. For young people, in particular, it is important that they are able to take decisions themselves and assume responsibility quickly. This is exactly what we are offering – right now and to an even greater extent in the future. To make the Bank profitable over the long term we have to tackle job cuts. In a Bank that will be smaller going forward, every single person will play an even more important role. These factors aside, Hamburg Commercial Bank continues to pay a commensurate salary and offers good benefits. These are good prerequisites to ensure we are attractive to young talent.

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Education and training are important to us. We focus on young talent - which is why we had 22 dual course students and 19 trainees here at the Bank at the end of 2018.

What role do modern forms of working together and technological equipment in the workplace have to play?
KW → These also represent important aspects. Tackling projects, evaluating them on a regular basis and sometimes having the courage to end something in order to learn from mistakes – agile working is gaining in importance for us. In future, it will be much more about skills and less about hierarchies. What matters is the content, not who said what. And of course, young people also want to work with good technological tools. We are working on improving things in this area and are making good progress.

“We tell the most interesting story on the German banking market right now. Of course, a challenging path lies ahead of us. But pursuing it and, above all to help shape it is a great opportunity.”

Hamburg Commercial Bank is undergoing some major changes. Going forward, does this mean that the Bank’s employees will need different abilities to those they had in the past?
KW → Our classic virtues such as accuracy, thoroughness and reliability will remain in demand. At the same time, we require a great ability to change and an openness to new things. Speed, pragmatism, a clear client focus and a keen eye on our own profitability are crucial factors. For the Bank it is about working substantially more profitably than before – this is something all our colleagues need to focus on.

Sponsoring / Corporate Social Responsability

Great social commitment

The Schleswig-Holstein Music Festival, the Hamburg Commercial Bank Run, the Elbphilharmonie Foundation or help for the homeless – the Bank supports a diverse range of cultural and social projects.

Exercise, have fun and help – that is the motto of the Run.

Sponsorship

We see an engagement with society as part of our corporate responsibility. The Schleswig-Holstein Music Festival (SHMF), the Elbphilharmonie Foundation, the Hamburg Commercial Bank Run – as the HSH Nordbank Run is now called – the "Kids into Clubs" initiative and the delivery of freshly prepared meals to homeless day centres "Herz As" in Hamburg and "Hempels e.V." in Kiel: our engagement is wide-ranging and geared towards the long term.

The Bank has been one of the principal sponsors of the Schleswig-Holstein Music Festival for more than 30 years. In addition, together with the Savings Banks Finance Group, it has sponsored the € 10,000 Leonard Bernstein Award for young artists. The predecessor institution of Hamburg Commercial Bank is a founding member of the Elbphilharmonie Foundation and supports the Elbphilharmonie's programme as a "classic sponsor". By sponsoring "Resonances Season 2018/19" the Bank helps to enable the Resonance Ensemble to offer contemporary interpretations of classical music at the Elbphilharmonie concert hall.

In 2018 alone, we raised around € 38,000 through our charity initiative "Good for Kids" at Kieler Woche. The HSH Nordbank Run through Hamburg's HafenCity, which attracted 21,862 participants in 710 teams, generated an even higher total of € 165,000. "Good for Kids" enables children and young people from socially disadvantaged backgrounds to join sports clubs and thus participate in public life.

Corporate Social Responsibility

For us, sustainable management also includes searching for new ways to manage our natural resources sparingly. In its Report on Corporate Social Responsibility, the Bank is guided by the criteria set out in the German Sustainability Code. Decades ago we were among the pioneers of renewable energy financing: today we are among the major players on the European market. In the real estate segment, one of our key business areas, our financing helps to realise modern, low-energy building projects.

Within the Bank itself a state-of-the-art lighting system, low-energy printers and a modernised IT landscape ensure that energy is used sparingly. The company car rules also take environmental aspects into account. Because our staff canteens favour domestically sourced produce, primarily from the local region, there are no long transport routes. The welfare of our colleagues is something particularly close to our hearts, which is why health management is a high priority for us at the Bank.

Report of the Supervisory Board

Report of the Supervisory Board on the 2018 financial year
In the 2018 financial year, the Supervisory Board performed the tasks incumbent on it by law and in accordance with the articles of association. In particular, it monitored the management of the company and provided advice to the Management Board in matters relating to corporate governance. One focal point of last year's work was the Bank's privatisation. In addition to strategic matters relating to the Bank's focus, the Supervisory Board continually reviewed the Bank's economic and financial development as a whole, as well as reviewed the individual business segments, and discussed these aspects in detail. The Supervisory Board was provided with explanatory information on any deviations from the plan in the course of business.

In the 2018 reporting year, the Management Board provided the Supervisory Board with regular, timely and comprehensive information on the Bank's business policy and other fundamental issues relating to corporate governance and planning, financial development, operating performance and the Bank's risk, liquidity and capital management, as well as on major legal disputes and transactions and on events of fundamental significance to the Bank. The Supervisory Board was involved in any decisions that were of key significance to the Bank. The Management Board also provided the Chairperson of the Supervisory Board and the Chairpersons of both the Risk and Audit Committees with information on key issues and upcoming decisions, also between the planned meetings. Where resolutions had to be passed between meetings, the Supervisory Board passed these resolutions using written proceedings.

In the 2018 financial year, the completion of the privatisation process had a decisive impact on the Bank's orientation, while market conditions, in particular the crisis on the shipping markets, eased slightly. The beginning of 2018 was characterised by preparatory measures for the signing process, i.e. the contractual agreement to sell the Bank. As the year progressed, the focus was on preparing for the closing process, which was successfully completed on 28 November 2018. Within this context, the Supervisory Board dealt, in particular, with the change in the guarantee scheme. The Supervisory Board was closely involved in both processes (signing and closing). It sought ongoing information on the status of the key milestones on the path towards privatisation and – where necessary – passed corresponding resolutions. The Supervisory Board sought legal advice within this context where necessary.

Meetings of the Supervisory Board
The Supervisory Board held nine meetings in the 2018 financial year, three of which were convened as extraordinary meetings. One meeting (28 November 2018) was the constituent meeting of the Supervisory Board following the election of new shareholder representatives after the sale of the Bank.


Juan Rodríguez Inciarte has been Chairman of the Supervisory Board of Hamburg Commercial Bank since November 2018

The Management Board provided the Supervisory Board with information on a regular basis, based on the figures available for each quarter, on the Bank's current financial situation, business developments on the whole and in the individual business segments, as well as in relation to the current business plan, on the risk situation, capital development and on the liquidity and funding situation. In addition, the Management Board provided the Supervisory Board with regular information on the current status of the privatisation process. The Supervisory Board subjected the reports to a critical analysis and, in some cases, requested additional information and documents. The Supervisory Board also addressed various Management Board matters. The auditor of the annual financial statements took part in the Supervisory Board meetings on a regular basis and was available to provide the Supervisory Board with supplementary information.

The meeting held on 15 February 2018 focused on an in-depth assessment of the financial, investment and workforce plan for 2018–2020 submitted by the Management Board. The Supervisory Board also addressed its Corporate Governance Report and Declaration of Conformity, as well as the Report of the Supervisory Board for the 2017 financial year and the sale of six aircraft.

On 23 and 26 February, the Supervisory Board dealt with the transactions relevant to the signing process as part of the privatisation. This included an intensive discussion about the related portfolio transaction and the relevant resolution recommendations to be made to the Annual General Meeting. The Supervisory Board was provided with detailed information by the Management Board and external consultants, discussed the items on the agenda extensively and in detail and ultimately passed corresponding resolutions.

The main issue covered at the meeting held on 25 April 2018 (year-end meeting) was the approval, based on the recommendation made by the Audit Committee, of the annual financial statements and Group financial statements for 2017 following the Supervisory Board's own assessment and prior discussion with the auditor of the annual financial statements. In this context, the review and approval of the non-financial declaration in accordance with Section 289 b of the German Commercial Code (HGB) ("CSR Reporting") for 2017 was also on the agenda. The other standard resolutions to be passed within this context regarding the recommendations to be made to the ordinary Annual General Meeting were also passed. The Supervisory Board also used this meeting to discuss the target achievement level of the Management Board for the 2017 financial year and to pass a resolution on the Management Board targets for 2018. In addition to the resolutions in connection with the annual financial statements, the Supervisory Board also dealt with the approval of the conclusion of two enterprise agreements to supplement an existing silent partnership agreement. The agenda for this meeting also included the discussions on the "Report on equity investments", the "Overview of secondary employment relationships of Management Board members" and the "Report on donations" of the Bank, which are conducted once a year.

On 14 June 2018, the Supervisory Board was provided with information, in particular, on the current status in connection with the action taken by the hybrid capital investors with regard to the portfolio transaction agreed in February and passed resolutions on the need for law firms to provide advice to the Management Board and Supervisory Board.

At the meeting held on 29 August 2018, the Supervisory Board dealt with Management Board matters but also with the assumption of costs for litigation risks of the Supervisory Board members in connection with the action taken by the hybrid capital investors. The Supervisory Board also took note of the report of the Chairman of the Management Board for the years 2013–2018 and was consulted prior to the appointment of the new remuneration officer.

On 16 November 2018, the last ordinary meeting of the year took place in the previous composition of the Supervisory Board. At this meeting, the Supervisory Board dealt with the results of its own efficiency review in accordance with Section 25 d of the German Banking Act (KWG) and the evaluation of the Management Board. The Management Board also presented and explained its annual report on the structure of the remuneration systems. The Management Board also provided the Supervisory Board with information about the action that had to be taken by the Supervisory Board in connection with the closing process and about a potential LME (Liability Management Exercise).

Following the closing as part of the privatisation process and the associated change of shareholders, the constituent meeting of the Supervisory Board took place on 28 November 2018 after the previous shareholder representatives had resigned from their positions with effect from the closing. At this meeting, the Chairman and Deputy Chairman of the Supervisory Board and the new members of the committees were elected. In addition, the Supervisory Board was informed about the D&O insurance policy in force at Hamburg Commercial Bank and about the current status of the SPA/LSPA closing and the planned potential LME.

At an extraordinary meeting on 10 December 2018, the Supervisory Board was informed about the transformation programme planned for 2019, as well as passing resolutions on Management Board matters.

In the year under review, the Supervisory Board also passed two resolutions using the written procedure, both of which related to recommendations for resolutions to be passed by Annual General Meetings.

The Supervisory Board continued its further training in various areas in 2018. To this end, the presentations made at Supervisory Board meetings were partly intended as a source of training. Examples include IFRS 9, the privatisation process, non-financial reporting in the management report in accordance with Section 289 b–e HGB, the German Ordinance on the Remuneration of Financial Institutions, various topics relating to the shipping markets and IT security management, as well as the GDPR.

Where individual members of the Supervisory Board were affected by resolutions passed by the Supervisory Board or its committees, either in person or on account of their function, or if other potential conflicts of interest arose, then these members did not participate in the deliberations and resolutions in the executive body concerned. The number of other significant mandates held by the Supervisory Board members can be found in the Corporate Governance Report in this Annual Report.

One member of the Supervisory Board attended fewer than half of the meetings of a committee to which he belongs. This committee met three times in the year under review and the member attended only one of the meetings.

All other members of the Supervisory Board took part in at least half of the meetings of the Supervisory Board and the committees of which they are members.

Committees of the Supervisory Board
The Supervisory Board has formed five committees from among its members that support it in its work.

Last year, the **General/Nominating Committee** held seven meetings, two of which were extraordinary meetings. The General Committee prepared the resolutions of the Supervisory Board in accordance with the rules of procedure for the Supervisory Board. Where necessary, the Committee passed its own resolutions or the Supervisory Board was provided with recommendations on the passing of resolutions.

The **Risk Committee** met five times during the last financial year and passed one resolution in writing. Representatives of the auditor of the annual financial statements also took part in the meetings on a regular basis. The Risk Committee took an intensive look at the Bank's risk position and risk management system. Within this context, it addressed the updates to the Strategic-Risk-Framework, which provides the risk framework for business strategy and planning. In particular, reports on current events and developments, and their impact on the risk situation, were made to the Committee at all of its meetings. The Risk Committee also discussed important individual exposures for the Bank and received reports on progress made in winding down NPL holdings. The Risk Committee discussed all commitments subject to a submission requirement and passed resolutions on business transactions requiring approval by law. At a joint meeting with the Remuneration Control Committee, the Risk Committee also reviewed the Bank's remuneration systems to see whether the incentives set by these remuneration systems took the Bank's risk, capital and liquidity situation, as well as the probability and due date of revenue, into account.

The **Audit Committee** met four times in 2018 and also received additional relevant information outside of its meetings. One resolution was adopted using the written procedure. Representatives of the auditor of the annual financial statements took part in all of the meetings. The members of the Audit Committee discussed the annual and consolidated financial statements of the Bank for 2017 and the corresponding audit reports with the previous auditor KPMG. Within this context, the Audit Committee also addressed the Dependent Company Report. The Committee reviewed the independence of the auditor of the annual financial statements in accordance with the requirements set out in the German Corporate Governance Code based on the declaration of independence issued by the auditing firm, and prepared the appointment of PwC Wirtschaftsprüfungsgesellschaft as the new auditor of the annual financial statements for 2018.

The auditor reported on the current results of its audit on a regular basis and presented the current status of the planning for the audit of the annual and Group financial statements. Regular reports were also provided to the Committee on the commissioning of the auditor of the annual financial statements to perform tasks not related to the audit, on the work of the Internal Audit department and on compliance matters. The Committee discussed the corresponding reports to satisfy itself as to the effectiveness of the risk management system – in particular the internal audit and internal control system. Furthermore, the Committee addressed the results of the securities account audit and the audit of investment services pursuant to the German Securities Trading Act (WpHG). Finally, the topics covered by the meeting also included current reports on IT restructuring and IT strategy.

The **Remuneration Control Committee** met three times in the reporting year and held one joint meeting with the Risk Committee. It took an in-depth look at the Bank's remuneration systems and received regular reports on the status of the implementation of the requirements resulting from the German Ordinance on the Remuneration of Financial Institutions (Institutsvergütungsverordnung), and on the current status of statutory developments relating to remuneration in the banking sector. In 2018, the Remuneration Control Committee continued to address the status of the implementation of the changes resulting from the amendment to the German Ordinance on the Remuneration of Financial Institutions that came into force in August 2017. The remuneration officer also reported to the Remuneration Control Committee on the results of his control activities and presented his remuneration control report, which has to be prepared once a year, to the Committee. The Chairperson of the Remuneration Control Committee consulted the remuneration officer on relevant issues on a regular basis even outside of the meetings.

There was no need for any meeting of the **Mediation Committee,** which is to be set up in accordance with the provisions of the German Co-Determination Act (Mitbestimmungsgesetz), in 2018.

The Chairpersons of the Committees regularly reported to the Supervisory Board during the subsequent plenary sessions about the work and results of the Committees' deliberations.

Audit and adoption of the annual financial statements and consolidated financial statements for 2018
The accounts, the annual financial statements, including the management report, and the Group financial statements, including the Group management report, for 2018 were audited by PricewaterhouseCoopers GmbH Wirtschaftsprüfungsgesellschaft, Hamburg. This company was selected by the Extraordinary General Meeting held on 21 November

2017 as the auditor of the annual financial statements and Group financial statements, an appointment that was confirmed by the Ordinary Annual General Meeting held on 28 June 2018. The audits led to an unqualified audit opinion being issued in each case.

The documents relating to the annual financial statements and the audit reports, including all appendices, were sent to all Supervisory Board members prior to the meetings. The auditor of the annual financial statements initially reported on the performance and principal findings of its audit to the Audit Committee at the latter's meeting held on 26 March 2019. On this basis, and on the basis of its own assessment, the Audit Committee discussed the results with the auditor of the annual financial statements in detail. The Chairperson of the Audit Committee informed the Supervisory Board of the outcome of its deliberations in the Audit Committee at the Supervisory Board meeting held on 27 March 2019. The auditor of the annual financial statements also took part in the meeting of the Supervisory Board and reported on the principal findings of its audit. Based on the recommendation made by the Audit Committee, the Supervisory Board ultimately agreed with the findings of the audits, following its own examination of the reports of the auditor and an in-depth discussion, and established that, following the final result of its own reviews, there were no objections to be raised. The Supervisory Board approved the 2018 annual financial statements drawn up by the Management Board, meaning that they have been formally adopted, and also the 2018 consolidated financial statements. It also approved the Report of the Supervisory Board for the 2018 financial year.

The Management Board also submitted its report on relationships with affiliated companies (Dependent Company Report) in the 2018 financial year to the Supervisory Board and the auditor of the annual financial statements on time. The auditor audited the Dependent Company Report and issued the following unqualified audit opinion:
"On the basis of our due and diligent audit and assessment, we confirm that

1. the factual statements made in the report are correct,
2. in respect of the legal transactions included in the report, the consideration paid by the company was not inappropriately high.
3. in respect of the measures listed in the report, there were no circumstances supporting an assessment significantly different to that made by the Management Board.

The Audit Committee and the Supervisory Board assessed the Dependent Company Report prepared by the Management Board and the audit report prepared by the auditor of the annual financial statements, and discussed them with the Management Board and the auditor of the annual financial statements as part of the review of the annual financial statements. The Supervisory Board approved the outcome of the audit conducted by the auditor of the annual financial statements as, based on its assessment, there were no objections to be raised to the declaration made by the Management Board in the Dependent Company Report.

Changes in personnel
On the closing date of 28 November 2018, all previous shareholder representatives on the Supervisory Board resigned from their positions. This means that the former Supervisory Board members Dr Thomas Mirow (Chairman), Silke Grimm, Stefan Jütte, Dr Rainer Klemmt-Nissen, Dr Philipp Nimmermann, Dr David Morgan, Elke-Weber-Braun and Jörg Wohlers have left the Supervisory Board. On the same day, an Extraordinary General Meeting was held at which the following new shareholder representatives were elected to the Supervisory Board: Juan Rodríguez Inciarte (Chairman), Mark Werner, Mark Neporent, Manuel González Cid, James Christopher Flowers, Michael Christner, Paulus de Wilt, Geoffrey Adamson, Allen Gibson and Chad Leat.
The Annual General Meeting also passed a resolution on expanding the Supervisory Board from 16 to 20 members. This means that the Supervisory Board comprised ten new shareholder representatives but only eight employee representatives. This gap is to be closed by the appointment of two additional employee representatives by the court.

An additional staff member joined the Management Board in the 2018 reporting year: Dr Nicolas Blanchard joined the Management Board as Chief Clients Officer on 10 December 2018. Mr Temp resigned from his position on the Management Board by mutual agreement with effect from 31 December 2018.

The Supervisory Board would like to thank the Management Board and all of the Bank's employees for their considerable personal commitment and achievements in the year of successful privatisation, which was a decisive year for the Bank.

Hamburg/Kiel, 27 March 2019

The Supervisory Board

Juan Rodríguez Inciarte
Chairman of the Supervisory Board of
Hamburg Commercial Bank AG

Corporate Governance

All statements in this Corporate Governance Report reflect the situation that prevailed on 20 February 2019 in the absence of any references to the contrary.
As an unlisted company, Hamburg Commercial Bank has been recognising the German Corporate Governance Code (GCGC) voluntarily since 2005. Corporate governance at Hamburg Commercial Bank is also principally based on the provisions of the German Stock Corporation Act, the German Banking Act and internal rules such as the Articles of Association and the rules of procedure that apply to the Management Board and the Supervisory Board, as well as the Code of Conduct of Hamburg Commercial Bank. By presenting the system of corporate governance and control and by reporting transparently on conformity to the recommendations of the Code, the aim is to strengthen the confidence that investors, clients and employees, as well as the general public, have in Hamburg Commercial Bank.

Declaration in accordance with Section 161 of the German Stock Corporation Act
In accordance with Section 161 of the German Stock Corporation Act, the Management Board and Supervisory Board of listed companies must publish an annual declaration of how their management and supervision systems conform to the recommendations of the German Corporate Governance Code or deviate from them. The Bank's aim is to conform to the GCGC as fully as possible even as a non-listed company. As a result, in February 2019, the Management Board and the Supervisory Board of Hamburg Commercial Bank voluntarily issued the Declaration of Conformity set out below, in which the deviations from the GCGC recommendations are disclosed.

Declaration of Conformity
The Management Board and the Supervisory Board of Hamburg Commercial Bank declare that since publishing their last Declaration of Conformity on 15 February 2018, Hamburg Commercial Bank has conformed to the recommendations of the German Corporate Governance Code in the version dated 7 February 2017 in every respect save for the exceptions stated below. Until the date on which the next Declaration of Conformity is publicised, Hamburg Commercial Bank will be conforming to all the recommendations of the Code save for the exceptions stated below.

Section 4.2.2 (2) sentence 3 and 4.2.3 (2) set out details on the remuneration of the Management Board which the Supervisory Board is to take into account when structuring the Management Board remuneration system.
Until the change of ownership, the Management Board remuneration system was based on the provisions of the guarantee agreement with the federal states of Hamburg and Schleswig-Holstein, in particular the Appendix entitled "Obligations incumbent upon HSH" dating back to 2009, which the majority owners refrained from amending in view of the political interests involved. This meant that variable remuneration was not possible for the Management Board. Similarly, the Supervisory Board did not comply with the requirement stating that it should consider the ratio of Management Board remuneration to the remuneration paid to the senior management and entire staff.
The Management Board contracts concluded following the change of ownership provide for both fixed and variable components for the Management Board members.

Pursuant to Section 4.2.3.3, the Supervisory Board is to establish, in respect of pension schemes, the level of provision aimed for in each case and take into account the resulting annual and long-term expense for the company.
A defined contribution plan is in place for the Management Board members of Hamburg Commercial Bank that does not aim at a certain level of provision.

In accordance with Section 4.2.4, the total compensation of each one of the members of the Management Board is to be disclosed by name, divided into fixed and variable compensation components.
This is not a GCGC recommendation, but rather a mandatory statutory provision for listed companies, because the German Commercial Code (HGB) sets out a mandatory disclosure requirement for listed companies. As an unlisted company, however, Hamburg Commercial Bank is not subject to this obligation in principle. Furthermore, the parameters of Management Board remuneration that applied up until the change of ownership have already been made sufficiently public in line with the requirements set out in the Appendix entitled "Obligations incumbent upon HSH" – set upper threshold for basic salary, no variable remuneration.

In accordance with Section 4.2.5, model tables are to be used to provide certain pieces of information on remuneration and fringe benefits for each Management Board member.
As Hamburg Commercial Bank does not disclose the Management Board remuneration paid to individual members, this information is not published either. (See also Section 4.2.4)

According to Section 5.3.2 (3) sentence 2, the Chair of the Audit Committee should be independent. The Chair of the Audit Committee who held this position up until the change of ownership was independent; since the change of ownership, a Chairman who cannot be regarded as independent within the meaning of the Corporate Governance Code has been in office on an interim basis. The position will soon be assumed by an independent member of the Supervisory Board, meaning that this deviation will then cease to apply.

In accordance with Section 5.4.1.2, the Supervisory Board is to specify concrete objectives regarding its composition, including a limit of length of membership to be specified for the Supervisory Board.

The Supervisory Board has decided not to set a limit on the length of membership of the Supervisory Board, as it is difficult to define an ideal length of membership.

Section 5.4.6 (3) sentence 1 recommends that the remuneration of Supervisory Board members be disclosed individually in the explanatory notes to the financial statements or the management report, classified by remuneration components. The remuneration paid to all Supervisory Board members in office up until the change of ownership is disclosed individually in the explanatory notes. A resolution still has to be passed on the disclosure of the remuneration paid to those Supervisory Board members who joined after the change of ownership.

According to sentence 4 of Section 7.1.2, the Group financial statements are to be publicly accessible within 90 days of the end of the financial year, and the mandatory financial information published during the year is to be publicly accessible within 45 days of the end of the reporting period. Hamburg Commercial Bank had not published either the Group financial statements for 2017 or the interim reports for 2018 by the specified deadlines. The Bank aims to adhere to the recommended publication deadlines in the future.

Hamburg Commercial Bank has complied with the recommendations set out in the Code insofar as they make sense for an unlisted corporation.

Hamburg/Kiel, 20 February 2019

For the Management Board

Stefan Ermisch

For the Supervisory Board

Juan Rodríguez Inciarte

Supervisory Board

Composition
According to the Articles of Association, Hamburg Commercial Bank's Supervisory Board consists of 20 members, of whom - in accordance with the provisions of the German Co-Determination Act (Mitbestimmungsgesetz) - half are representatives of the capital side and half are employee representatives. The capital side of the Supervisory Board comprises expert representatives of the business world, some of whom are independent of the shareholders and the Bank. At the time this report is published, status proceedings are underway, the aim being to switch from parity co-determination (where half of the Supervisory Board members are employee representatives) to one-third employee participation. Once these proceedings have been completed, the Supervisory Board is to consist of 18 members, 12 of whom will be shareholder representatives and six of whom will be employee representatives.

Section 5.4.1 of the GCGC stipulates that the Supervisory Board is to specify concrete objectives regarding its composition which, whilst considering the company-specific situation, take into account the international activities of the company, potential conflicts of interest, the number of independent Supervisory Board members, an age limit and a regular limit to Supervisory Board members' term of office, both to be specified, as well as diversity. The latter objective shall, in particular, provide for an appropriate degree of female representation.

In its previous composition, the Supervisory Board set objectives. The extent to which these objectives had been met by the time of the change of ownership is reported below. As explained above, at the time this report is published, the Supervisory Board is in a transitional phase following the change of ownership and prior to the transition to the new co-determination system of one-third participation. It only makes sense for the Supervisory Board to set itself the objectives set out in the German Corporate Governance Code once it has achieved the planned composition.

The objectives set by the Supervisory Board back in 2011 are as follows:

1. The Bank will seek to continue to have at least the same number of international members on its Supervisory Board as it currently has (minimum one member).
2. When nominating new members to the Supervisory Board, the Bank will seek to avoid potential conflicts of interest, while also taking the rules of procedure for the Supervisory Board into due consideration, in future as well.
3. The Bank will seek to adhere to the age limit of 68 years at the date of appointment stipulated in the Rules of Procedure for the Supervisory Board in future.
4. The Bank will seek to maintain the proportion of representation by women at least at the current level of 20 percent in future as well. The Supervisory Board considers an initial target of 30 percent to be an appropriate proportion of women.
5. On the shareholder side, the Supervisory Board will aim to have independent members comprise at least half of its members in the future, too. (Objective added in 2012)

When nominating new members, care is taken to prevent potential conflicts of interest and ensure a sufficient number of independent members. New members have fallen below the age limit of 68 years at the time of appointment in each case.

As a company subject to co-determination – be it parity co-determination or co-determination under the German One-Third Participation Act (Drittelbeteiligungsgesetz) – Hamburg Commercial Bank also falls under the scope of the German Act on Equal Participation of Women and Men in Executive Positions in the Private and the Public Sector (Gesetz für die gleichberechtigte Teilhabe von Frauen und Männern in Führungspositionen in der Privatwirtschaft und im öffentlichen Dienst), also known as the "Quota Act". The Supervisory Board has set a target for the proportion of women on the Supervisory Board of 30 percent. By the time of the change of ownership, the Supervisory Board had reached this target with 31.25 percent of its members being women. On the shareholder side, the proportion of women came to 25 percent while on the employee side, it came to 37.5 percent.

The Supervisory Board of Hamburg Commercial Bank deliberately refrained from setting a limit on the length of membership of the Supervisory Board. The Supervisory Board found it difficult to define such a limit and also considered it important to be able to retain existing expertise on the Supervisory Board.

In addition, pursuant to Section 5.4.1, the Supervisory Board is to draw up a competence profile for the entire Supervisory Board. As part of its annual efficiency review, which was conducted in November 2018, the Supervisory Board looked at the skills, competencies and experience within the Supervisory Board and updated its competence profile, which was prepared for the first time in 2014. The competence profile gives the Supervisory Board an overview of the competencies represented within the Supervisory Board. This means that, when members have to be appointed to the Supervisory Board or when the Supervisory Board is looking for suitable candidates in the future, it can draw up corresponding objectives directly to make sure that competencies are replaced/additional competencies added.

Section 5.4.1 of the GCGC also stipulates that the Supervisory Board must provide information about what it regards as the appropriate number of independent Supervisory Board members representing shareholders, and the names of these members. Section 5.4.2 of the GCGC explains when a Supervisory Board member is to be considered non-independent. Based on these provisions, members are considered non-independent in particular if they have a personal or business relationship with the corporation, its governing bodies, a controlling shareholder or a company affiliated with the controlling shareholder that may cause a substantial and not merely temporary conflict of interest. Up until the change of ownership, the Supervisory Board of Hamburg Commercial Bank considered it appropriate for at least half of the Supervisory Board to be composed of independent members on the shareholder side. These members were: Dr Thomas Mirow, Silke Grimm, Stefan Jütte and Elke Weber-Braun.

Procedure

The Supervisory Board appoints, monitors and advises the Management Board and is involved in fundamental decisions made by the Bank. The Management Board informs the Supervisory Board regularly and in good time of the proposed business policy and other fundamental matters during the meetings and also orally, particularly in conversations between the Chairman of the Management Board and the Chairman of the Supervisory Board.

Section 26 d (11) sentence 2 no. 3 of the German Banking Act (KWG) requires the Supervisory Board to evaluate the structure, size, composition and performance of the management and supervisory body on a regular basis, at least once a year. To this end, shortly before the change of ownership, the Chairman of the Supervisory Board, his deputy and the chairs of the committees not only examined various aspects of the work of the Supervisory Board using questionnaires, but also evaluated the work of the Management Board. The results of the survey were discussed in detail in a plenary session of the Supervisory Board. The efficiency review revealed that the Supervisory Board is satisfied with the efficiency of its activities on the whole.

In order to ensure that the Supervisory Board has up-to-date specialist and expert knowledge at all times, various submissions made to the Supervisory Board last year were considered a source of training. These submissions dealt with current topics. Further information on the contents of the training can be found in the Report of the Supervisory Board.

Other mandates

In order to be able to perform their Supervisory Board duties properly, the Supervisory Board members have to devote sufficient time to these activities. This means that the individual Supervisory Board members can only have a limited number of other duties over and above their Supervisory Board activities. The Supervisory Board members of Hamburg Commercial Bank have the following number of other Supervisory Board mandates at other companies:

Supervisory Board member	**No. of other mandates** (as at: 20 February 2019)
Juan Rodríguez Inciarte	1
Peter Axmann	2
Manuel González Cid	3
Michael Christner	2
J. Christopher Flowers	2
Chad Leat	3

Detailed information on the Supervisory Board activities in 2018 can be found in the Report of the Supervisory Board.

Remuneration
The remuneration paid to those Supervisory Board members in office up until the change of ownership is disclosed individually in the explanatory notes to the annual financial statements.

Management Board

Composition
As of February 2019, the Management Board of Hamburg Commercial Bank consists of four members and is divided into the following areas of Board responsibility: CEO (Chief Executive Officer), CRO (Chief Risk Officer), CFO (Chief Financial Officer) and CCO (Chief Clients Officer). When selecting new Management Board members, the Supervisory Board must adhere to the relevant legal requirements. The German Corporate Governance Code requires, in particular, the appropriate representation of women, while the German Banking Act states that consideration should be given to ensuring balanced and varied knowledge, skills and experience for all Management Board members. The rules of procedure for the Supervisory Board also contain requirements that the Supervisory Board and/or the General/Nominating Committee has to take into account when identifying applicants to fill a Management Board position. This means that the Supervisory Board looks at the Management Board position to be filled on a case-by-case basis and selects Management Board members taking into account the requirements of the position in question and the competencies already represented on the Management Board based on an individual job profile.

Procedure
The Management Board is responsible for the management of the Bank and works with Hamburg Commercial Bank's other corporate bodies and with the employees' representatives on a basis of mutual trust in the Bank's best interests. It defines the Bank's strategic alignment in consultation with the Supervisory Board. The Chairman of the Management Board represents the Management Board as a collegial body, presides over its meetings and coordinates its work. The Management Board largely met once a week during the period under review. The members of the Management Board are jointly responsible for running the Bank's business. Their duties and responsibilities are laid down in the Rules of Procedure for the Management Board, as supplemented by the business allocation plan.

Other mandates
One Management Board member has a mandate on the Supervisory Board of one of the Bank's subsidiaries and one Management Board member has a mandate on the Supervisory Board of another company. Other than this, the Management Board members do not perform any management or supervisory functions at other companies.

Remuneration
Details of the compensation system for the Bank's Management Board can be found in the explanatory notes to the annual financial statements.

Shareholders, Annual General Meeting

Hamburg Commercial Bank's shareholders exercise their rights at the Annual General Meeting. The Management Board convenes the Annual General Meeting once a year, stating the agenda and including the requisite reports and documents.

In addition to the agenda items that an Annual General Meeting has to cover by law, the ordinary Annual General Meeting held in June 2018 also addressed the approval of planned share transfers. An Extraordinary General Meeting was held in February to pass the resolutions required in connection with the privatisation process. In November 2018, two further Extraordinary General Meetings were held at which amendments to the Articles of Association, share transfers and the election of new shareholder representatives to the Supervisory Board were on the agenda.

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Information on the combined management report
To improve the clarity of presentation, the management reports of Hamburg Commercial Bank AG (formerly HSH Nordbank AG) and the Hamburg Commercial Bank Group have been combined in accordance with Section 315 (5) of the German Commercial Code (HGB) in conjunction with Section 298 (2) HGB, unlike in the previous year. The annual and Group financial statements of Hamburg Commercial Bank (including the combined management report) will be jointly submitted to the operator of the German Federal Gazette and published in the Federal Gazette. In addition, the annual and Group financial statements of Hamburg Commercial Bank are available on the Internet at www.hcob-bank.com. The following information in the combined management report relates to the Hamburg Commercial Bank Group as a general rule; in the event of material differences with regard to Hamburg Commercial Bank AG, separate explanations are provided.

Basis of the Group

Business activities

Successful sale of HSH Nordbank AG and conclusion of EU state aid proceedings

The federal state owners Hamburg and Schleswig-Holstein, as well as the minority owner Sparkassen- und Giroverband für Schleswig-Holstein, sold their stake of 94.9 % in HSH Nordbank AG, which was held indirectly via HSH Beteiligungs Management GmbH, in full to several investors on 28 February 2018 (signing). The sale was closed on 28 November 2018 after all of the conditions precedent had been fulfilled. The buyers are independent funds of Cerberus Capital Management, L.P., J.C. Flowers & Co. LLC and GoldenTree Asset Management LP as well as an Acquisition Company of Centaurus Capital LP and BAWAG P.S.K.

The sale marks the end of the long-standing EU state aid proceedings, which resulted in far-reaching structural relief for the Bank. This is reflected primarily in a significant improvement in the risk and capital structure. As part of the privatisation process the Bank was relieved of large parts of its non-performing legacy loans (portfolio transaction). These mainly included ship financing arrangements from the years prior to 2009. In addition, the second loss guarantee of € 10 billion provided by the federal state owners was terminated prematurely in return for a compensation payment of € -100 million and settled in full.

HSH Nordbank is the first successfully privatised Landesbank in Germany. The privatisation lays a solid foundation for the next stage in the forward-looking transformation process, during which the Bank will gradually develop into an agile commercial bank with a business model that is sustainable in the long run. The privatised bank has changed its name and has been operating under the name Hamburg Commercial Bank AG since 4 February 2019.

Headquarters, regional focus, clients and products

Hamburg Commercial Bank AG, formerly known as HSH Nordbank AG, emerged in June 2003 from the merger of Hamburgische Landesbank Girozentrale with Landesbank Schleswig-Holstein Girozentrale. It is managed in the legal form of a corporation (*Aktiengesellschaft*). The Bank has its registered office in Hamburg and Kiel. In line with the process of focussed transformation, its registered office is to be located in Hamburg in the future.

Hamburg Commercial Bank is one of the leading banking partners for upper medium-sized companies in the core region of Northern Germany. The Bank is also active throughout Germany in the Real Estate, Project Finance, Corporate Clients, Shipping and Capital Markets & Products segments. In the project and real estate financing business, the focus is also on other European countries. The Bank conducts business with shipping clients throughout the world. Based on conventional loan financing, Hamburg Commercial Bank offers tailored products and individual financial solutions for its customers.

Segments, divisions and locations

The operating business activities of Hamburg Commercial Bank are divided into the Corporate Clients, Real Estate, Shipping and Treasury & Markets segments. In addition, the reporting date marks the last time the Bank is reporting on the results of the Non-Core Bank, in which the legacy portfolios, which have since been sold and are non-strategic and predominantly non-performing, were bundled. The administrative divisions and overall bank positions are disclosed as segments not subject to reporting requirements in the "Other and Consolidation" division.

The Bank has branches in Singapore, Athens and Luxembourg as well as a representative office in Hong Kong in line with its focused direction. In Germany, over and above the offices in Hamburg and Kiel, the Bank has offices in Berlin, Düsseldorf, Frankfurt am Main, Munich and Stuttgart.

The branches listed above are of secondary importance for understanding the Group situation.

Equity holdings and scope of consolidation

In addition to the parent company, the scope of consolidation for the Group financial statements comprised 32 fully consolidated subsidiaries as at the reporting date (31 December 2017: 53 fully consolidated subsidiaries). There were no additions compared with the previous year's reporting date. The company CAPCELLENCE Vintage Year 18 Beteiligungen GmbH & Co. KG, which was newly established during the year, was incorporated into a Group company during the year under review.

The decrease in the scope of consolidation by 21 subsidiaries is due to:

- The sale of the shares in FSL Holdings Pte. Ltd. in the first quarter of 2018 as part of the winding-down of legacy burdens. This sale also resulted in the companies FSL Asset Management Pte. Ltd. and FSL Trust Management Pte. Ltd. leaving the scope of consolidation.
- The liquidation of 2200 Victory LLC in the third quarter of 2018 and the liquidations of Castellum ABF S.A. and Stratus ABF S.A., which were used as refinancing vehicles, in the fourth quarter of 2018.
- The closing of the portfolio transaction in the fourth quarter of 2018, which led to a loss of control over a total of 15 subsidiaries. In addition to the investments in GODAN GmbH and Ilex Integra GmbH, this involved five single ship companies, four single-purpose companies from the aviation sector, the Life Insurance Group (three companies) and Senior Preferred Investments S.A.

The impact of these changes to the scope of consolidation on the statement of income is addressed, to the extent that the impact is material, in the "Earnings situation" section. Further details on the scope of consolidation can be found in Note 5 (Scope of consolidation) in the notes to the Group financial statements.

Shareholder structure

Following the sale of the Bank by HSH Beteiligungs Management GmbH (94.9 % of the shares) and the nine trusts initiated by J.C. Flowers & Co. LLC (5.1 % of the shares), Hamburg Commercial Bank has been owned since 28 November 2018 by renowned, globally active institutional private investors that have a high level of expertise in the banking business, in particular. The shareholder structure is as follows:

Ownership structure

Several funds initiated by **Cerberus Capital Management, L.P.**			One fund advised by **J.C. Flowers & Co. LLC**	One fund initiated by **GoldenTree Asset Management LP**	**Centaurus Capital LP**	**BAWAG P.S.K.** Bank für Arbeit und Wirtschaft und Österreichische Postsparkasse Aktiengesellschaft
Promontoria Holding 221 B.V. 9.89 %	Promontoria Holding 231 B.V. 13.88 %	Promontoria Holding 233 B.V. 18.73 %	JCF IV Neptun Holdings S.à r.l.	GoldenTree Asset Management Lux S.à r.l.	Chi Centauri LLC	
42.5 %			**35.0 %**	**12.5 %**	**7.5 %**	**2.5 %**

Restructuring of the Management Board and Supervisory Board

In the context of the Bank's privatisation, the following changes were made to the Management Board and Supervisory Board. Since 1 January 2019, the Management Board of Hamburg Commercial Bank has consisted of Stefan Ermisch (CEO), Ulrik Lackschewitz (CRO), Oliver Gatzke (CFO) and Nicolas Blanchard (CCO), who has been responsible for all client business and products since December 2018. At the same time, Torsten Temp, the long-standing Management Board member responsible for the Market divisions, resigned from his position at the end of 2018. Ulrik Lackschewitz is the Deputy Chair of the Management Board. Juan Rodríguez Inciarte has been the new Chair of the Supervisory Board since 28 November 2018.

Further information on the members of the boards is set out in Note 62 (Related companies and parties).

Deposit guarantee fund

With the successful closing of the privatisation process for HSH Nordbank AG on 28 November 2018, the legal requirements for Hamburg Commercial Bank's membership of the German Savings Bank Association (DSGV) ceased to apply and its membership subsequently expired (Section 5 of the DSGV Articles of Association).

Pursuant to the agreement concluded on the basis of Section 94 (4a) of the Framework Statute, membership of the guarantee scheme of the German Savings Banks Finance Group (SFG) will continue for a further three years until 31 December 2021. All issues of HSH Nordbank AG (excluding equity/instruments with equity characteristics, notably under paragraphs 41, 44 of the EU - Commission Communication 2013/C 216/01 of 30 July 2013 ("Banking Communication")) therefore continue to fall under the voluntary institutional protection of the guarantee fund of the Savings Banks Finance Group (Section 39 (1) of the Framework Statute) until 31 December 2021.

The German Savings Banks Finance Group has an institutional guarantee scheme: This scheme protects deposits held at a savings bank, Landesbank or a Landesbausparkasse. The objective of the protection scheme is to stabilise the member institutions and avert emerging or existing financial difficulties at these institutions. Under the voluntary institutional protection there is no legally binding entitlement to support measures vis-à-vis the protection scheme in the event of the occurrence of a guarantee case.

The seamless transition of Hamburg Commercial Bank to the deposit protection fund for private banks is planned for 1 January 2022. This deposit guarantee fund consists of the Compensation Scheme of German Banks ("EdB", statutory deposit guarantee fund") and the voluntary deposit protection fund of the Association of German Banks ("ESF"). The scope of ESF deposit guarantee fund is governed in particular by Section 6 of the Statute of the deposit guarantee fund.

Hamburg Commercial Bank will be admitted to the EdB as of 1 January 2022 on the basis of the German Deposit Protection Act (EinSiG) by way of a referral by BaFin. The inclusion of Hamburg Commercial Bank in the ESF on 1 January 2022 presupposes the Bank to meet the requirements, as set out in the Statute, for participation in the ESF at the end of 2021. If this is the case, the Bank, like all other banks, will in principle contribute to the ESF based on the maximum deposit guarantee per depositor set out in the Statute, corresponding to 15 % of the Bank's regulatory capital. From as early as 1 January 2019, the Auditing Association of German Banks (*Prüfungsverband deutscher Banken e.V.*) will support Hamburg Commercial Bank during the three-year transition period.

This procedure, which has been agreed with the German Savings Banks Finance Group and the Association of German Banks (*Bundesverband deutscher Banken*), ensures continuity in the security of deposits at Hamburg Commercial Bank.

External influencing factors and processes

The following aspects are of particular relevance to Hamburg Commercial Bank's business: The development of the economy and the financial markets (including interest rate levels, EUR/USD exchange rate changes), developments in the relevant sectors such as the real estate market and shipping, regulatory requirements and discretionary decisions by the supervisory authorities, assessments by rating agencies and capital market participants and other stakeholders, such as the ESF, as well as the further development of the transformation process.

The Bank has defined processes within its business organisation that form the basis for operating and managing the Bank as well as for its internal control system. The main processes include strategy and planning, corporate management, customer management, financing, capital markets as well as support processes.

Objectives and strategy

Hamburg Commercial Bank is committed to clarity; in line with the Hanseatic tradition, the now privatised commercial bank makes clear, binding commitments and grows together with its clients in the long term. The Bank is committed to its clients and stands for reliability and honesty. Its actions are straightforward, decisive and precise. Central to this perceived role is a focussed and entrepreneurial approach that creates added value for clients, society, shareholders, and the Bank and its employees.

The Bank's overarching objective is to slowly but surely continue to develop its business model, which is anchored in northern Germany, and to consolidate its market position in the German banking market. In view of the demands placed on the Bank by a rapidly changing banking environment, the Bank is focusing on its transformation in order to achieve a sustainable and agile corporate structure. This will be based on a cost-effective and, at the same time, needs-based service and product portfolio that concentrates on competitive areas and is continuously optimised in line with client needs.

Based on its mission statement, in which the objectives, strategy, purpose and values are combined in an appropriate framework, Hamburg Commercial Bank's strategy architecture includes the following central components:

Strategy architecture

The Strategic Risk Framework (SRF) describes the focus of risk management and forms the foundation for the Bank's risk culture. As a consistent guideline, it effectively brings the organisation and business operations into line with the key risk strategy principles. Details on the SRF and the bank-specific risk types are explained in the Risk report.

The business strategy is defined by the Management Board and describes the overriding strategic direction with regard to the business model and business area portfolio. This transforms the mission statement into a concrete strategy. It describes the objectives for each key business activity and the measures to be taken to achieve these objectives.

Taking into account the business strategy, a consistent risk strategy is defined on the basis of the SRF. This takes into account the development of key business activities, including risk strategy guidelines and liquidity aspects.

The funding strategy provides the framework for the refinancing of Hamburg Commercial Bank. It is a core component of the Bank's business strategy. As part of the definition process, the requirements regarding liquidity resources are geared towards sustainability to ensure that regulatory and rating requirements are met at all times. Risk and liquidity management is geared towards the gradual optimisation of the liabilities side, taking profitability requirements into account.

Further functional strategies are defined for the Bank's core business strategies.

The stated objectives and strategies are basically aimed at ensuring the Bank's sustainable development. When it comes to defining and implementing them, the Bank's employees use fundamental rules of conduct summarised in the "Code of Conduct" as a guide. The "Code of Conduct" is a binding code of behaviour. As a normative basis, it provides employees with reliable guidance for responsible action that meets the statutory requirements, but also ethical and social standards. This allows economic, ecological and social aspects to be taken into account in a balanced way. The combined separate non-financial report (pursuant to Sections 315b, 315c in conjunction with Sections 289b to 289e HGB) is available on the Bank's website at https://www.hcob-bank.com/groupreporting and is not part of this combined management report.

Realignment of the Bank

The Bank is undergoing a profound and extensive process of transformation spanning a period of several years. Its objective is to establish a business model that is client-focused and competitive in the long run. Now that the privatisation process has taken pressure off the Bank's balance sheet structure, in particular, the activities of the now privatised Hamburg Commercial Bank will focus on increasing profitability and general efficiency.

The focus is on the strategic vision, which is characterised in particular by a profitable and competitive product range, as well as efficient structures and processes. The realignment process will be based on existing customer relationships and business areas, which are being further developed in line with Hamburg Commercial Bank's principles and, following the abolition of the EU restrictions, are being carefully expanded and also selectively internationalised in some cases.

The Bank is bundling its efficiency and earnings enhancement activities in a cross-bank transformation project. The measures focus on five key areas: Development of profitable and risk-oriented growth strategies ("Go-To-Market"), strict focus on profitability and earnings ("Portfolio Management"), diversification and optimisation of the funding structure ("Liability Optimisation"), consistent cost management as well as moves to boost efficiency ("Operating Efficiency") and optimisation of the organisational structure ("Organisational Vitality"). A Transformation Office with a corresponding structure that falls under the direct responsibility of the CEO has been established. The stringent project structure ensures consistent development and rapid implementation of the individual measures. In general, the operating business model will be streamlined considerably in line with the risk-relieved structure. The reduction of complexity in processes and products, as well as in the organisational structure, in particular after the conclusion of the EU proceedings and the fact that the Bank has now been relieved of the Non-Core Bank, offers considerable potential.

The strategic realignment is being combined with digital transformation. The focus in this regard is on the development of digitalised value-adding processes focusing on clients, products, internal business processes and corporate culture. The Bank is pursuing a holistic and systematic approach with the aim of developing client groups and markets more efficiently in the future. This will also allow processes to be streamlined on the basis of increasing automation, allowing further efficiency gains to be achieved.

Digitisation also plays a central role when it comes to matters relating to customer relations. On the basis of the digitalisation strategy that has been adopted, several courses of action are being implemented in parallel, starting from the client perspective. The aim is to bring the acquisition and sales process, client onboarding, digital collaboration with clients and also back office processes into line with cutting-edge digital developments, substantially improving their competitiveness in the process. With regard to the selected fields of action, the Bank is focusing on a manageable number of key issues, the implementation of which is being driven forward in an agile and cross-sectoral manner.

The Bank's competitive realignment in the long term is characterised by solid financial key figures. In this respect, the Bank has defined a strategic target vision. It is characterised by a CET1 capital ratio of at least 16 %, an NPE ratio of a maximum of 2 %, a cost-income ratio of a maximum of 40 % and a pre-tax profitability of above 8 %. All strategic measures in the transformation process will be brought into line with this objective, which is to be achieved in full by 2022 at the latest.

Strategic direction for the business areas

The divisions are being developed on an ongoing basis and their business portfolios and positioning are being adjusted to reflect the changing underlying conditions in the market and competitive environment. In line with its strategic objectives, Hamburg Commercial Bank wants its business portfolio to meet stringent return requirements.

In addition to its business in Germany, the Bank is planning to carefully drive the expansion of its activities outside of Germany and across Europe for selected projects and sectors in the interests of ensuring a balanced portfolio structure. In addition, product sales will be optimised and adapted further to create a competitive offering.

In the **Corporate Clients** segment, the Bank will continue to pursue the approach of gearing business to segment-specific return and risk requirements nationwide. At the same time, the potential in the core region of northern Germany as well as in the project financing business in the Energy & Utilities and Logistics & Infrastructure business areas abroad is to be exploited in a focused manner. In particular with regard to the business with German corporates, market access is being enhanced further by way of digitisation strategies.

The **Real Estate Clients** division will continue to make a risk-conscious contribution to the Bank's portfolio mix taking account of the development in the German real estate markets. The profitability of transactions is the major driver for the sustained improvement in the Bank's risk/return profile. In the future, the Bank aims to cautiously expand its international activities with its existing established, internationally active clients, focusing on European metropolitan regions.

In the **Shipping** division, the Bank is still aiming to selectively conclude additional new business as a strategic partner based on its long-standing expertise and in accordance with strict margin and risk requirements. The focus is on the diversification of the portfolio through domestic and international commitments with counterparties with a good credit standing.

The **Treasury & Markets** division includes the operational treasury function and, in Markets, the Bank's capital market and capital market-related client business. Operational treasury implements the central management of the liquidity and market price risks associated with the Bank's positions, as well as the management of the cover pool, in consultation with Bank Management. Responsibility for liquidity management and the Bank's issuance activities is also anchored in this division. Markets stands for trading with capital market and investment products, syndication as well as the corresponding sales activities and the provision of support to savings banks, banks and insurance companies.

The customer departments are supported by products and services provided by the Treasury & Markets, Transaction Banking and Structured Finance divisions in order are to ensure a holistic offering.

Management system

Key value drivers and ratio system

The Bank's integrated management system is aimed at the targeted management of key value drivers – profitability/income, efficiency/costs, capital, liquidity and risk – in line with the statutory requirements (SREP, BCBS 239) and the SRF. The Bank uses a risk-adjusted key indicator and ratio system for this purpose that ensures that the Bank is managed in a uniform and effective manner. The Bank is managed mainly on the basis of figures for the Group prepared in accordance with the International Financial Reporting Standards (IFRS)/the relevant prudential rules and also takes the risk limits and guidelines defined in the SRF into account.

In addition, a multi-level contribution margin accounting system is also used to manage the individual business areas. Other components of the Overall bank management system are the annual strategy and planning process, plan/actual comparisons and targets agreement and assessment process. Further information on management is included in the Risk report under "Risk management by central committee structure" and "Risk reporting and measurement systems".

Management indicators of the IFRS Group

The Bank's internal control system is based on key management indicators relating to the individual value drivers of the IFRS Group. In the Bank's external reporting, the development of these indicators is compared, on the one hand, against the previous year and the prior-year forecast ("Economic report" section). On the other hand, their expected development in 2019 and the strategic objectives for 2022 are also described ("Forecast, opportunities and risks report" section).

Compared with the previous year, changes have arisen with regard to the most important key management indicators, in particular as a result of privatisation. With the sale of the non-performing loans as part of the portfolio transaction and the termination of the second loss guarantee, significant risk relief was achieved for the Bank's balance sheet, together with an improvement in the capital structure. Against this backdrop, the Bank is streamlining the most important key management indicators and will focus, on the future, on the development of the key management indicators in line with its strategic objectives. The key management indicators thus comprise the RoE, the CIR, the CET1 ratio, the NPE ratio, the LCR and the rating. Following the implementation of the portfolio transaction and the associated disposal of the assets allocated to the Non-Core Bank, it is no longer opportune to look at these indicators on a segment-by-segment basis. As a result, the Bank will report on the development of the key management indicators at Group level as it moves to achieving the strategic objectives. Hamburg Commercial Bank's integrated management system ensures a comprehensive view of the key value drivers to an adequate extent. The most important key management indicators are defined as follows:

Definition of the most important key management indicators

Financial key management indicators	
RoE (Return on Equity)	RoE is calculated as the ratio of income before taxes to average equity capital disclosed on the balance sheet and shows the return on capital. The risk-adjusted allocation of the average equity capital disclosed on the balance sheet is determined on the basis of the regulatory capital committed.
CIR (Cost-Income Ratio)	The CIR is a cost efficiency ratio that measures administrative expenses as a percentage of total income plus other operating income.
CET1 Ratio (Common Equity Tier 1) phase-in, in-period[1]	The CET1 ratio is defined as the quotient of the core Tier 1 capital excluding hybrid instruments and the sum of the risk-weighted assets, expressed as a percentage. The CET1 ratio is determined in the same period calculation (i.e. taking the Group financial statements into account) in accordance with the transitional rules (phase-in) of the Capital Requirements Regulation (CRR).
NPE Ratio (Non Performing Exposure)	The NPE ratio measures the sum of the risk positions (EaD, exposure at default) of borrowers in default as a percentage of the sum of the Bank's risk positions.
LCR (Liquidity Coverage Ratio)	The LCR represents the security provided to the Bank in the event of a short-term acute liquidity stress scenario of more than 30 days by maintaining a liquidity buffer (short-term stress test ratio). The LCR is calculated as the ratio of highly liquid assets to net cash outflows over the next 30 days. It is calculated at Group level for the purposes of internal control. The LCR is calculated without taking the institutional protection into account, i.e. taking into account the limit on the deposit guarantee for client deposits of € 100,000 per client.
Non-financial key management indicators	
Rating	Credit ratings awarded by the rating agencies in relation to the issuer rating (long-term).

[1] The regulatory CET1 ratio, which is calculated on a "not in-period" basis, can be found in the Risk report.

The extent of the indicators used at Hamburg Commercial Bank for managing the overall bank goes far beyond the important management indicators listed in this section and includes many other supporting key performance indicators, which are used by management for the purposes of managing and allocating financial resources in an effective and integrated manner. Further details regarding the key figures and ratios used for risk management are set out in the Risk report.

Hamburg Commercial Bank also updated and refined its recovery/resolution plans in accordance with the statutory requirements. The recovery and early warning indicators defined in the German Recovery and Resolution Act (Sanierungs- und Abwicklungsgesetz, SAG) and by the EBA (European Banking Authority) are regularly monitored and assessed in order to be able, where necessary, to implement targeted measures on a timely basis.

Economic report

Underlying economic and industry conditions

Global economy loses momentum, high level of volatility on the financial markets

The global economy lost some of its momentum in 2018 compared with the previous year. Following growth of 3.8 % in 2017, it is likely to have expanded by 3.7 %. The decisive factors behind this less dynamic growth are the economic cycle, which is already well advanced in many countries, as well as a number of risk factors that have led to mounting uncertainty. On the one hand, there are the trade disputes, especially between the US and China, which have torn value chains apart at the expense of growth. On the other hand, the negotiations for a Brexit agreement between the EU and the United Kingdom have been very tough, which has significantly increased the risk of a hard Brexit. There were also other trouble spots to deal with - such as the currency crisis in Turkey or the budget dispute between the EU and Italy.

The international financial markets did not escape these conflicts unscathed. The stock markets suffered noticeable losses in the year under review, while interest rates in the eurozone - measured against ten-year German government bonds - fell again. Their US counterparts were able to close 2018 with moderately higher yield levels compared with the beginning of the year on balance - after what were significant increases at times. The US dollar has been able to appreciate significantly against the euro as a "safe haven".

Recent increase in economic risks

The US grew at a comparatively fast pace in 2018. In particular, the tax relief for companies passed by the US government at the end of 2017 had a stimulating effect. Growth in 2018 should therefore have accelerated further from 2.2 % in the previous year to just under 3 %. Compared with the previous quarters, however, GDP growth is likely to be somewhat lower at the end of the year, as some economic indicators are sending out the first few signals of a slowdown. The economic situation is still very robust, however, which is underscored by a very low unemployment rate of 4.0 %.

After China was able to expand at a slightly faster pace in 2017, the rate of expansion is likely to have slowed to 6.6 % in the year under review. In particular, the trade disputes with the US are putting the brakes on economic activity. Although the Chinese administration is trying to counteract this by taking both monetary and fiscal policy measures, the effect cannot be completely mitigated. Emerging markets in particular were affected by the stronger US dollar, rising US dollar interest rates and fears of a trade war, with Argentina, Turkey and South Africa in particular suffering hefty currency losses due to high current account deficits and/or political instability.

Compared with 2017, economic momentum in the eurozone slowed noticeably in the year under review. After 2.4 % in the previous year, 2018 is expected to bring growth of 1.8 %. Hopes of stabilisation in the summer failed to materialise. On the contrary, economic indicators have cooled further, meaning that the second half of the year was somewhat weaker than the first. This development was corroborated by the ongoing protests staged by the "yellow vests" against the reform policy in France, the paralysing Italian budget dispute with the EU and the fact that the automotive industry in Germany which was put out of action due to a one-off effect (the unsuccessful introduction of a new exhaust test procedure in the automotive industry). But it is not only this particular one-off effect, which led to a GDP contraction of 0.2 % in the third quarter of 2018 as against the previous quarter, that is putting pressure on the German economy. Trade disputes via third countries would also appear to be having a greater impact on the export-oriented economy than expected. There was no rebound in the fourth quarter of 2018, with the economy stagnating instead. At 1.5 %, total GDP growth in 2018 was significantly lower than in 2017 (2.2 % before adjustments for calendar effects).

ECB puts an end to its asset purchases, uncertainty sends the stock markets south and the bond markets reap the benefits

In 2018, the ECB took the first few steps towards normalising its monetary policy, gradually reducing its net asset purchases over the course of the year and discontinuing them completely at the end of the year. Maturing bonds will, however, continue to be reinvested in the capital market. The cautious stance taken by the central bank with regard to tightening monetary policy and the high level of uncertainty among investors once again benefited long-term German government bonds in 2018 overall. Their yields fell below 30 basis points at the end of the year.

In 2018, the US Federal Reserve systematically continued with its policy of interest rate hikes, lifting the key interest rate by 0.25 percentage points each quarter, meaning that the Fed Funds Rate currently lies within the target range of 2.25 % to 2.50 %. At the same time, the US Fed is steadily and gradually reducing its total assets by reinvesting only part of the maturing bonds on its balance sheet. The Fed's interest rate hikes have boosted Treasury yields, but in view of the uncertainty caused by the trade conflict, yields on long-term US government bonds have risen to a lesser extent than short-term yields, meaning that the yield curve has flattened considerably. The difference between the yields on ten-year and two-year T-notes briefly touched on a low of eleven basis points.

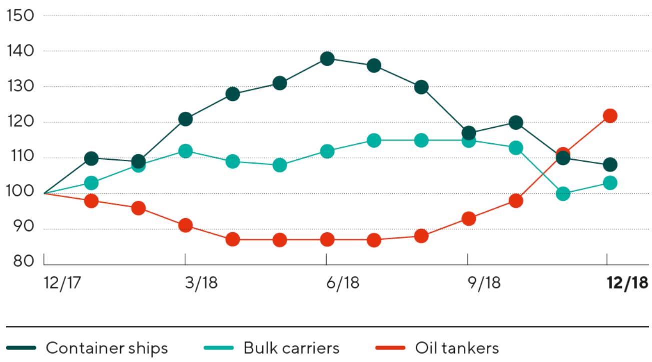
International stock markets came under considerable pressure in 2018 following solid performance in the previous year. At the beginning of the year, the German stock market (Dax) initially reached a level of more than 13,500 points, before falling considerably to below 10,500 points by the end of the year. Over the year as a whole, this equates to significant losses of around 18 %. The Euro Stoxx 50 was also hit by losses. With losses of 14 %, however, the result was not quite as negative as for the Dax. The US stock market fared somewhat better, meaning that the Dow Jones fell by only 6 % in 2018. At the beginning of the year, the euro was still trading well above 1.20 against the US dollar on the currency market, before the euro lost significant ground due to the economic slowdown in the eurozone and the trade disputes, particularly in May, only achieving lower levels against the US dollar for the remainder of the year. At the end of the year, the currency pair was trading at 1.14.

Development in relevant markets still encouraging overall

The **shipping markets** were volatile in the year under review and showed uneven development. Despite setbacks in the second half of the year, the market for container vessels and bulkers continued on a positive trajectory overall. On the oil tanker market, however, charter rates continued to decline before a boom set in at the end of the year.

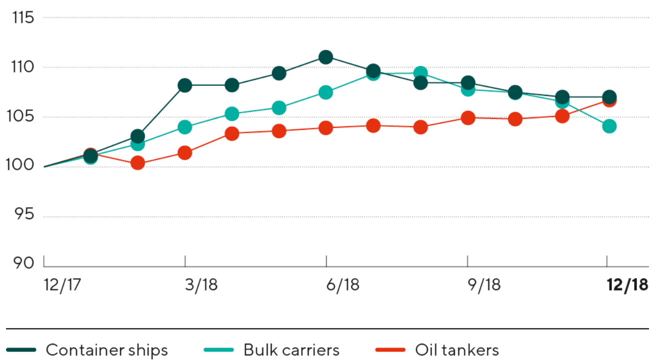
Time charter rates

(Indexed market average, 12/2017=100)



Secondhand prices

(Indexed market average, 12/2017=100)



In the market for **container vessels**, the recovery of charter rates up until mid-2018 was followed by a phase of weakness in the second half of the year. Second-hand prices followed the pattern set by charter rates with lower volatility. Demand for container transport showed robust development in line with the good macroeconomic environment, although growth had already started to slow. The uncertainty caused by import tariffs that had come into force, the threat of trade conflicts coming to a head and problems in a number of emerging markets had a corresponding impact.

On the supply side, fleet growth accelerated significantly again compared with 2017. The number of deliveries remained high, while only a few ships were scrapped. Despite consolidation, the shipping line companies are still fighting hard for market share, but recently stepped up their efforts to tighten capacity management, which increased the number of laid-up vessels at the end of the year.

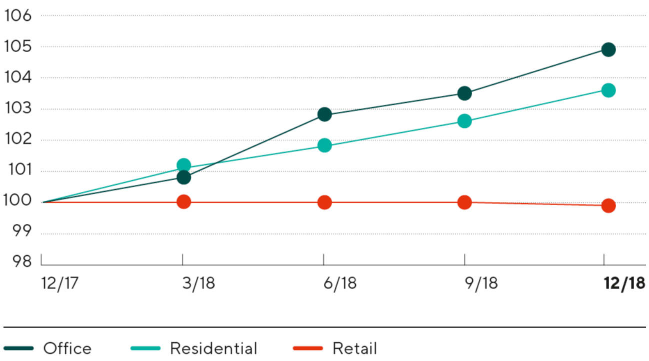
As far as **bulkers** are concerned, the upward trend continued in 2018. The last quarter of the year, however, saw a setback in charter rates and a weaker trend in second-hand prices. In particular, the rates for the large Capesize ships fell significantly of late – just like Chinese imports of coal and iron ore. Overall, however, demand for transport showed robust development. Although trade restrictions with the US led to shifts in trade flows, this ultimately did not have any negative impact on the volumes transported. Another positive factor for the market was the fact that the fleet of bulker grew at only a moderate pace, with relatively few new ships being delivered.

Charter rates for **oil tankers** had stabilised at a low level after a weak first quarter of 2018. At the end of the year, there was a genuine rally to the highest level seen in two years. The increase in second-hand prices, which had been cautious in the past, also accelerated noticeably. The main reason for this was the fluctuating oil production within "OPEC+" (consisting of the fifteen member countries of the "Organisation of Petroleum Exporting Countries (OPEC)" and ten cooperating states, including Russia). In October and November, production was upped significantly before a decision was taken to cut it back again. US crude oil exports, on the other hand, rose steadily. The strong scrapping activity, especially in the first half of the year, also brought relief, meaning that fleet growth almost came to a complete standstill in a year-on-year comparison.

The trends in the German **real estate markets** were once again predominantly positive in 2018. Rents and property prices continued to rise, particularly on the residential and office property markets in the country's major cities, with the latter rising at a faster rate. Not least thanks to the persistently low interest rates, real estate remained an attractive investment alternative for investors, although the return advantage is now becoming much less pronounced.

Rents

(Indexed market average, 12/2017=100)



Construction activity picked up considerable speed in 2018, especially for commercial real estate. In the **residential real estate** sector, the number of building permits for multi-storey residential buildings increased, while the number of building permits for owner-occupied houses dropped. This means that in the country's large cities, the supply of housing is moving in line with demand, which remains high. Nevertheless, the markets in Germany's major cities remained characterised by excess demand, while the rent restrictions imposed on apartments proved largely ineffective, with the result that rents rose significantly in almost all cities. For the first time in four years, however, the pace of growth slowed noticeably.

On the **office property markets**, net demand for space continued to rise thanks to the positive labour market situation and continued expansion initiatives by companies renting space. Although office completions increased significantly, they were not sufficient to meet the high demand. Vacancies fell for the eighth year in a row, even dropping below the fluctuation reserve in some major cities, mainly in Berlin and Munich. This caused rents in all major cities to rise sharply in some cases, primarily in Berlin. It was not uncommon for increases in peripheral locations and locations on the outskirts to exceed those in the top locations.

On the **retail property markets**, on the other hand, even rents in the prime inner-city locations of the largest conurbations stagnated, while they declined slightly in medium-sized and small cities. This is not least due to the ongoing structural change in stationary retailing in favour of online retailing, which is putting pressure on the demand for rental space among retailers, especially in the non-food sector. Rents were noticeably more resistant in city districts where the local food supply is located, an area that has barely felt any competition from online trading so far.

In many large cities, rents in these secondary locations rose at least at a moderate pace. The market values of commercial properties and retail parks, in particular, increased significantly despite the lack of or modest growth in rents. On the other hand, shopping centres recorded slight losses in value.

On the **European office property markets**, the number of emerging markets increased significantly in 2018. Thanks to what is often still positive economic development overall, vacant space fell in many large cities, meaning that rents rose sharply in some cases, especially in Scandinavia, France and Spain. A high vacancy rate only translated into slower rental growth on a small number of markets. On the office property market in London, demand for space weakened in the course of the year, although it was still sufficient to reduce vacancies somewhat. In anticipation of the unforeseeable consequences of the United Kingdom’s withdrawal from the European Union in 2019, however, rents did not increase. They stagnated, as did market values, which bears testimony to the cautious approach adopted by investors. In the vast majority of cities in the rest of Europe, on the other hand, office real estate reported increasing values, and in some cases even strong growth, such as in the Netherlands and Scandinavia.

Although production growth in the German **manufacturing sector** was still noticeably higher than in the same period of the previous year in the first eleven months of 2018, it slowed in the course of the year. With the exception of the automotive industry and energy supply, the main sectors showed positive development, albeit to varying degrees.

Following a record year in 2017, **wholesale** companies recorded a further increase in sales at the beginning of 2018 compared with the same period of the previous year, although growth momentum slowed significantly as the year progressed. The **retail sector** is still benefiting from consumer-driven economic growth in Germany and also recorded a positive sales trend in 2018, although the growth momentum has weakened compared to the previous year.

The **health market** is growing constantly, including the hospital market, as a result of demographic trends and medical advances. The financial situation of many hospitals remains strained despite increasing revenues. The profitability of hospitals is, however, expected to increase in the medium term thanks to the entry into force of the Hospital Structure Act (Krankenhausstrukturgesetz) at the beginning of 2016.

In the **logistics sector**, sales in 2018 (in real terms) continued to show strong development, but at a slightly slower pace than in the same period of the previous year. The measured economic climate remains above the long-term average in the third quarter of 2018, meaning that it is still in expansive territory overall.

After a weak start to the year, the global **project financing volume** remained stable at the previous year's level in the first three quarters of 2018 and was down by only 0.1 % on the volume for the same period of the previous year. While the project financing volume in the Americas increased significantly year-on-year (+43.8 %), the financing volume in the "Europe, Middle East and Africa" (EMEA) region declined slightly (-4 %), with a sharp decline in the Asian region (-27.1 %).

Investments in **transport infrastructure** were relatively stable and accounted for 25 % of the project financing volume in the EMEA region in the first three quarters of 2018 (2017: 18 %). The major institutional investors include pension funds and insurance companies, which consider infrastructure investments to be a supplementary investment alternative in the low interest rate environment.

The expansion of **renewable energies** made further progress in the course of 2018, both in Europe and in Germany, although developments varied considerably: The changeover to the bidding procedures implemented in connection with the amendment to the Renewable Energies Act (EEG) had led to an increase in demand for the transitional year of 2017, especially in Germany, and has now led to the expected significant slowdown in 2018. The gross capacity increase in the onshore wind energy segment was 50 % lower than in the same period of the previous year.

The expansion in the solar segment continued in Europe. In Germany alone, new installations in the photovoltaics segment came to around 2,960 megawatts in 2018, up considerably on the prior-year value of 1,750 megawatts. The political target corridor of 2,500 megawatts of new photovoltaic output a year, which was clearly missed in previous years not least due to the cuts under the Renewable Energies Act (EEG), has thus been exceeded again for the first time since 2013.

Banking market faced with weak profitability, consolidation pressure and strategic realignment

The macroeconomic and monetary policy uncertainties were reflected in increasing risks in the banking environment over the course of the year, which were reflected not least in the share prices of banks on both sides of the Atlantic. US banks, however, once again outperformed their European and, in particular, their German counterparts by far. Key issues in Europe included the risks resulting from Brexit and – as in previous years – the stability of Italian banks. Measured based on the respective indices, European and German financial institutions both showed much weaker performance than the market as a whole. At the same time, although interest rates remained at a low level, bank funding spreads increased significantly in the course of the year against the backdrop of mounting uncertainty.

In view of these developments, the issues that are all too familiar in the European banking market are becoming more urgent than ever. German banks, in particular, which have come bottom of the European ranking list in terms of profitability for some time now, are being called upon to review their strategic orientation. This is because the high pressure on margins, which also places tight constraints on the ability to retain profits, increasingly harbours the risk of loan financing not being priced in a risk-commensurate manner. In addition, the expansion of non-banks, mainly FinTechs, is creating additional competitive pressure. At the same time, the need for investments in the future viability of institutions are leaving their mark on the cost side in the form of high project and IT costs. Against this backdrop, many banks, in addition to focusing their business models, initiated comprehensive cost and efficiency programmes in order to be able to generate adequate returns on a sustainable basis. It is clear that conventional moves to cut costs alone are not enough to improve profitability in the long term. Rather, the aim is to ensure that business models are the best possible fit for client profiles, to exploit the potential of digital technologies and to develop a forward-looking corporate culture.

At the same time, financial investors, in particular, would also appear to be expressing more of an interest in playing an active role in the existing consolidation process, particularly in Germany. After all, from an investor perspective, the challenging market environment resulting from the low interest rates, weak earnings and intense competition creates not only risks, but also opportunities that can be exploited by ongoing consolidation. This applies both to the purchase of problem loan portfolios, as well as to takeovers of smaller and medium-sized institutions. All in all, these solutions have the potential to strengthen the German banking market and accelerate the process of transformation in the future.

Fresh impetus for future bank financing conditions came from the legislator and the rating agencies. While a decision had already been made back in November 2017 to harmonise the European regulations regarding the design of the national liability cascades within the context of the BRRD for MREL-eligible liabilities (Minimum Requirements for Eligible Liabilities), the regulations were transposed into German law at the end of July 2018. The arrangement provides for the introduction of a new class of instruments, non-preferred senior unsecured liabilities, which can count towards the requirements for bank MREL ratios, meaning that they contribute to the liability buffers in the event of insolvency. In Germany, the new regulations led to an extensive rating operation performed by Moody's with regard to the existing German senior unsecured liabilities, which, unless they contain structured components, were transferred to the liability class of senior non-preferred liabilities.

Underlying conditions influence Hamburg Commercial Bank's business

The highly competitive environment, which remains challenging for banks, was also reflected in Hamburg Commercial Bank's business performance. Trends in the markets relevant for the Bank remained encouraging overall. The real estate environment in Germany, for example, remained largely positive. The situation on the shipping markets was volatile but still satisfactory overall. In the Corporate Clients division, however, the solid liquidity base of clients and the low level of interest rates still had a tangible impact in an environment that remained competitive. In view of these market developments, the development in the volume of new business concluded painted a mixed picture. Margin development remains under pressure due to the intense competition. Nevertheless, thanks to its strict focus on earnings, the Bank succeeded in significantly increasing new business margins compared with the previous year, partially escaping price competition as a result.

The first-time adoption of the new accounting standard IFRS 9 on 1 January 2018 only had a minor impact on the capital position of Hamburg Commercial Bank at Group level, as was the case at most German banks. The Bank is responding to the ongoing challenge of maintaining a cost base that is commensurate with the market environment by implementing cost-cutting measures consistently and systematically, most recently as part of the transformation project that has been implemented. In this way, the Bank is also countering the cost increases triggered by a large number of new regulatory requirements and laying the foundation for a streamlined and efficient privatised bank.

The Bank's business performance and position are explained in detail in the following sections.

Business development – Significant developments and events in the 2018 reporting year

Successful completion of privatisation and completion of EU state aid proceedings

The privatisation process was successfully completed on 28 November 2018 after the Bank secured both regulatory approval and the European Commission's approval of the acquisition following a viability review of the new corporate structure. The sale of the Bank to renowned private investors marks the end of the long-standing EU state aid proceedings, which resulted in far-reaching structural relief. The privatised bank has changed its name and has been operating under the name Hamburg Commercial Bank since 4 February 2019. This marks the completion of the first privatisation of a Landesbank in Germany. The privatisation lays a solid foundation for the next stage in the forward-looking transformation process, during which the Bank will gradually be developed into an agile commercial bank with an appropriate level of profitability and a business model that is sustainable in the long run.

Significant structural improvements in risk and capital structure achieved

In light of the future viability of the Bank and the good portfolio quality that it is aiming to achieve in this regard, largely non-performing portfolios consisting mainly of ship financing in an amount of € 6.3 billion (EaD) were sold to a special-purpose entity (SPE) from the sphere of the investors (the portfolio transaction) on 28 February 2018 within the context of the privatisation process (signing). The sale largely relieved the Bank of non-performing legacy loans and the NPE ratio fell significantly as a result. The closing of the portfolio transaction was subject to a condition precedent and was finalised immediately after the sale of the shares on 29 November 2018.

In addition, an agreement was reached with the guarantor HSH Finanzfonds AöR and HSH Beteiligungs Management GmbH on the premature termination of the second loss guarantee in return for a compensation payment of € -100 million as part of the privatisation process. With the closing of the share purchase agreement on 28 November 2018, the guarantee agreement was also cancelled accordingly. Within this context, the guarantor made payments that were still outstanding which, together with the loss compensation already paid for defaulted loans in 2018, amounted to approximately € -6.2 billion.

Seamless transition agreed from the guarantee scheme of the German Savings Banks Finance Group to the guarantee scheme for private banks

One of the central conditions for the sale of the Bank was the extension of the full membership of the guarantee scheme of the German Savings Banks Finance Group (SFG) for three further years after the conclusion of the share purchase agreement, and the associated seamless transition of the Bank to the guarantee scheme for private banks. In June 2018, the German Savings Banks Association (DSGV) amended its Articles of Association, opening up the fundamental option for the Bank to extend its membership of the guarantee scheme of the German Savings Banks Finance Group for an additional third year after closing. At the same time, the Bank applied for admission to the guarantee scheme of private banks (BdB). After protracted and complex negotiations, an agreement on the Bank's seamless transition was finally reached in October 2018. Accordingly, in November 2018, the BdB approved the seamless transition to full membership of the deposit guarantee fund (ESF) as of 1 January 2022. The Bank's admission was tied to clear conditions, which are also reflected in the Bank's strategic objectives and are aimed in particular at the successful implementation of the transformation process.

Extensive transformation process implemented

The completed privatisation process paves the way for the transformation process, which is intended to lead the Bank to efficiency and higher profitability in the long turn after the focus of late was on winding down extensive legacy burdens and, as a result, securing the Bank's continued survival. In view of the persistently challenging banking environment, which is characterised by intense competition and increasingly more demanding regulatory requirements, a stringent and sustained increase in efficiency, taking feasible digitisation initiatives into account, is an absolute must.

The Bank had already launched corresponding activities in the first quarter of 2018, and a cross-bank transformation project has since been implemented. The packages of measures covers five key areas and relates to fundamental aspects of the profound transformation. The primary objectives are to develop profitable, needs-based and risk-oriented new business strategies, to make existing portfolios profitable, to simplify and optimise the product and process structure, to diversify the Bank's funding structure and to establish a more performance-oriented and agile corporate culture.

The idea is that these measures will allow the Bank to achieve its strategic objectives and, at the same time, comply with the agreements reached with the BdB. The strong commitment of the new owners, whose primary objective is to establish an optimised and sustainable business model in the long term, provides additional security in the implementation of the transformation process.

Satisfactory group development overall influenced by one-off effects

The Bank achieved its main operational targets and exceeded them in some respects, taking special factors into account. The Bank continued to implement the cost reduction programme that has been in place since 2014 in a stringent manner and in line with its planning. As a result, administrative expenses fell significantly (-16 %) compared with the previous year. As far as new business activities are concerned, developments were mixed. In this highly competitive environment, the Bank selects new business based on strict risk and return requirements. The development in new business margins during the reporting period shows that the systematic focus on return is already bearing considerable fruit. New business profitability is also in line with the current ambition level. At the same time, receivables are lagging behind expectations. All in all, the new business volume is moderately below the projected value. While the Bank deliberately slowed down the dynamics of the mediumsized corporates business in the face of competitive pressure on margins, activities in the Real Estate and Shipping segments developed satisfactorily. The central earnings and cost ratios were, however, also influenced by one-off effects. These include both positive effects, which are reflected in the high net income from hybrid financial instruments, and effects with a pronounced negative impact, which mainly relate to expenses for privatisation and restructuring, as well as loan loss provisions. Further details on the development of key management indicators are provided in the chapters below.

Earnings, net assets and financial position

Group key management indicators	2017	2018 forecast	2018
Net income before taxes (€ m)	-453	Loss before taxes of around € -100 million	97
RoE (%)	-9.7	Negative due to expected loss	2.2
CIR (%)[1]	30.7	Increase despite lower cost base, as ratio was positively overstated in 2017	27.2
NPE ratio (%)	10.4	Around 2 %	2.0
NPE Coverage Ratio AC (%)[2]	63.8	Remains at the good level seen in 2017	61.0
CET1 capital ratio (%) (in-period)[3]	15.4	Clearly above SREP requirements	18.5
LCR (%)	169	Constant compared to 2017 year-end	225
NSFR (%)	114	Constant compared to 2017 year-end	121

[1] Following change in presentation according to Note 3 paragraph B).

[2] The calculation of the coverage ratio has changed since the introduction of IFRS 9 and is therefore defined as the ratio of specific loan loss provisions on defaulted loans measured at amortised cost (AC) and the exposure at default (EaD) of these defaulted loans (NPE). For comparison purposes, the value as at 31 December 2017 has been adjusted pro forma.

[3] From March 2018, the capital ratios will no longer be shown taking into account the regulatory relief effect of the federal state guarantee. To enable a comparison with the key capital figures as at December 2018, pro forma ratios are shown as at 31 December 2017. "Pro forma" means that, for the items included in the reference portfolio for the second loss guarantee, the RWA are recognised in line with the credit risk rules and not in line with the rules regarding securitisation. Within this context, valuation allowances that have been set up are still recognised in a manner that reduces the capital requirements in line with the regulatory requirements.

Satisfactory group development influenced by one-off effects

The following aspects, in particular, contributed to the satisfactory business development overall:

- **Net income before taxes** showed significantly positive development compared with the expected loss. On the one hand, this was thanks to satisfactory operating performance overall. Net operating interest income was moderately above expectations. While the average interest-bearing receivables portfolio increased slightly, gross new business, which also includes the volume earmarked for syndication, was slightly down on the previous year at € 8.4 billion (€ 8.6 billion). On the other hand, one-off effects also had a significant impact on the net result. The revaluation of hybrid instruments contributed € 994 million to the net result. Furthermore, there are significant burdens, primarily resulting from the compensation payment for the early termination of the second loss guarantee (€ -100 million), privatisation and restructuring expenses (€ -366 million) as well as substantial loan loss provisions that were higher than planned. In addition, the funding structure, which has to be optimised further, and the refinancing costs for the portfolio transaction, which were borne by the Bank until the disposal of the portfolio, had a marked impact on earnings.
- The development of **RoE** and **CIR** was also influenced by one-off effects. The RoE reported exceeds expectations due to the fact that net income was higher than planned, while the CIR is down due to the extraordinary positive earnings effects. In view of the influencing one-off effects, neither figure provides any information on actual performance development. The Bank expects that it will be able to achieve sustainably adequate ratios (RoE of at least 8 % and CIR of max. 40 %) by 2022 thanks to the measures launched as part of the transformation programme.
- The **NPE ratio** fell significantly, as was to be expected. This was due to the disposal of the non-performing legacy loans as part of the portfolio transaction, which led to a significant reduction in risk on the face of the Bank's balance sheet. In arithmetical terms, the NPE ratio came to 1.6 % as at the reporting date. Findings after the reporting date led to adjusting events resulting in further defaults. Even taking these cases into account, however, the NPE ratio is still in line with the strategic objective and amounts to around 2.0 %.
- The **NPE Coverage Ratio AC** came to a solid 57.6 % as at the reporting date. Taking into account the results of adjusting events and the loan loss provisions set up for macroeconomic and political risks, the NPE coverage ratio AC came to 61 % at the beginning of the new year.
- The **CET1 ratio** remains at a good level. As at 31 December 2018, it amounted to 18.5 % (in-period), clearly in line with expectations.
- The solid liquidity ratios (**LCR**: 225 % and **NSFR**: 121 %) significantly outstrip the Bank's forecasts. Within this context, the improvement in the deposit structure and the lower liquidity requirements relating to the volume of receivables had a positive effect.

Further details on the reasons underlying the business performance are set out in the following "Earnings", "Net assets and financial position" and "Segment results" sections.

Net earnings

Since 1 January 2018, Hamburg Commercial Bank has been applying the provisions set out in IFRS 9 – Financial Instruments in full when preparing the Group financial statements. As a result, the current Group statement of income features changes compared with the structure as at 31 December 2017. Accordingly, some figures for the comparative period have been restated. Further information on the changes in accordance with IAS 8.14 can be found in the section entitled "Adjustments to the prior-year figures" in the notes to the Group financial statements.

Statement of Income

(€ m)	2018	After adjustment 2017	Change in %
Interest income from financial assets categorised as AC and FVOCI	923	1,130	-18
Interest income from other financial instruments	1,592	1,657	-4
Negative interest on investments categorised as AC and FVOCI	-21	-30	-30
Negative interest on other cash investments and derivatives	-227	-275	-17
Interest expenses	-1,893	-2,202	-14
Positive interest on borrowings and derivatives	224	296	-24
Net income/loss from hybrid financial instruments	994	304	>100
Net interest income	**1,592**	**880**	**81**
Net commission income	35	65	-46
Result from hedging	-9	-18	50
Net income from financial instruments categorised as FVPL[1]	-136	254	>-100
Net income from financial investments	102	62	65
Result from the disposal of financial assets classified as AC	2	302	-99
Net income from financial investments accounted for under the equity method	–	2	-100
Total income	**1,586**	**1,547**	**3**
Loan loss provisions	-316	-2,086	-85
Hedging effect of credit derivative second loss guarantee	-51	810	>-100
Total income after loan loss provisions	**1,219**	**271**	**>100**
Administrative expenses	-402	-481	-16
Other operating income	-107	21	>-100
Expenses for regulatory affairs, deposit guarantee fund and banking associations	-89	-49	82
Net income before restructuring and privatisation	**621**	**-238**	**>100**
Net income from restructuring and privatisation	-366	-66	>-100
Expenses for government guarantees	-158	-149	6
Net income before taxes	**97**	**-453**	**>100**
Income tax expenses	-20	-75	-73
Group net result	**77**	**-528**	**>100**
Group net result attributable to non-controlling interests	7	7	–
Group net result attributable to Hamburg Commercial Bank shareholders	70	-535	>100

[1] In the previous year, under IAS 39, the item Net trading income.

Total income influenced by one-off effects

Total income increased marginally in the 2018 financial year to € 1,586 million compared to € 1,547 million in the previous year. On the one hand, net operating interest income, which was above plan contributed to total income. On the other hand, one-off effects from the revaluation of hybrid instruments had a positive effect. So the termination for the existing silent participations with effect from the end of 2018 and potential buyback offers result in a reassessment of the cash flows from the hybrid instruments. The silent participations were terminated subject to a notice period of two years. As a result, the outstanding hybrid capital instruments will either be redeemed in 2021 at the HGB carrying amount for the 2020 financial year or will be bought back by the Bank prior to the redemption date in 2021 as part of potential voluntary buyback offers. Against this backdrop, the reassessment of the cash flows from the hybrid instruments, taking into account the discounting and compounding effects, leads to positive net income from hybrid financial instruments in the amount of € 994 million. In the previous year, the revaluation had a positive effect on total income in the amount of € 304 million. In addition, the Bank had achieved unrealised gains of € 356 million in the previous year in order to partially offset the considerable burdens resulting from non-performing legacy loans attributable to the former Non-Core Bank. The following developments in the individual income line items were relevant:

Net interest income contributed € 1,592 million (previous year: € 880 million) to total income. Net interest income includes interest income from operating activities that exceeded expectations, as well as positive valuation effects, mainly due to the fair value measurement of the portfolio transaction and the hedging of the liquidity position. In addition, the change in the net income from hybrid instruments of € 690 million contributed to the year-on-year increase. Net interest income was hit significantly by expenses incurred to build up liquidity and for the funding structure, which the Bank is counteracting during the transformation period with measures to optimise the liabilities side. Furthermore, refinancing costs incurred in connection with the portfolio transaction had a marked negative impact in the period leading up to the disposal of the portfolio.

Net commission income came to € 35 million as at reporting date (previous year: € 65 million). The decline is attributable, in particular, to lower income from loan commission. In addition, net commission income in the previous year included significant income for the restructuring of non-performing legacy loans in the Non-Core Bank.

Net income from financial instruments categorised as FVPL had a negative impact on total income in the amount of € -136 million (previous year: € 254 million). This development was mainly due to subsequent valuation effects, most of which arose as a result of the portfolio transaction. These are offset by interest income of the same amount arising from the recognition of interest on defaulted portfolios measured at FV in accordance with IFRS 9, which has to be reported accordingly under net interest income. In addition, the previous year's result benefited significantly from the positive net income from foreign currency and increases in the value of the credit investment portfolio. Net operating trading income from cross-selling activities and the management of central liquidity and market price risks also declined compared with the previous year.

Net income from financial investments including other income items contributed € 104 million (previous year: € 366 million including € 302 million in the result from the disposal of financial assets classified as AC) to total income. It mainly includes gains from the sale of securities.

Mounting geopolitical risks put pressure on loan loss provisions

Loan loss provisions amounted to € -287 million as at the reporting date (previous year: € -1,402 million).

On the one hand, this development is due to specific loan loss provisions set up in the Shipping division, which are largely related to restructuring measures for a significant loan exposure. On the other hand, the increasing geopolitical and economic uncertainties are reflected in the substantial general loan loss provisions that were set up. By setting up these provisions, the Bank is taking precautions in view of the increasing probability of downside scenarios due to the risk of a hard Brexit or the possible escalation of the trade conflict between the US and China, which could have a negative impact on economic development in Europe and in the sectors relevant to the Bank (in particular shipping and real estate). In addition, the Bank has set up corresponding loan loss provisions for ships on the basis of the emission requirements that will apply as of 2020. In the previous year, furthermore, significantly higher amounts allocated for legacy loan exposures, especially in the shipping portfolio of the Non-Core Bank, had a considerable negative impact on the Group net result.

After currency effects and compensation, and taking into account the hedging effect from the credit derivative, the total loan loss provisions come to € -367 million (previous year: € -1,276 million).

Marked reduction in administrative expenses

Administrative expenses came to € -402 million as at the reporting date (previous year € -481 million). The Bank is continuing to successfully implement its cost-cutting programme, which has been ongoing since 2014 and counteracts the increasing pressure on earnings and margins in the highly competitive banking market and the increasing expenses for regulatory requirements, stringently and in line with its plans. During the reporting period, the Bank once again made the progress it planned to make in implementing measures for operating expenses. The ongoing cost reduction program will be consolidated with the measures forming part of the trans formation project, which aim to reduce costs and increase efficiency, and will be implemented resolutely until an appropriate CIR of 40 % at the most has been achieved. Corresponding negotiations with the Bank's social partners commenced directly after the closing date and are still ongoing.

Operating expenses came to €-186 million (previous year: € -215 million). Depreciation of property, plant and equipment and amortisation of intangible assets came to € -18 million (previous year: € -36 million).

As far as personnel costs are concerned, the planned reduction from the 2018Plus programme was agreed almost entirely with employees and the ambitious personnel cost targets continued to be consistently implemented. The further reduction in the number of employees as planned is reflected in the corresponding reduction in personnel expenses from € -230 million to € -198 million. Compared to the end of 2017, the number of employees within the Group continued to drop considerably by -210 to 1,716 (computed on a full-time equivalent (FTE) basis).

Other income line items

Other operating income amounted to € -107 million (previous year: € 21 million) and mainly includes provisions for litigation risks. Further details can be found in Note 17 in the notes to the Group financial statements.

The expenses for regulatory affairs, the deposit guarantee fund and banking associations amounted to € -89 million (previous year: € -49 million). The marked increase is mainly due to provisions set up for expected one-off payments to be made to the Association of German Banks (Bundesverband deutscher Banken) due to the planned change in the guarantee scheme as at 1 January 2022.

Rising restructuring and privatisation costs reflect transformation measures

Earnings were also hit considerably by restructuring and privatisation expenses amounting to € -366 million (previous year € -66 million). Net income from restructuring and privatisation includes, in particular, provisions for personnel measures planned as part of the transformation project (€ -259 million). In addition, the Bank has set up restructuring provisions for measures to reduce operating expenses. What is more, expenses from the privatisation process amounting to € -66 million (previous year: € -52 million), which were incurred in connection with external consulting in particular, had a significant negative impact on earnings.

Guarantee premium includes substantial special charge for early termination of the second loss guarantee

The expense for the guarantee premium had a significant impact on the Bank's net result in the amount of € -158 million (previous year: € -149 million). In addition to the base premium, the Bank made a compensation payment of € -100 million due to the premature termination of the second loss guarantee. The compensation payment was part of the cancellation agreement concluded between HSH Finanzfonds AöR, HSH Beteiligungs Management GmbH and Hamburg Commercial Bank AG as part of the privatisation process.

Group net result outstrips expectations by far

As at 31 December 2018, Hamburg Commercial Bank generated net income before taxes of €97 million (previous year: € -453 million). The net result exceeded expectations due to the satisfactory operating performance and in view of the aforementioned one-off effects. Significant burdens from restructuring provisions for the comprehensive and far-reaching transformation programme, as well as provisions for credit risks which were set up to reflect increasing geopolitical and economic uncertainties, were offset in full by total income.

After taxes, the Group net result comes to € 77 million (previous year: € -528 million). Income tax expense includes tax income from current taxes of € 15 million and tax expense from deferred taxes of € -34 million. Income from current taxes relates mainly to previous years. The deferred tax expense comprises the reversal of deferred taxes on temporary differences and offsetting income from the recognition of deferred tax assets on loss carryforwards.

Net assets and financial position

Since 1 January 2018, Hamburg Commercial Bank has been applying the provisions set out in IFRS 9 – Financial Instruments in full when preparing the Group financial statements. As a result, the current Group statement of financial position features changes compared with the structure as at 31 December 2017. Further information can be found in the section entitled "Adjustments to the prior-year figures" in the notes to the Group financial statements.

Material items on the statement of financial position

(€ m)	2018	2017	Change in %
Assets			
Cash reserve	5,362	6,625	-19
Loans and advances to banks	3,167	3,838	-17
Loans and advances to customers	32,791	39,174	-16
Loan loss provisions	-831	687	>100
Credit derivative under the second loss guarantee	–	1,014	-100
Trading assets	3,094	3,641	-15
Financial investments	10,100	13,647	-26
Non-current assets held for sale and disposal groups	65	139	-53
Other assets	1,373	1,617	-15
Total assets	**55,121**	**70,382**	**-22**
Liabilities			
Liabilities to banks	5,470	8,271	-34
Liabilities to customers	28,093	36,205	-22
Securitised liabilities	9,458	12,444	-24
Trading liabilities	2,812	3,875	-27
Liabilities relating to disposal groups	–	47	-100
Subordinated capital	1,614	2,252	-28
Equity	4,437	4,373	1
Other liabilities	3,237	2,915	11
Total liabilities and shareholders' equity	**55,121**	**70,382**	**-22**

Drop in total assets in the course of the year
The Group's total assets fell, as planned, by around one-fifth in the 2018 financial year to € 55,121 million (31 December 2017: € 70,382 million). The following developments were decisive for the decline in total assets:

The cash reserve fell compared with the previous year-end to € 5,362 million (31 December 2017: € 6,625 million). Loans and advances to banks also decreased and amounted to € 3,167 million (31 December 2017:€ 3,838 million). The Bank's active liquidity management, which aims, among other things, to gradually reduce the above-average liquidity reserves built up during the privatisation period, led to a moderate decline in extensive balances at central banks.

Loans and advances to customers came to € 32,791 million (31 December 2017: € 39,174 million), also below the level seen in the previous year. The decline is mainly due to the closing of the portfolio transaction. In connection with the closing of the privatisation process, the portfolio transaction agreed to relieve the Bank of large parts of its non-performing legacy loans and the early termination of the second loss guarantee were implemented at the same time. As a result, the loan loss provisions disclosed on the balance sheet are once again free of effects resulting from the guarantee and amount to € -831 million (31 December 2017: € 687 million).

Trading assets decreased to € 3,094 million (31 December 2017: € 3,641 million). While securities held for trading increased slightly, the positive fair values of derivatives in trading assets declined. Financial investments dropped to € 10,100 million (31 December 2017: € 13,647 million). This was due, in particular, to the winding down of securities portfolios in the context of liquidity management.

Almost all line items on the liability side of the balance sheet decreased as well, as was to be expected. Liabilities to banks, for example, fell considerably to € 5,470 million (31 December 2017: € 8,271 million). The repo transactions business in particular, but also time deposits, declined due to lower refinancing requirements. In line with the gradual reduction in liquidity, liabilities to customers also declined to € 28,093 million (31 December 2017: € 36,205 million).

Securitised liabilities were also down on the previous year-end to € 9,458 million (31 December 2017: € 12,444 million). This is due, among other things, to the termination of the hybrid instruments contained therein subject to a notice period of two years with effect from 31 December 2020, and to the resulting reassessment of the cash flows as at 31 December 2018. Trading liabilities comprising negative market values of derivatives (€ 2,812 million, 31 December 2017: € 3,875 million) were down in line with the positive fair values of trading assets. The subordinated capital came to € 1,614 million, down on the previous year (31 December 2017: € 2,252 million). The main reason behind this is the reassessment of cash flows following the termination of the hybrid instruments. Reported equity remained virtually unchanged and amounted to € 4,437 million (31 December 2017: € 4,373 million).

Business volume also down

In line with the declining total assets, business volume decreased to € 64,496 million (31 December 2017: € 78,611 million). By contrast, off-balance sheet business was higher than in the previous year: sureties and guarantees amounted to € 1,748 million (31 December 2017: € 1,862 million) and irrevocable loan commitments increased to € 7,627 million (31 December 2017: € 6,367 million). The increase is mainly due to effects from the first-time application of IFRS 9 in the 2018 financial year. Further explanations can be found in the financial information as at 31 March 2018 in the section entitled “Accounting and measurement principles” in the chapter entitled “Application of accounting methods IFRS 9 - Financial instruments”, sub-section “IV. Loan loss provisions and impairment of financial instruments” in the notes to the Group financial statements.

Structure of liabilities by financial instruments

(€ m)	2018		2017	
	Total	of which >1 year	Total	of which >1 year
Secured: Pfandbriefe and asset-based funding	**13,074**	**11,148**	**15,485**	**11,008**
Pfandbriefe	8,021	6,772	9,014	7,096
Other secured funding	5,053	4,376	6,470	3,912
Unsecured liabilities (senior preferred)	**23,212**	**2,873**	**31,897**	**5,884**
Unsecured liabilities (senior non-preferred)	**6,555**	**4,441**	**9,030**	**6,657**
Profit participation certificates and other subordinated liabilities	**1,067**	**1,067**	**1,060**	**1,060**
Hybrid instruments	**727**	**687**	**1,700**	**1,700**
Total	**44,635**	**20,216**	**59,172**	**26,309**

The above table breaks down Hamburg Commercial Bank’s liabilities by financial instrument and thereby takes into account the requirements of capital markets participants. Liabilities with a maturity of more than one year are separately shown. The financial instruments can be reconciled to the balance sheet line items liabilities to customers, liabilities to banks, securitised liabilities and subordinated capital. The carrying amounts of financial instruments excluding principal repayments and accrued interest are assigned to maturity bands in the above table.

One focal point within the framework of long-term refinancing relates to securitised debt instruments (covered bonds (Pfandbriefe), asset-based funding). These mainly include debt instruments issued under Pfandbrief programmes (mortgage, public sector and ship Pfandbrief programmes) as well as other asset-based funding issues, repo transactions and deposits from development banks. The total amount of secured debt instruments outstanding was € 13,074 million as at 31 December 2018 (31 December 2017: € 15,485 million).

The unsecured liabilities that can be classified as senior preferred and senior non-preferred include call and time deposits mainly comprising client deposits and other unsecured financing instruments. They totalled € 29,767 million as at the reporting date (31 December 2017: € 40,927 million). Call and time deposits are shown together with structured unsecured financial instruments in the "Senior Preferred" category and amount to € 23,212 million in total (December 31, 2017: € 31,897 million). The "Senior Non-Preferred" category mainly consists of bearer and registered bonds that do not have any structured elements and amounts to € 6,555 million as at 31 December 2018 (31 December 2017: € 9,030 million).

The two line items Profit participation certificates and other subordinated liabilities (€ 1,067 million, 31 December 2017: € 1,060 million) and Hybrid instruments (€ 727 million, 31 December 2017: € 1,700 million) in total represent subordinated capital. Out of the hybrid instruments (Resparc I and Resparc II), € 180 million (31 December 2017: € 508 million) is reported in the balance sheet item Securitised liabilities. The main reason for the significant reduction in hybrid instruments is the termination of the instruments subject to a notice period of two years with effect from 31 December 2020 and the resulting reassessment of cash flows as at 31 December 2018.

Capital and funding

RWA, regulatory capital and capital ratios

(in-period)[1]	31.12.2018	31.12.2017[2]
Risk-weighted assets (RWA) (€ bn)	22.1	26.2
Regulatory capital (€ bn)	5.2	6.7
of which: CET1 capital (€ bn)	4.1	4.0
Overall capital ratio (%)	23.4	25.8
Core capital ratio (%)	18.5	19.7
CET1 capital ratio (%)	18.5	15.4

[1] In-period: ceteris paribus calculation taking full account of the balance sheet amounts as at the reporting date.

[2] From March 2018, the capital ratios will no longer be shown taking into account the regulatory relief effect of the federal state guarantee. To enable a comparison with the key capital figures as at December 2018, pro forma ratios are shown as at 31 December 2017. "Pro forma" means that, for the items included in the reference portfolio for the second loss guarantee, the RWA are recognised in line with the credit risk rules and not in line with the rules regarding securitisation. Within this context, valuation allowances that have been set up are still recognised in a manner that reduces the capital requirements in line with the regulatory requirements.

CET1 ratios at a good level

The CET1 ratio rose significantly to 18.5 % compared with 31 December 2017 (pro forma 15.4 %). The main reason behind the development compared with 31 December 2017 (pro forma) is a reduction in RWA of around € 4 billion, which is mainly attributable to the decline in market risks and the decline in the business volume, particularly in the Non-Core Bank. As a result, this is significantly higher than the internal level of ambition of at least 16 %.

The Tier 1 capital ratio and the total capital ratio declined compared with 31 December 2017. The reason for the development compared with 31 December 2017 lies in the termination of the hybrid instruments. The existing hybrid instruments are subject to the regulatory phase-out regulations for additional Tier 1 capital pursuant to Art. 486 CRR. As part of the privatisation process, the capital structure is being restructured and optimised. Within this context, the hybrid instruments were terminated at the end of 2018 subject to a notice period of two years. As a result, regulatory recognition of hybrid instruments as AT1/T2 capital for the regulatory capital ratios under the CRR and SREP requirements ceases to apply at the end of the 2018 at the same time. The termination of the existing hybrid instruments results in a reassessment of the cash flows associated with the hybrid instruments. The resulting positive valuation effect leads to a significant strengthening of the Common Equity Tier 1 capital in 2018. In 2019, SREP requirements (Pillar 2 Requirement "P2R" incl. the combined capital buffer requirements) for CET1 capital in the amount of around 10.6 %, Tier 1 capital (T1) of around 12.1 % and an overall capital requirement of 14.1 % apply to the Bank. The Pillar 2 Guidance "P2G" (incl. early warning buffer) for the CET1 ratio in 2019 comes to around 11.6 % (previous year: 11.2 %). The increase is due primarily to the phasing-in of the CRR requirement for the capital conservation buffer. The CRR and SREP requirements for AT1/T2 are significantly exceeded by the strengthened Tier 1 capital/available subordinated capital.

Reference is made to the Risk report for information on compliance with the regulatory requirements.

Hamburg Commercial Bank's leverage ratio (in-period) came to a very solid 7.4 % as at 31 December 2018 (31 December 2017: 7.7 %). The development is negatively affected by the termination of the existing hybrid instruments, whereas this is offset by the reduction in the leverage exposure (in-period) to € 55.6 billion in the reporting period (31 December 2017: € 67.6 billion), which reduces the drop in the leverage ratio. The leverage ratio is still well above the internal ambition level of at least 4 % and, as a result, is also in excess of the regulatory reference value of 3 %.

Funding activities further expanded
In the 2018 financial year, the Bank raised around € 3.4 billion in long-term funds, significantly exceeding the budgeted figure.

The Bank issued two benchmark mortgage Pfandbriefe, thus continuing the series of successful capital market issues. The Pfandbriefe have maturities of three and a half years and five years and a volume of € 500 million each. The Bank also expanded its range of asset-based funding transactions. Secured by real estate loans, almost GBP 250 million in long-term funds were raised.

Since the end of 2017, the Bank has been offering private clients fixed-term deposits via various online platforms (Zinspilot, Check24, DB, ZinsMarkt) and has gradually expanded its group of sales partners. Multi-channel funding has led to a continuous increase in the portfolio, which amounted to € 3.2 billion as at the reporting date.

Besides the issuing activities, the level of deposits also contributed to the implementation of the funding strategy. The volume of deposits was reduced as planned in order to further optimise the balance sheet. This allowed the Bank to achieve a structural improvement in the deposit and depositor structure.

Depositor structure

(%, previous year figures in brackets)

The regulatory requirements for the liquidity ratios were exceeded by far during the reporting period. This was due to the improvement in the deposit structure and lower volume of receivables related liquidity requirements.

In addition to successful fundraising, the Bank also received inflows from the settlement of losses and the termination of the second loss guarantee, as well as purchase price payments for the sold portfolios.

Key liquidity ratios

	31.12.2018	31.12.2017
Total deposits (€ bn)	16.7	25.0
LCR (%)	225	169
NSFR (%)	121	114

Rating

Rating overview as at 31 December 2018

	Moody's	S&P
Issuer rating (long-term)	Baa2, stable	BBB, stable
Short-term liabilities	P-2, stable	A-2, stable
Stand-alone rating (financial strength)	ba2, stable	bbb-, stable
"Preferred" Senior Unsecured Debt	Baa2, stable	-
"Non-Preferred" Senior Unsecured Debt	Baa3, stable	-
Public Pfandbrief	Aa2, stable	-
Mortgage Pfandbrief	Aa2, stable	-

Hamburg Commercial Bank is rated by Moody's and S&P. Both rating agencies regard the successful privatisation and conclusion of the EU state aid proceedings, as well as the structural measures implemented within this context, which have led to a significant improvement in the financial and risk profile, as a decisive milestone on the road towards a business model that is sustainable in the long term. Against this backdrop, Moody's upgraded its rating to Baa2 (issuer rating) on 28 November 2018. S&P awarded the Bank a BBB (issuer rating) rating for the first time on 6 December 2018. In light of the intensive transformation process and the agreed seamless transition of the deposit guarantee fund, the agencies are focusing on the implementation of the measures, particularly with a view to improving operational performance.

Moody's has awarded the Bank long-term and deposit ratings of Baa2. The outlook has been raised to stable. In addition, Moody's has introduced a rating for unsubordinated and unsecured liabilities of banks that are considered, in the event of the insolvency of a German bank, before non-subordinated liabilities of this bank within the meaning of Section 46 f (6) of the German Banking Act (KWG). This rating is referred to as "Preferred" Senior Unsecured Debt and is at the Baa2 level for Hamburg Commercial Bank.

S&P's short-term rating is A-2. No further issue ratings have been commissioned.

The Risk report contains supplementary information on the capital and refinancing situation of Hamburg Commercial Bank.

Segment results

Segment overview[1)]

(€ m)		Corporate Clients	Real Estate	Shipping	Treasury & Markets	Core Bank[3)]	Non-Core Bank	Other and Consolidation[4)5)]	Group
Total income	**2018**	**222**	**189**	**108**	**218**	**737**	**-11**	**860**	**1,586**
	2017	250	215	107	573	1,145	79	323	1,547
Loan loss provisions (including credit derivative)[2)]	**2018**	**-54**	**-55**	**-205**	**16**	**-298**	**7**	**-76**	**-367**
	2017	-53	2	63	1	13	-1,295	6	-1,276
Administrative expenses	**2018**	**-122**	**-57**	**-35**	**-74**	**-288**	**-117**	**3**	**-402**
	2017	-118	-51	-39	-84	-292	-190	1	-481
Net income before taxes	**2018**	**34**	**67**	**-156**	**149**	**94**	**-253**	**256**	**97**
	2017	73	157	110	482	822	-1,550	275	-453
Segment assets (€ bn)	**31.12. 2018**	**12**	**12**	**5**	**19**	**48**	**0**	**7**	**55**
	31.12. 2017	12	10	5	21	48	12	10	70

1) After changes in the allocation of transformation costs for liquidity provisioning and the funding structure, as well as changes in presentation according to Note 3 (Changes in the Group statement of income); previous year's figures adjusted accordingly.
2) Summary of "Loan loss provisions" and "Hedging effect of credit derivative under the second loss guarantee".
3) Core Bank is the total of the four segments: Real Estate, Shipping, Corporate Clients and Treasury & Markets.
4) Net income before taxes including result from restructuring and privatisation.
5) Consolidation also includes the effects from differences in accounting.

Core Bank development

The development of the Core Bank has to be viewed in a differentiated manner. On the one hand, **operating performance** was satisfactory overall. Net operating interest income was moderately above expectations. The average interest-bearing receivables portfolio increased slightly as against the previous year. New business amounted to € 8.0 billion during the reporting period (previous year: € 8.5 billion). Gross new business, which also includes the volume earmarked for syndication, amounted to € 8.4 billion (€ 8.6 billion). The underwriting book and the deals concluded showed encouraging development that was in line with the business strategy guidelines during the reporting period. The Bank systematically selects its business transactions on the basis of stringent internal risk and return requirements and focuses primarily on profitability ambitions. As a result, new business margins rose noticeably in the period under review, whereas the volume of new business fell just short of expectations. The cross-selling result was in line with requirements, mainly due to investment products.

On the other hand, **one-off effects** had a significant impact on the development of the Core Bank. **Total income** fell considerably, by around € 400 million, to € 737 million . On the one hand, this development is attributable to lower income from the sale of securities. In the previous year, the Bank realised unrealised gains in order to partially compensate for the considerable burdens resulting from non-performing legacy loans attributable to the former Non-Core Bank. On the other hand, the previous year included positive valuation effects relating to client derivatives, which had a marked positive impact on net income from financial instruments categorised as FVPL.

Loan loss provisions increased significantly to € -298 million (previous year: € 13 million). This was due both to economic risks, which resulted in substantial general loan loss provisions being set up in the segments, and to loan loss provisions relating to individual cases, which had a significant negative impact on the Shipping segment in particular.

Guarantee expenses, which include a considerable one-off payment for the early termination of the second loss guarantee, also had a noticeable impact on the development of the Core Bank in the amount of € -41 million. Guarantee expenses are calculated based on originally guaranteed portfolios that were also included in the Core Bank and are incurred for the last time during the reporting period.

By contrast, **other income line items** developed in line with expectations. Administrative expenses are being reduced in line with the targets, and the Bank is implementing its cost-cutting programme rigorously. Regulatory expenses amount to € -27 million.

Taking one-off effects into account, the **Core Bank's net income before taxes** fell significantly as a result to € 94 million as against € 822 million in the previous year, putting it well below the planned figure as well.

The development of the **key Core Bank figures that are relevant from a management perspective** is shown in detail below:

Key management indicators - Core Bank	2017	2018 forecast	2018
Net income before taxes (€ m)	822	Below net result for 2017	94
RoE	23.4%	Below the value achieved in 2017	2.6%
CIR	25.3%	Increase despite lower cost base, as the ratio was positively overstated 2017	38.5%
New business (€ bn)	8.5	Moderately above the previous year's level	8.0

The **return on equity** amounts to 2.6 % (previous year: 23.4 %). The decline is due in particular to the one-off effects described above. In its planning, the Bank had assumed a decline in earnings and, as a result, also a lower RoE, although the extent of the negative effects (including expenses for privatisation and restructuring, as well as loan loss provisions) exceeded its expectations by far.

By contrast, the **cost-income ratio** developed in line with expectations, and the implementation of cost savings went according to plan during the reporting period. This results in a corresponding drop in administrative expenses.

Following the successful completion of the privatisation process and the structural improvements that it has achieved, the Bank is entering the next phase of its transformation. One focal point in this respect will also be on increasing operating performance in the segments, taking into account the cost structures within the entire Group. Against this backdrop, the Bank has defined a strategic target vision at Group level and is consistently bringing its business activities into line with these guidelines. The Bank is aiming to achieve its long-term target ratios for the Group, namely a return on equity before tax of more than 8 % and a cost-income ratio in excess of 40 %, by 2022 at the latest. The measures implemented as part of the transformation project are geared towards this objective and will be implemented intensively now that the EU state aid proceedings have been completed.

Total assets of the Core Bank amounted to around € 47.7 billion as at the reporting date (31 December 2017: € 48.4 billion). In preparation for the closing, a total of € 2.5 billion (thereof € 0.4 billion in NPE volume) of transactions not included in the portfolio transaction was transferred from the Non-Core Bank to the Core Bank in the first half of 2018. Most of these loans were healthy portfolios that were previously allocated to the non-strategic business but are to remain within the Bank. The transfer did not result in any significant change in the segment results.

Segment results in the Core-Bank

The **Corporate Clients** segment is well diversified and is organised on a sector-specific basis. It combines the Energy & Infrastructure, Trade, Food & Healthcare, Industry & Services and Wealth Management business areas. In addition, the business unit offers the consultancy areas of structured financing, leveraged buy-out and mergers & acquisitions from a single source for all clients of the Bank.

In the Corporate Clients segment, net income before taxes amounted to € 34 million (previous year: € 73 million). This development is due to total income that down to € 222 million (previous year: € 250 million). This primarily reflects lower net income from financial instruments categorised as FVPL, which in the previous year included significant positive valuation effects on client derivatives. In addition, net commission income fell short of expectations and the previous year. This is due to the business development in an environment that has been highly competitive for years now.

The net result was hit, in particular, by loan loss provisions of € -54 million (previous year: € -53 million), most of which relate to individual exposures and, to a lesser extent, to general loan loss provisions.

New business showed subdued development in line with the competitive market environment. It amounted to € 2.6 billion in total (previous year: € 3.1 billion). The Bank systematically selects its business transactions on the basis of stringent internal risk and return requirements and focuses primarily on profitability requirements. As a result, and due to the considerable pressure on margins, momentum was deliberately reduced, particularly in the business with medium-sized corporates. As a result, new business in the individual segments is down on the prior-year results. One encouraging exception is the development in the Industry & Services business segment. New business in this segment increased in a year-on-year comparison. Cross-selling income also fell short of that achieved in the previous year, although the decline was less pronounced than the drop in the new business volume. In the energy sector, the volume of receivables increased compared with the end of the previous year. The focus here was on the financing of wind turbines. Following the successful market entry in Portugal in the previous year, the renewable energy segment managed to consolidate its market position in Netherlands and strength its position in France again in 2018. In the business with corporates, the Bank was partially successful in stabilising its credit margins and exploiting the improved refinancing opportunities to increase margins.

The **Real Estate Clients** segment once again made a significant contribution to earnings of € 67 million (previous year: € 157 million) in 2018. The repayment of existing high-margin transactions had a negative impact on net interest income, which amounted to € 168 million compared with € 178 million in the previous year. In addition, total income in the previous year included positive valuation effects from client derivatives that boosted the result. In addition, net income before taxes as at the reporting date was hit by considerable allocations to general loan loss provisions. The Bank is taking precautions because the German real estate market is approaching its zenith after a long-standing upswing and economic uncertainty is generally on the rise.

New business totalled € 4.6 billion in a competitive environment that remained intense (same period of the previous year: € 4.7 billion), ahead of expectations. The Bank succeeded in continuously improving new business margins and significantly increasing the profitability of new business. The RoE achieved in the Bank's new business exceeds the ambition level and makes a positive contribution to developments in the Overall Bank. The positive development in business with international institutional investors continued and the high market penetration in the northern German core region was expanded. The division is also exploiting its good market position in the metropolitan regions of western Germany. In the medium term, the resumption of international business will further improve the portfolio mix and the risk profile.

In the **Shipping** segment, net income before taxes amounted to € -156 million (previous year: € 110 million). The significant decline is attributable in particular to the significant burden of € -205 million from loan loss provisions. By contrast, the Bank had reversed € 63 million in loan loss provisions in the previous year. The development as at the reporting date is due in particular to specific loan loss provisions, most of which were set up in connection with restructuring measures for a major loan exposure. In addition, the Bank also set up general loan loss provisions to reflect economic uncertainties and the emission requirements for ships that will apply from 2020 onwards.

Developments on the shipping markets varied from sub-segment to sub-segment during the reporting period. Despite a market environment that remains challenging, new business with national and international shipping companies with good credit ratings, in which margins have risen over the course of time, came to € 0.9 billion, above both the previous year's level and the planned level. The profitability of new business improved significantly.

The **Treasury & Markets** segments generated net income before taxes of € 149 million (previous year: € 482 million). Income from the client business with capital market products and income from the management of liquidity and market price risks contributed to this result. The net result also includes valuation gains and income realised from securities portfolios.

The reason for the significant decline in the net result compared with the previous year lies in the one-off effects included in the previous year from the realisation of unrealised gains, which were realised in order to partially compensate for the considerable burdens resulting from non-performing legacy loans in the Non-Core Bank.

Development of the Non-Core Bank

Key management indicators for the Non-Core Bank	2017	2018 forecast	2018
Net income before taxes (€ m)	-1,550	Loss, but significantly lower than in 2017	-253
Total assets (€ bn)	11.7	Will fall considerably	0.2

With the successful completion of the privatisation process, the non-performing portfolios previously separated in the Non-Core Bank have been almost completely disposed of, meaning that the Non-Core Bank has fulfilled its function. Developments within the Non-Core Bank are being reported for the last time as at 31 December 2018.

As expected, the Non-Core Bank reported a loss of € -253 million as at the reporting date, down significantly year-on-year (previous year: € -1,550 million). The net result in the previous year had been influenced by the very substantial loan loss provisions in connection with the portfolio transaction. On the other hand, the net result as at the reporting date was mainly affected by guarantee charges (€-118 million) incurred for the last time that are largely attributable to the early termination of the second loss guarantee, as well as administrative expenses, which amounted to € -117 million (previous year: € -190 million). The decline in operating expenses was much more pronounced than expected. Refinancing costs for the portfolio transaction that had to be borne by the Bank between the signing and closing of the transaction also put pressure on the net result.

As at 31 December 2018, total assets of the Non-Core Bank amount to € 0.2 billion, which represents a considerable drop. In addition to IFRS 9 changeover effects, the decline is attributable to the transfer of Non-Core Bank portfolios to the Core Bank (€ 2.5 billion in the first half of 2018) and to the original winding-down of non-performing loans that were not sold as part of the portfolio transaction. Furthermore, as expected, the sold loan portfolios were transferred to the sphere of the buyers following the closing of the share purchase agreement, and the second loss guarantee was settled with definitive effect. In connection with these measures, the outstanding receivables (compensation item: € 6.2 billion on 31 December 2017) were paid to the Bank by the guarantor, Finanzfonds AöR. The amount of € 0.2 billion reported relates to loan exposures that have not yet been transferred as part of the portfolio transaction.

"Other and Consolidation" division

Administrative functions and overall bank positions are disclosed in Other under "Other and Consolidation" as segments not subject to reporting requirements. "Consolidation" also comprises items that reconcile the internal reporting results presented in the segment report to the Group financial statements prepared in accordance with IFRS. In addition to the measurement and disclosure differences, the result from restructuring and privatisation is allocated in full to this division. From 31 March 2018, the costs for transformation-related liquidity provisioning and funding structure incurred during the privatisation period and during the Bank's realignment are reported under "Other and consolidation". The prior-year and budgeted comparative figures have been adjusted accordingly. This is the Bank's way of improving transparency with regard to the expenses associated with the transformation process and at the same time highlights the operating performance of the customer segments more clearly.

The Group net result before taxes amounts to € 256 million as at the reporting date (previous year: € 275 million). Various one-off effects contributed to this net result.

At € 994 million, the valuation of hybrid instruments had a significant positive impact on total income. By way of example, the termination for the existing silent participations with effect from the end of 2018 and potential buyback offers result in a reassessment of the cash flows from the hybrid instruments. In the previous year, the valuation of the hybrid instruments had a positive effect on total income in the amount of € 304 million.

By contrast, the net result was hit to a considerable degree by the above-mentioned costs of building up liquidity reserves and the funding structure, which are reflected in total income. What is more, the net result was impacted considerably by restructuring expenses of € -366 million (previous year: € -66 million), other operating income of € -106 million (previous year: € 23 million), as well as the expenses for regulatory affairs, the deposit guarantee fund and banking associations of € -60 million.

The figure reported under loan loss provisions of € -76 million (previous year: € 6 million) arose due to settlement-related guarantee effects. Since the introduction of IFRS 9 in 2018, the hedging effect of the second loss guarantee on the balance sheet has resulted in compensation effects relating to the items Net income from financial instruments categorised as FVPL and Loan loss provisions. All in all, these effects are virtually neutral for the two income statement items and are shown under "Other and consolidation". They arose in connection with the guarantee settlement, meaning that they will no longer apply in the future.

The segment assets of "Other and Consolidation" mainly include the liquidity reserve. Segment assets as at 31 December 2018 came to € 7.2 billion (31 December 2017: € 10.3 billion).

Final assessment of the situation of Hamburg Commercial Bank

The development of the Hamburg Commercial Bank Group in the 2018 financial year was characterised by various effects, some of which were extraordinary. Overall, the situation was satisfactory. The Bank achieved its main objectives, and in some cases even exceeded them, taking into account one-off effects.

In operational terms, the Bank's development in a highly competitive environment was encouraging overall. This was thanks to the stringent focus on earnings, which led to rising new business margins and improved profitability, as well as new business driven by real estate clients, project financing and shipping. The implementation of the ongoing cost-cutting programme was also satisfactory, and administrative expenses fell considerably again (-16 %).

In addition, one-off effects in connection with the privatisation process, the far-reaching transformation process and the ongoing optimisation of the liabilities side also played a significant role in shaping the Bank's development. These include significant burdens resulting in particular from restructuring expenses, the guarantee compensation payment, loan loss provisions and refinancing costs for the portfolio transaction, as well as costs relating to the liquidity and funding structure, which is in need of improvement. In addition, significant positive effects resulting from the revaluation of the hybrid instruments contributed to the Bank's development. Ultimately, the considerable burden was compensated for and the earnings forecast at Group level was exceeded.

Other key management indicators relating to capital and liquidity exceed clearly defined levels of ambition in some cases. The in-period CET1 ratio comes to 18.5 %, which is also a good level in a peer group comparison. As expected, the development of the risk ratios is in line with the risk structure, which has been optimised as part of the privatisation process. The NPE ratio is making the expected progress and has improved significantly to 2.0 % (31 December 2017: 10.4 %).

Overall, the successful completion of the privatisation process has resulted in the expected structural relief. In addition, the agreements reached with the guarantee schemes provided a reliable framework for the seamless transition to the deposit guarantee fund for private banks as of 1 January 2022.

The Bank is in the midst of a far-reaching transformation process as it moves towards establishing a profitable business model that is sustainable in the challenging banking environment in the long run and for which a solid foundation was laid in 2018.

After the reporting date, and with regard to the calculation of the NPE ratio and the coverage ratio, events occurred that were described in the chapter entitled "Earnings, net assets and financial position" under the information on the development of the key Group figures that are relevant from a management perspective. Other than that, there were no incidents worthy of reporting after the reporting date.

Details regarding the continuing challenges, as well as opportunities and risks of future development, can be found in the Forecast, opportunities and risks report.

Employees of Hamburg Commercial Bank

The human resource strategy supports the overall bank strategy and provides the framework for operational human resource functions. It attaches great importance to ensuring that quantitative and qualitative staffing levels are in place and to managing and avoiding related personnel risks. This is associated with moves to retain and attract motivated and committed employees, particularly in view of the challenges posed by the ongoing transformation process.

The Human Resources division is responsible for its governance function, especially in managing personnel expenses and implementing, complying with and enhancing the legal and regulatory principles and guidelines. Modern and reliable operating processes form the basis for all topics relating to human resource functions.

Effective resource management

The successful implementation of the programmes initiated by the Management Board in 2015/2016 to permanently reduce administrative expenses continued in 2018. The target for the planned workforce reduction in 2018 was almost reached in a socially responsible manner with the help of the arrangements agreed with the Works Council. The number of employees had decreased to 1,716, based on full-time equivalents (FTE), by the 2018 year end in the course of the ongoing reduction in staff within the Hamburg Commercial Bank Group (31 December 2017: 1,926). Changes to the scope of consolidation also had an impact on the headcount. The number of employees (FTE) at Hamburg Commercial Bank AG (single entity) decreased to 1,510 by the end of 2018 (31 December 2017: 1,690).

Group employees

	31.12.2018	31.12.2017
Full-time equivalents (FTE) in the Group[1]	**1,716**	**1,926**
of which: Women	631	719
of which: Men	1,085	1,207
of which: Employees in Germany	1,648	1,838
of which: Employees abroad	68	88
Total number of employees in the Group (headcount)	**2,021**	**2,295**
Key employee figures		
Part-time employees (%)	26.7	26.7
Average age in years[2]	46.0	45.9
Average period of employment (years)	14.8	14.5

[1] Total number of employees excluding trainees, temporary staff and interns.
[2] Head offices only; does not include branches or subsidiaries.

Focus on modern HR development

In 2018, HR development focused on deepening and further developing the expertise of the Bank’s employees. The training courses required for regulatory purposes were supplemented by future-oriented content. We prepared our managers for changes in their leadership role using seminars such as “Leadership of the coming Y and Z generations” or “Social media for managers”. A range of health and communication-oriented seminars rounds off Hamburg Commercial Bank's HR development programme.

Young professionals programme expanded further

In addition to the development of all employees, measures were taken again in 2018 to further strengthen the recruitment and promotion of our young professionals. Hamburg Commercial Bank offers high-quality education for the Bachelor of Arts/Science degrees in business management/information systems and for the office management specialist occupations. A total of 23 dual students/apprentices were employed in 2018.

In the past year, ten dual students and one office management apprentice completed their dual studies/vocational training at Hamburg Commercial Bank with a very good or good overall score and received an open-ended job offer. These young professionals now have further promotion possibilities following their training.

For new entrants to the profession, Hamburg Commercial Bank offers a 24-month trainee programme covering a wide range of topics. High-quality training is hereby ensured by giving the participants a comprehensive insight into each of the Bank's fields of activity. A total of 22 trainees were employed in 15 business units in 2018.

Due to the exceptional young professionals programme, Hamburg Commercial Bank was again honoured in 2018 by Absolventa GmbH as a provider of a career-enhancing and fair trainee programmes as was also recognised as a "Fair Company" for its good treatment of interns and university graduates. The young professionals programme is a key element for counteracting the demographic trend and increasing average age of Hamburg Commercial Bank's employees.

Further expansion of exemplary health care and social management services

Employees are provided with extensive health care and social management services in an integrated approach. Besides in-house seminars, these also include individual counselling for employees, managers and whole teams. In addition, Hamburg Commercial Bank helps its employees to strike a balance between work-related and family commitments by offering comprehensive advice and information on topics such as maternity and parental leave, childcare and caring for relatives. The services offered are regularly reviewed and flexibly tailored to employee requirements.

Remuneration paid to employees

The specific design of the remuneration systems that apply at Hamburg Commercial Bank aims to harmonise the interests of the Management Board, employees and shareholders and to motivate the Management Board and employees to act in the interests of Hamburg Commercial Bank and make full use of their individual potential.

The remuneration system for employees below the Management Board level is based on a total remuneration approach, counteracts any significant dependence on variable remuneration and thereby prevents the employees from taking excessively high risks for the purposes of realising the variable remuneration potential. The amount of the total budget for the variable performance-related remuneration is determined on the basis of the Bank's performance, which is calculated using parameters that reflect the success of the Bank. In addition to achieving key financial ratios, these parameters also take account of the fulfilment of the Bank's strategic objectives amongst other things. They take account of the concept of sustainability and are always tailored to the business model as well as the overall bank strategy and risk strategy, which are updated on an annual basis.

The budget for the overall bank for variable performance-related remuneration of the employees is distributed to the employees taking into account the performance of the divisions and based on the achievement of individual objectives. Fixed upper limits for the ratio of variable to fixed remuneration were set for all employees of the group in accordance with the German Ordinance on the Remuneration of Financial Institutions (Institutsvergütungsverordnung – InstitutsVergV) in order to avoid disproportionately high variable remuneration.

In accordance with the specific requirements of the InstitutsVergV, Hamburg Commercial Bank defines a group of employees as so-called risk takers, who have a significant influence on the overall risk profile of the Bank by virtue of their function. In accordance with the InstitutsVergV, parts of their variable remuneration are paid on a deferred basis and are dependent on the Bank's sustained performance in line with the regulatory requirements, among other things.

The InstVergV, which has applied since 2010 and sets out provisions on the regulatory requirements that the remuneration systems of institutions have to meet, has been implemented on an ongoing basis and in full in the Bank's collective agreements. Negotiations with the Bank's co-determination bodies on the new requirements of InstitutsVergV 3.0, which was published in 2017, and on moves to revamp the current remuneration system were commenced in 2018, but had not been completed in full by the reporting date.

Details on the remuneration paid to employees are published in a separate remuneration report on Hamburg Commercial Bank's website in accordance with the InstitutsVergV. The remuneration report does not form part of the management report.

Management Declaration pursuant to Sections 289f and 315d of the German Commercial Code (HGB)

Equal opportunities, women in management positions and diversity concept

Hamburg Commercial Bank is continuing to actively address the issues of equal opportunity and the promotion of women with the assistance of its equal opportunities officer. The Bank set the following quotas in line with the law, which came into force in May 2015, regarding equal representation of women and men in management positions in the private sector and public services and the resulting introduction of Section 76 (4) of the German Stock Corporation Act (AktG):

- At the level of managers reporting directly to the Management Board, Hamburg Commercial Bank was aiming to achieve a ratio of 16 % women. This objective has been achieved. The department head ratio also meets the target at 17 % (target of 15 %). The efforts made to promote young female professionals in particular will allow the Bank to fill vacant positions at the next higher level from the group of female department heads in the future.

Statistics on equal opportunities as at 31 December 2018[1)]

	Number			Ratio	
	Women	Men	Total	Women	Men
Managers reporting directly	3	16	19	16%	84%
Heads of department	9	44	53	17%	83%
Total	**12**	**60**	**72**	**17%**	**83%**

[1)] Head Office excluding employees released from their duties.

- In August 2015, the Supervisory Board approved a target of 20 % for the proportion of women on Hamburg Commercial Bank's Management Board, which was to be achieved by 30 June 2017. This objective has not yet been achieved. In July 2017, however, the Supervisory Board renewed its objective of appointing a female member of the Management Board by 30 June 2022, which would correspond to a quota of 25 % based on the current size of the Bank's Management Board.
- Under the requirements of Section 111 (5) AktG, also newly introduced in 2015, Hamburg Commercial Bank is required to set targets for the proportion of women at the Supervisory Board level as well. In line with the requirements of the German Corporate Governance Code (GCGC), the objective pursued by the Supervisory Board since 2011 has been to ensure that the proportion of women does not fall below 20 %. As a result of the privatisation and the associated replacement of the shareholder representatives on the Supervisory Board, the proportion of women has fallen from 31 % (31 December 2017) to 15 %.

One of Hamburg Commercial Bank's top priorities is to ensure a composition of the Management Board and Supervisory Board that is appropriate for the Bank and meets the different requirements of the responsible boards and, as a result, to ensure the adequate exercise of management and control functions. This means that, in addition to the described targets for the proportion of women on the Management Board and Supervisory Board, there are additional requirements aimed at achieving the balanced composition of the Management Board and Supervisory Board. The rules of procedure for the Supervisory Board, for example, state, in Section 6 (3c) (aa), that when filling a post on the Management Board, consideration should be given to ensuring balanced and varied knowledge, skills and experience for all Management Board members.

Forecast, opportunities and risks report

Forecast report including opportunities and risks

The following section should be read in conjunction with the other sections in this management report. The forward-looking statements contained in this forecast report are based on assumptions and conclusions based on information available to the Bank at the time this management report was prepared. The statements are based on a series of assumptions that relate to future events and are incorporated in Hamburg Commercial Bank's corporate planning. The occurrence of future events is subject to uncertainty, risks and other factors, many of which are beyond Hamburg Commercial Bank's control. Actual events may therefore differ considerably from the following forward-looking statements below.

Anticipated underlying conditions

Unless otherwise stated, statements made regarding the underlying conditions are based on internal assessments and estimates.

Economy as a whole and financial markets

WEAKER GROWTH EXPECTED WORLDWIDE

Growth is likely to slow further across the globe in 2019. This is due to what is already a relatively high level of production capacity utilisation in many regions, the uncertainty associated with the trade conflict and Brexit, higher US interest rates and a relatively strong US dollar.

In the US, the high pace of growth seen last year is unlikely to be maintained in 2019, as the first early indicators would already suggest. This is because the positive economic effect of the tax reform passed at the end of 2017 is gradually coming to an end, and bottlenecks in the labour market are also starting to come to light. Moreover, trade policy and retaliatory tariffs imposed by key trading partners, the relatively strong US dollar and higher interest rates are likely to put a damper on growth. Overall, the Bank expects to see growth of 2.1 % for the current year, which represents a significant loss of momentum compared with the strong previous year. In China, the slowdown in growth is likely to continue. The Bank anticipates an expansion rate of 6.2 %. In general, in addition to an escalation in the trade conflict, the emerging markets will have to expect tighter financing conditions in view of higher US dollar interest rates and a relatively strong US dollar. This is expected to slow growth in this group of countries.

In the eurozone, the economic slowdown continued unchanged at the end of 2018. Nevertheless, the Bank does not expect to see any recession in the EMU area in 2019. Rather, growth is likely to continue to lose momentum, coming in at a rate of 1.3 % compared with the previous year. The trade conflict, the prospect of a Brexit deal at the end of March, the protests against the government's reform policies in France and the lack of growth-stimulating policies in Italy are having a negative impact. In the event of a hard Brexit, the economic drag would be even more pronounced. The ECB's low interest rate policy, which ensures favourable financing conditions for the corporate sector and households alike, is still having a stimulating effect. Unemployment is on a downward trajectory in the eurozone, meaning that private consumption should prop up growth.

MORE CAUTIOUS FED, ECB WRESTLES WITH FIRST INTEREST RATE HIKE, CAUTIOUS RISE IN YIELDS

In view of the first economic warning signals in the US and the existing risks, the Fed has recently become more cautious about further interest rate hikes in 2019. It wants to adopt a patient and flexible stance, meaning that market participants have currently priced out further interest rate steps. In the Bank's view, however, the Fed's new rhetoric only points to fewer increases than originally envisaged. In this respect, the Bank still expects to see an interest rate hike of 25 basis points to a target range for the Fed Funds Rate of between 2.50 % and 2.75 %. The ECB has committed itself to not implementing any initial interest rate hike before the end of summer 2019. Thereafter, however, it could continue to normalise its monetary policy and raise the deposit rate and the key interest rate slightly. The overall upward trend in economic risks is likely to play a key factor. Long-term yields should increase, albeit only moderately due to uncertainties.

The euro is likely to remain weaker against the US dollar to begin with, not least due to the high level of uncertainty among market participants. In the future, the euro could make gains against the US dollar again, because, unlike the eurozone, the US could move into a slight recession in 2020.

Outlook for relevant markets

SHIPPING MARKETS

The outlook for the shipping markets is characterised by greater uncertainty. This relates, on the one hand, to the global economy and, on the other, to impending regulatory changes.

The market for container vessels is expected to recover in general in 2019, as demand growth is expected to be as robust as in the previous year. The risk of setbacks, however, has increased: trade restrictions could be stepped up considerably, geopolitical risks could intensify, and a possible hard Brexit could put a damper on the European economy. On the supply side, fleet growth will taper off significantly as scrapping activities accelerate. New ships resulting from the recent increase in the number of new orders again will only be launched on the market subject to a time lag. This means that 2019 is likely to bring higher fleet utilisation. Both charter rates and ship values can therefore be expected to rise in general, although they will be subject to pronounced fluctuations.

The demand growth for bulkers is likely to weaken continuously over the next few years. This is mainly due to Chinese imports of coal and iron ore, which are expected to continue to lose momentum. If trade disputes were to escalate or persist for a prolonged period, this could have more serious implications. On the supply side, growth rates remain at the moderate level seen in the previous year. There will only be a noticeable increase in the number of ships entering the market again after a certain time lag. Ultimately, fleet utilisation as a whole should increase moderately in 2019 and support the development in charter rates and ship values.

The oil tanker market is expected to move into a volatile upward trend in 2019. Although the renewed production cut by OPEC+ adopted in December is likely to have a negative impact, further increases in US crude oil exports could partly compensate for this, although this would be called into question if trade disputes were to intensify. Demand growth for oil tanker tonnage is expected to be solid overall. On the supply side, the scrapping of ships is likely to decline significantly in view of the improved ship earnings situation. Given the stable low level of deliveries, fleet growth is likely to be subdued. With a moderate increase in capacity utilisation, both charter rates and second-hand prices should rise tentatively overall.

Although the overall trend for the shipping markets is expected to be moderately positive, the risks have increased. The economic cycle is at its peak in some regions and the economy could be hampered further by the ongoing trade war and the imminent prospect of Brexit. The costs associated with meeting the emission targets for ships that will apply as of 2020 will also pose a burden for the markets. These increased risks are expected to lead to greater fluctuations in charter rates and ship values during the year in general.

GERMAN REAL ESTATE MARKETS

After almost a decade of an upswing, the German real estate markets are approaching their zenith in 2019. This is because the extremely low interest rates have bottomed out and the domestic economy, which has remained robust to date, is likely to lose momentum in view of the marked deterioration in the foreign trade environment since last year. This is likely to put a damper on growth on the real estate markets:

On the **housing markets** in most large cities, demand is likely to grow at a slower pace than in the past few years due to a further drop in the influx of inhabitants. It will still, however, cover the growing supply of housing resulting from brisk new construction activity, meaning that vacancy levels will remain low for the time being. The retail sector is benefiting from consumer sentiment that remains robust, as well as from rising household incomes as a result of the good labour market situation. At the same time, the growth in retail sales is declining, not least in shops in central inner-city locations. The ongoing above-average growth in online trading remains the decisive factor driving this trend. The local supply sector, especially as far as food is concerned, has so far been able to largely escape this competition.

On the **office real estate markets,** a slowdown in recruitment is likely to lead to less demand for space, albeit at a level that is still slightly above average. The number of office completions, on the other hand, is expected to rise sharply again. This is likely to satisfy most of the demand, meaning that vacancy rates will hardly fall any more. Office rents should continue to rise as a result, both in central and peripheral locations, albeit at a noticeably slower pace than in previous years.

Rents for **retail properties,** on the other hand, are likely to stagnate for the most part, especially in the prime inner-city locations, only increasing slightly in a small number of city district locations with a strong local supply situation. Rents are expected to increase more slowly, but still moderately, as the number of completions increases. The statutory limits on rent increases when apartments are re-let should also have more of a dampening effect following the supplementary measures resulting from the amendment to the legislation in 2018. Given the price level reached after the very strong increases in previous years and based on gradually rising interest rates, which will remain relatively low nonetheless, house prices and the market values of office properties will still show only a very moderate increase in 2019. The market values of retail properties are likely to dip from the current level in view of the ongoing structural change and depending on the location and the type of business.

OTHER SECTORS

The overall conditions for German growth will remain challenging in 2019, also due to foreign trade risks (such as the risk of a hard Brexit or the possible escalation of the trade conflict between the US and China). Although growth is likely to continue, economic momentum is expected to slow further.

Robust private consumption, based on a positive employment trend, strong wage increases and fiscal policy impulses argue in favour of a continuation of growth, which should support demand and, as a result, **retail trade**. A further increase in equipment investment also appears likely because companies in Germany are struggling with capacity bottlenecks, order books are still well filled and financing conditions remain favourable. Although this points to a further upward trend in industrial activity, the **manufacturing sector** and **wholesale and foreign trade** companies are also likely to lose further momentum in 2019. The **logistics sector,** in particular, is subject to the risks of a general macro-economic downturn and a weakening in global trade. **Construction output** is likely to be close to the capacity limit, meaning that no further substantial expansion is to be expected.

The increase in transport demand as a result of what is still strong global economic growth on the one hand and high maintenance requirements on the other are providing positive stimuli for investments in **transport infrastructure**. Institutional investors are likely to continue to be important.

The prospects for the expansion of **renewable energies** remain mixed as far as 2019 is concerned: whilst the capacity added is likely to stagnate at a good level overall in Europe, there are definitely growth opportunities globally. A distinction, however, has to be made between wind and solar energy as well: in the German wind energy segment, the significant correction in new capacity should continue in 2019. New installations are likely to increase again in the rest of Europe. The absolute increase in generation capacity in the solar energy sector in Germany – and also in Europe as a whole – is likely to be continue to expand in 2019 due to the European climate protection targets and cost degression. On the one hand, however, restrictions on state subsidies have produced a gloomier outlook, while on the other hand, special depreciation for a total volume of four gigawatts are planned in Germany for the years from 2019 to 2021.

BANKING ENVIRONMENT

Against the backdrop of increasing geopolitical and economic uncertainties, as well as potentially high volatility in the financial markets, the overall banking environment is expected to remain challenging in 2019. Even though the growth forecasts are currently still relatively positive, the downside potential is classed as increasingly critical due to the complex and difficult situation (e.g. trade conflicts, Brexit).

Although, with regard to monetary policy, signs are emerging of a gradual turnaround in Europe, too, this is likely to be further delayed if the economic uncertainties become more entrenched. The ECB is likely to maintain its expansive monetary policy in the first instance, meaning that the pressure on net interest income resulting from the low interest rate environment is likely to continue to increase for the time being.

In a European comparison, the need to adapt is the most pronounced on the German banking market, as German institutions have below-average sources of income that do not rely on interest, low credit margins due to the intense competition and, at the same time, very high cost-income ratios and low RoE's that are below the cost of capital as a result. As a result, while German banks are likely to reap above-average benefits from a steeper yield curve, they are still exposed to considerable pressure on profitability. As a result, the gradually increasing pace of consolidation is likely due on the one hand to the high cost pressure, while on the other, it points towards the potential to be exploited in the German banking market.

Regulators and market participants will continue to focus even more so than in the past on an increasingly comprehensive view of bank's capital and liquidity resources. This is particularly important regarding the extent to which banks are prepared for the new regulatory standards for bail-in eligible liabilities. These relevant capital and liquidity requirements that form part of the resolution mechanism include in particular the institution-specific minimum requirements for regulatory capital and eligible liabilities (MREL) defined by the national banking supervisory authorities and resolution authorities. This should provide banks with an even stronger incentive than in the past to optimise the increasingly granular liability side of their balance sheets as they attempt to strike a balance between regulatory requirements on the one hand and cost considerations on the other.

In addition, further fundamental adjustments are already emerging. The changes summarised under Basel IV, which, amongst other things, will serve to improve the comparability of RWA profiles and the reduction of complexity concerning risk identification, are at the same time aimed at the harmonisation of supervisory practices in the EU and are designed to improve transparency vis-à-vis the markets. The focus here is on the banks' internal models for calculating risk.

Expected business development of Hamburg Commercial Bank

Financial key management indicators			
	2018	2019 forecast	Strategic objective for 2022
RoE (%)	2.2	A ratio of between 1 % and 3 % is expected	>8
CIR (%)	27.2	A significant increase in the CIR is planned, as favourable one-off effects will not occur again	<40
CET1 ratio (%) (in-period)	18.5	The CET1 ratio is expected to be significantly above the regulatory requirements	≥16
LCR (%)	225	The ratio is expected to continue to be comfortably above the regulatory requirements	>140
NPE ratio (%)	2.0	A ratio of around 2 % is expected	<2
Non-financial key management indicators			
	2018	2019 forecast	Strategic objective for 2022
Rating	Baa2/BBB	Stable at the level already achieved	Baa1/BBB+

Key basis for the forecast
In its corporate planning, the Bank generally assumes that:

- the interest rate environment in Europe will slowly return to normal in the coming years and the ECB will begin to raise interest rates for the first time in 2020,
- the seamless transition to the deposit protection fund for private banks that has been agreed for 1 January 2022 will be achieved as planned and the Bank will meet the conditions set out in the Statute for participation in the ESF by the end of 2021,
- operating performance will be gradually improved by implementing the transformation programme and, above all, the earnings and cost ratios will improve significantly,
- the reduction of administrative expenses and the planned reduction in personnel can be implemented within the planned period and scope. Within this context, the Bank communicated the transformation programme immediately after the closing date at the start of December 2018, providing its social partners with all of the necessary information. In order to implement the HR objectives accordingly, negotiations on the social plan and reconciliation of interests with the works council need to be concluded,
- the bank-specific funding costs will fall as a result of the optimisation of the funding structure.

The Bank is systematically implementing its transformation programme. The business strategy, which is strictly geared towards an appropriate return on equity, and the systematic restructuring moves will support the achievement of the strategic objectives and, as a result, the sustainable realignment of the business model.

In 2019, one key focal point will be measures to optimise the organisational and cost structure. The Bank is currently negotiating a reconciliation of interests and a social plan with the works councils with the aim of clarifying the situation for employees as quickly as possible and implementing the measures as soon as possible. With regard to planned operating cost reductions, the optimisation of the IT infrastructure is extremely important. In this respect, establishing an efficient IT platform is a top priority. The current IT landscape is geared to the individual needs of the past. Now that the capital structure has been restructured, the Bank must become more standardised and streamlined if it wants to achieve its ambitious cost targets and, at the same time, open up scope for new business approaches. The forthcoming IT transformation programme will introduce a state-of-the-art, integrated and standardised application landscape. The workstation infrastructure will be aligned towards mobility and cloud use. This will reduce complexity and costs and increase flexibility and scalability. Hamburg Commercial Bank relies on the capabilities of a strategic partner to operate the application landscape and meet the challenges associated with transformation. Successful IT transformation is to be used to cut IT costs by around 40 % by 2022 as against the actual costs in 2018.

In addition, all other packages of measures under the transformation program will be vigorously pursued in order to establish a sustainably viable and flexible business model and, in doing so, lay the foundation for the Bank's successful survival in a rapidly changing and challenging environment.

In view of the operational measures identified and taking into account the fundamental aspects referred to above, the Bank expects to generate a slightly positive pre-tax net result in 2019 and, on this basis, a low positive RoE for the Group. The cost-income ratio, on the other hand, will increase considerably to begin with, as it was significantly overstated on the reporting date due to positive one-off effects. After adjustments to reflect the positive one-off effects, the cost-income ratio came to well in excess of 60 %. The Bank will gradually achieve its strategic target of a maximum of 40 % as part of the restructuring process. With regard to the CET1 ratio and the LCR, the Bank assumes that these ratios, which were at a good level as at the reporting date, will both comfortably exceed the regulatory requirements in 2019, too. On the basis of the risk-relieved balance sheet structure, it is assumed that the NPE ratio will come in at around 2 %, in line with the Bank's strategic objective. In general, the Bank expects that the planned progress made in the transformation process will have a positive effect on the rating agencies' assessment, meaning that its rating position, which improved after the closing, will be strengthened further.

The Bank addresses the main opportunities and risks associated with the forecasts below. Opportunities are defined as possible future developments or events that may give rise to a positive divergence from the forecast or an objective for the Bank. In contrast, as part of the forecast report, risks are defined as possible future developments or events that may give rise to a negative divergence from the forecast or an objective. The bank-specific risk types are then separately explained in the Risk report.

General opportunities and risks

A) ECONOMIC FACTORS

In view of the aforementioned global economic risks (in particular the risk of a hard Brexit or the possible escalation of the trade conflict between the US and China and the resulting economic risks for Europe as well), there is a danger that growth will be significantly weaker and developments on the financial markets significantly more volatile than the Bank has assumed in its planning. In general, macroeconomic risks are currently on the rise, meaning that the probability of downside scenarios and resulting burdens on earnings is increasing.

On the other hand, a more rapid resolution of the existing uncertainties would have a positive impact on the development of macroeconomic factors taken into account in the planning, thereby favouring the Bank's profitability.

B) INDUSTRY-SPECIFIC FACTORS

Against the backdrop of the risks to global trade, developments on the shipping markets could slow considerably. The export-oriented German economy could also suffer more in such a scenario than assumed in the planning. On the other hand, a more hesitant turnaround in the ECB's monetary policy would generally have a positive impact on the development of the real estate markets, in particular.

In addition, there is the risk that interest rates will remain low and that funding spreads for banks will also increase, which could have a negative impact on funding costs and, as a result, on earnings.

C) REGULATORY ENVIRONMENT

New regulatory initiatives, but in particular the discussion regarding the risk parameterisation of internal models in the run-up to Basel IV, could potentially result in higher capital requirements for banks.

D) COMPETITION/DIGITALISATION

The fierce competition in the German banking market, especially in the persistently low interest rate environment, is still putting pressure on asset margins and profitability in the lending business. On the other hand, digitalisation offers opportunities for optimising business processes, tapping into new sources of income and positively influencing IT developments, a trend that earnings and cost ratios, in particular, could benefit from.

Company-specific opportunities and risks

A) TRANSFORMATION PROGRAMME

If the transformation programme and, in particular, the planned cost-saving measures are not implemented as planned, it is impossible to rule out a scenario in which some costs cannot be reduced to the extent desired or not as quickly as planned. Similarly, delays in the transformation process, which could arise in connection with the ongoing negotiations with social partners or in the implementation of the measures, could have a negative impact on the extent and timing of planned savings measures. Furthermore, it cannot be excluded that the reduction in headcount associated with the efficiency measures is not implemented as planned or results in higher operational risk. The risk of losing key expertise may also be increased as a result of the personnel measures taken. Furthermore, a higher than expected employee turnover in sales divisions could make it more difficult to achieve the new business and income objectives.

On the other hand, if the transformation programme is implemented successfully, there will be an opportunity to continue to adapt the current cost-reduction structures and realise additional cost potential. This potential could arise from possible synergies and, where appropriate, from new strategic options. The measures to have the individual locations focus on particular areas - business centre in Hamburg and tasks relating to operations and IT in Kiel - could also make a positive contribution in this regard. The Bank is confident that it will achieve its stated objectives after also taking account of the successes already achieved in the past. The rapid and success ful implementation of the transformation programme would make a significant contribution to a sustained increase in efficiency and the long-term stabilisation of the Bank's business model.

B) TRANSITION/MEMBERSHIP OF DEPOSIT PROTECTION FUNDS

Agreements have been reached regarding Hamburg Commercial Bank's inclusion in the deposit protection fund for private banks as of 1 January 2022 that provide a reliable framework for its seamless transition to full membership of the deposit protection fund (ESF). If the agreements reached are not adhered to and, as a result, or for other reasons, the Bank is not admitted to the guarantee system of the Association of German Banks as of 1 January 2022 as planned, this could lead to a notable outflow of deposits and a marked increase in funding costs.

Also as a result of the different manner in which the deposit guarantee funds work, i.e. institutional protection under the protection system of the German Savings Banks Finance Group versus protection of deposits, there is a risk of liquidity outflows associated with the change in the deposit guarantee fund.

Hamburg Commercial Bank may also be required to make special payments because of its membership of the support fund of the Landesbanks and the European bank levy in the event that future compensation and support measures result in the underfunding of these organisations. It is currently not possible due to the calculation method used, which is based on the relative development of institution-specific parameters compared to the sector, to assess whether and to what amount such payments will arise. However, such payments may adversely impact earnings in general.

C) TRANSFORMATION PHASE

The objective being pursued with the Bank's realignment is the sustainable and profitable restructuring of its business model. In order to achieve the ambitious strategic objective, both the successful implementation of the transformation programme and acceptance among market participants - in particular for the implementation of the funding targets - and other relevant stakeholders are essential.

Details on the bank-specific risk types are explained in the Risk report section.

Overall appraisal and net income forecast

The overarching financial objective of Hamburg Commercial Bank is to achieve a return on equity of more than 8 % in order to considerably increase the value of the equity contributed and, as a result, the value of the company. The privatisation process led to the launch of an extensive transformation programme spanning a period of several years that is scheduled to be concluded in full in 2022 and will involve the operational and financial restructuring of the Bank. In 2019, the Bank will be focusing on boosting its operational performance. In order to achieve this objective, it will be forging ahead systematically with the measures developed as part of the transformation programme. Due to the existing and increasing uncertainties and the challenges faced by the banking environment, the Bank has to implement the restructuring process in a stringent and rapid manner. This will ensure that the corporate structure is developed further in a cost-effective and sustainable manner and, at the same time, will ensure the agreed seamless transition to the deposit protection fund for private banks will be ensured.

On the basis of what was generally satisfactory performance of the IFRS Group in the 2018 financial year, the Bank is confident, from today's perspective, that it will be able to achieve the targets it has set for 2019 as a whole. The 2019 financial year will be characterised by the implementation of the operating income and cost measures and, in particular, by the planned reduction in personnel. The individual measures implemented, such as organisational changes and extensive adjustments in the area of HR, will be continuously reviewed as part of the measures controlling process and adjusted where appropriate to ensure the successful implementation of the transformation programme.

Taking into account the restructuring provisions set up as at the reporting date, the Bank expects to achieve slightly positive IFRS net income before taxes in 2019. The earnings forecast is subject to any unforeseeable effects resulting from the implementation of the restructuring process.

The earnings forecast and future development of Hamburg Commercial Bank are associated with major challenges, which are described in detail in both the forecast and the Risk report.

Risk report

Risk management system

Principles of risk management

Active risk management represents a core component of the overall bank management at Hamburg Commercial Bank. The current version of the Minimum Requirements for Risk Management (MaRisk) laid down by the Supervisory Authorities serves as the main framework for the design of our risk management system. In addition, comprehensive requirements of the European Supervisory Review and Evaluation Process, SREP, and the henceforth applicable ECB guides for the Internal Capital Adequacy Assessment Process (ICAAP) and Internal Liquidity Adequacy Assessment Process (ILAAP) must be observed.

Hamburg Commercial Bank defines risk as the threat that unfavourable future developments may adversely affect the Bank's assets, earnings or financial position.

Hamburg Commercial Bank conducts an annual risk inventory in order to identify material risks as defined by MaRisk. This includes a review of the existing quantitative and qualitative criteria for determining materiality taking due account of the Bank's risk appetite and if necessary such criteria are redefined. Based on the results of the risk inventory risks are broken down into "financial risks" and "non-financial risks". Financial risk is defined as the risk of a change in the value of an asset having an impact on the financial figures. Non-financial risk is the risk of losses arising from inadequate internal procedures, controls and the Bank's operating activities. Whilst the Bank by itself has hardly any influence on the movement in value of an asset, but can maintain a capital or liquidity buffer for this, non-financial risks can be influenced by the Bank itself primarily through stringent management, adequate staffing and resources and a risk appetite derived from the risk culture. A non-financial risk governance process under the overall responsibility of the Group Risk Management and Compliance divisions was implemented in 2018 that ensures that the NFR is managed on an integrated and stringent basis. The material risk types at Hamburg Commercial Bank that can be quantified include default risk, market risk, liquidity maturity transformation risk as a type of liquidity risk for financial risks and operational risk, which also includes legal and compliance risks, for non-financial risks. These risk types are taken into account in assessing the capital adequacy.

In addition to insolvency risk (financial risk) as a second type of liquidity risk other material risk types of Hamburg Commercial Bank include business strategy risk and reputation risk as so-called "Other NFR". Default risk is the most significant risk type based on Hamburg Commercial Bank's business model.

Determination of risk appetite and risk guidelines

The Strategic Risk Framework (SRF), which serves as the foundation of the risk culture, sets out the focus of the Bank's risk management activities and defines the objectives of risk management based on the planned development of key business activities and measures taken to achieve these objectives. The focus is on securing and allocating scarce resources as well as ensuring a sustainable revenue optimisation taking into account the risk appetite, business strategy objectives, the market environment and both the existing and planned portfolio.

The transformation into a profitable private bank, implementation of the objectives of the new owners and meeting of the requirements of other stakeholders (especially the banking supervisory authorities, Deposit Guarantee Fund of the Association of German Banks) is supported by the SRF guidelines.

The SRF contains the risk strategy principles as the key guidelines for risk-conscious action and cornerstone of a sustainable risk culture. These form the framework for the formulation of the risk appetite statement (RAS) and risk strategy. The RAS is broken down into a financial and non-financial RAS on the basis of the risk inventory and is aimed at providing a condensed description of selected risk appetite areas in order to achieve the Overall Bank's objectives. The financial RAS consists of a catalogue of key figures and ratios, the non-financial RAS of qualitative targets regarding the risk culture. Their implementation is ensured via the risk strategy and limit system, whereby the risk strategy describes the management of risks based on the risk inventory in accordance with the business strategy and RAS. It provides the framework for the sub-risk strategies (counterparty default for performing and non-performing exposure respectively, market and liquidity risks, non financial risk {NFR} along with reputation risk and operational and business strategy risks) and forms the foundation of the business strategy and a key basis for planning within the Bank.

Key risk indicators of the Group

A functioning limit system requires that the risk appetite be derived on a rigorous basis. This is derived separately for the three scarce resources – regulatory and economic capital and liquidity – from the risk capacity. Starting from the risk appetite the Bank has established a system of risk limits and guidelines for all three resources, which serves to avert risks that could jeopardise its continued existence and to achieve the risk strategy objectives.

The SRF is approved by the Management Board ("tone from the top") and reviewed at least once a year. Where necessary, adjustments are made during the year. It is also fully integrated into the Bank's processes, for example by its embedding in the Bank's objectives and the definition of guidelines for the strategy process, in risk reporting and the Code of Conduct.

Key risk indicators of the Group

	31.12.2018		Limit		Guideline
ICAAP utilisation from an economic perspective/RBC	**43 %**	**<**	**90 %**		**–**
Economic capital required (in € bn)	**1.6**	**<**	**2.5**		**–**
of which: for default risks	1.1	<	1.4		–
for market risks	0.2	<	1.0		–
for liquidity risks	0.1	<	0.3		–
NPE ratio	2.0 %[1]		–	<	3,0%
CET1 ratio (same period calculation, including Pillar 2 requirement)	18.5 %	>	11.5 %		–
T1 ratio (same period calculation)	18.5%	>	13.0 %		–
Overall capital ratio	23.4 %	>	15.0%		–
MREL	47.0 %	>	32.2 %		–
Leverage ratio	7.4 %	>	4.0 %		–
Liquidity coverage ratio (LCR)	225.0 %	>	125.0%		–
Net stable funding ratio (NSFR)	121.0 %	>	102.0 %		–
NLP2 in the stress case (in € bn) Month 1	9.4	>	0.5		–
Month 2	10.3	>	0.5		–
Month 3	9.7	>	0.5		–

[1] The NPE ratio was 1.6 % as at the reporting date. Further defaults were recognised as a result of adjusting events identified on the basis of knowledge obtained after the reporting date, whereby the NPE ratio remains in line with the strategic objectives even after taking these defaults into account.

Organisation of risk management

The organisation of risk management at Hamburg Commercial Bank is primarily aligned to the requirements of the business model while at the same time taking regulatory requirements into account.

The Risk Committee of the Supervisory Board is in particular responsible for reviewing Hamburg Commercial Bank's current and future overall risk tolerance and strategy. In addition, it advises the Supervisory Board on the current and future overall risk tolerance and strategy and supports the Supervisory Board in monitoring the implementation of this strategy by the Management Board. The Risk Committee is regularly informed of the risk position and risk management by the Management Board in meetings.

The Overall Management Board is responsible for Hamburg Commercial Bank's risk management system including the methods and procedures to be applied for measuring, managing and monitoring risk and thereby for ensuring that it is appropriate for Hamburg Commercial Bank's profile and strategy. As a member of the Management Board, the Chief Risk Officer (CRO) is responsible for risk controlling at Hamburg Commercial Bank, including risk monitoring and back office functions. In particular, this includes the Group Risk Management, Credit Risk Management as well as Loan and Collateral Management divisions.

The Group Risk Management division is responsible for the risk strategy, the risk controlling function required for regulatory purposes and the methodological guidelines and models for calculating all risk-relevant components. The division develops the methods and tools for identifying, measuring, managing and monitoring risks and, by setting risk limits and risk guidelines, supports operative portfolio management, for which BU Bank Management is largely responsible.

Credit Risk Management is responsible, among other things, for credit risk analysis, including the preparation and setting of the internal rating and drafting of the credit applications for the Bank's entire lending business. Credit Risk Management is also responsible for designing the processes and rules that apply to the lending business within Hamburg Commercial Bank.

Special Loan Management is responsible for managing the workout and restructuring of loan commitments.

Loan and Collateral Management is responsible for the settlement and administration of the lending business as well as for obtaining and ongoing valuation of loan collateral.

Trading transactions are settled in the Transaction Banking division, the risk monitoring of which is carried out in Group Risk Management.

The market and trading divisions are directly responsible for risks and income within the scope of their business activities and thereby make an active contribution to the Bank's risk management.

A regular, internal review of the ICAAP is performed at Hamburg Commercial Bank in accordance with the requirements of Articles 73 and 74 CRD IV across 3 lines of defence, including the business divisions and independent internal control functions (Risk Management and Controlling, Compliance and Internal Audit amongst others) based on their respective tasks and responsibilities. Accordingly, the operating activities of all divisions form the first line of defence. In principle, a distinction is made between risk takers and risk managers pursuant to SREP GL 276b in the demarcation of the control and monitoring units.

The risk manager is responsible for managing the risks for which he is responsible within the framework of the applicable standards and guidelines (risk ownership). This task results from the responsibility for, e.g., processes, clients, employees, products, models and/or systems.

The risk taker is primarily responsible for the appropriate use of systems and/or models as well as for process-compliant conduct in order to avoid or reduce operational risk related to his activities.

By means of the PDCA cycle, i.e. Plan (planning of objectives, measures), Do (implementation), Check (measuring the effectiveness of the measures and report), Act (identification of corrections) – only within the 1st line –, this separation can be described as follows: The risk manager plans and checks, the risk taker does and acts when necessary.

The task of the first line of defence is to also provide the divisions in the second line of defence (II a and II b) with all relevant information, so that this can be analysed, evaluated and processed by them. The first line of defence's obligation to cooperate is therefore highly relevant for a functional risk management process.

The II a line of defence is basically responsible for monitoring and controlling as well for determining the procedures for setting the limits for the relevant risks. It is defined by the officer functions required by law but also by similar monitoring activities in other areas of the Bank. The divisions in the II a line of defence also act as risk managers in specific cases, such as BU Legal & Taxes for legal and tax risks or BU Human Resources for personnel risk.

The overarching II b line of defence is the responsibility of the GRM (responsible for OpRisk controlling) and Compliance (works towards legal and regulatory compliance) divisions.

Internal Audit forms the third line of defence and provides independent and objective auditing and advisory services, which are aimed at creating added value and improving the business processes. It supports the organisation in achieving its objectives by evaluating the effectiveness of risk management, the controls in place and the management and monitoring processes under a systematic and targeted approach and helping to improve these. Internal Audit monitors and validates the timely elimination of deficiencies identified by the Bank's own activities or external audits. As a tool used by Hamburg Commercial Bank's Overall Management Board it is an essential component of corporate governance. It regularly provides the Overall Management Board and Audit Committee of the Supervisory Board with information on the findings of its audits, which are carried out on the basis of a risk-based audit plan that is approved by the Overall Management Board on an annual basis.

The CRO makes decisions independently of the Management Board member responsible for the Market divisions and Trading and periodically informs the Overall Management Board and Risk Committee of the risk situation of the Hamburg Commercial Bank Group. In this way the separation of functions required under the regulatory rules between the market and trading divisions on the one hand and risk controlling, settlement and control as well as back office on the other is taken into account at all levels of the Bank from an organisational perspective.

Business areas are managed in line with uniform Group standards on the basis of a Global Head principle. Based on this, the heads of the individual divisions as the respective Global Heads are responsible on a Group-wide basis for the strategy of the business areas assigned to them and have the disciplinary responsibility for the employees working in their business area. The Global Heads are supported by the head of the respective foreign branch (General Manager) in the implementation of the strategy on site in the foreign branches whilst maintaining the separation of duties in accordance with MaRisk. The General Manager is responsible for compliance with local legal and regulatory requirements. The global head principle also applies to risk controlling to ensure that a Group-wide coordinated risk controlling process is in place.

Hamburg Commercial Bank has stipulated rules in accordance with the MaRisk requirements, under which formalised audit processes are gone through prior to entering into transactions in new products or new markets (NMNP processes). This ensures that the products are properly considered under risk aspects in the relevant systems and reflected in the relevant processes and their effectiveness ensured and that transactions involving new products or new markets are only entered into with the approval of the Management Board. There is also an NPNM review process in place under which the appropriate mapping of older products is reviewed on a regular basis.

Hamburg Commercial Bank uses an "economic scope of consolidation" as the basis for the Group-wide risk management. It includes those entities that are to be specifically monitored at the Group level due to material risks.

Risk management by a central committee structure

Committees with the following composition and tasks were in place in 2018 to support the Management Board in monitoring and managing all significant risks: In addition to the members of the Management Board the committees are composed of the heads of the risk and other departments, which ensures that information regarding questions on risk is regularly exchanged. Insofar as internal or external regulations do not permit delegation of decisions to the committees, such decisions are prepared by these committees for approval by the Overall Management Board.

The Overall Bank Management committee (OBM committee), which is chaired by the Chief Financial Officer (CFO) and Chief Risk Officer (CRO), is the committee responsible for managing and allocating financial resources within the risk limits, risk guidelines and plan targets. Its duties include, inter alia, the monitoring and management of risks associated with bottleneck resources (including risk concentration, credit, liquidity as well as FX and interest rate risks). The OBM committee also looks at market risk positions that serve the Bank's strategic goals. This means that the OBM drafts decisions on strategic guidelines, the type of management, objectives restrictions and other targets for the corporate investment portfolio. The relevant decisions are made by the Overall Management Board. The risk limits adopted by the Management Board are monitored by the units with operational responsibility. Risk limit overdrafts are escalated to the Management Board together with recommended courses of action and the implementation of measures to reduce such overdrafts is monitored. Furthermore, the OBM Committee is the body responsible for monitoring the recovery plan indicators and drafting all resultant decisions.

The Scenario Steering Committee (SSC), in which the trend of market indicators is monitored and decisions made regarding simulation assumptions and scenarios (macroeconomic and segment-specific), provides significant support to the OBM committee. The simulation scenarios together with their key assumptions and an analysis of the results are also presented to the Overall Management Board in addition to the OBM Committee. The OBM has also been supported by the Model Steering Committee (MSC) since 2018. MSC's objective is to discuss model developments and validations and model risk governance across GRM and to approve such–in accordance with the relevant decision-making competence–or draft a decision for the OBM Committee.

The Credit Committee (CC) is an independent, decision-making body at the level of individual lending transactions, which is chaired by the head of the Credit Risk Management (CRM) division with the participation of the CRO on a case-by-case basis. Operating profitability is managed at the individual deal level by the CC in order to meet the Overall Bank's profit targets. The committee also performs an active portfolio management function to achieve ongoing improvements in portfolio quality (diversification, granularity) and makes individual lending decisions from a credit risk perspective. When necessary, the committee also operationally manages the utilisation of limited bottleneck resources. The CC is guided by the requirements for Group resource management defined in the OBM committee.

The Business Review Meeting (BRM), chaired by the CRO and with the involvement of the Management Board member responsible for the Market divisions and selected division heads, regularly monitors the achievement of targets by the divisions with regard to new business, income and costs and discusses other general topics of strategic importance. The analysis is used as a basis for identifying any plan variances at an early stage and initiating any possible measures, such as the allocation of new income or cost targets.

The completed transformation of the Bank and associated change in the organisational structure will also entail a change in the committee structure.

Risk reporting and measurement systems
Hamburg Commercial Bank maintains a central data storage system, which takes into account supervisory requirements, for the purposes of analysing, monitoring and reporting risks. Risk reporting is generally ensured by means of the management and reporting systems in the Group Risk Management division. The risk management systems ensure effective risk management and are adequate with regard to Hamburg Commercial Bank’s profile and strategy.

The following key reports are prepared for the overall risk:

- The management report, which as an integrated financial and risk report provides information on Hamburg Commercial Bank’s overall situation with regard to the key value drivers, particularly income, costs, liquidity, capital and risk as well as on the trend of the recovery plan indicators, is submitted to the OBM committee, Management Board and also the Risk Committee (relevant extracts thereof). Adherence to the risk limits and risk guidelines laid down in the SRF and relevant for managing economic capital is monitored by means of this report. The management report also includes reports on problem loans and new business in addition to information on the trend of the relevant key default risk figures, structural analyses on business areas and conspicuous individual commitments. It also includes the profit centre accounting, rating validation results and rating migration development as well as information on the monitoring and management of country risk. The management report is generally prepared on a monthly basis. In addition, it is updated on a weekly basis for selected key figures and ratios.
- The Risk Committee also receives for its quarterly meetings the trend of aggregated risk parameters of Hamburg Commercial Bank in the form of the "current risk trend" report.

The management reporting policy sets out the management requirements regarding the structure, contents, frequency, deadlines and form of the internal reporting combined in the management report.

Other overall risk reports include the Disclosure Report under Part 8 of the Capital Requirements Regulation (CRR) and the Risk Report in the Annual Report. In addition to risk reports on the overall risk there are reporting instruments based on the risk type. The Management Board is informed on a daily basis of the market risk and earnings trends as well as the extent to which limits are utilised and the CRO and the divisions concerned are informed of the insolvency risk trend in the Normal Case and Stress Case. The OpRisk Steering Committee receives a quarterly report regarding the development of the risk position, material loss events and management measures addressed. The Overall Management Board is informed once a year regarding the capital required, the loss event trend and material loss events and loss potential as well as any measures required.

Internal control system

BANK-WIDE INTERNAL CONTROL SYSTEM
The Management Board of Hamburg Commercial Bank bears the overall responsibility for ensuring that a proper business organisation is in place at the Hamburg Commercial Bank Group, including an appropriate and effective internal control system (ICS).

The ICS of Hamburg Commercial Bank is based on a bank-wide main and sub-process structure (process map), which also includes the domestic and foreign branches. A person responsible for the process is designated for all main processes.

The top priorities of this ICS assessment are the structured and systematic examination of potential or known process risks together with the definition of and decision on measures to be taken to mitigate them. Furthermore, the ICS makes a contribution to the effectiveness of the processes by specifying uniform rules for the Bank as a whole. An implemented ICS cycle also ensures that the ICS is continuously enhanced with respect to its correctness and functionality as well as its appropriateness and effectiveness. Clear roles and responsibilities are defined within the ICS cycle to ensure that the tasks are performed in a proper manner.

Central responsibility for the management and monitoring of the ICS as well as for methodology guidelines and their enhancement lies with the ICS Office in the Corporate Compliance organisational unit.

It is also responsible for carrying out random quality assurance checks and appropriate reporting to the Management Board and Supervisory Board.

In order to ensure that the system is functioning on a sustained basis, the process is closely monitored by means of continuous communication and governance throughout the Bank.

The Bank’s sub-processes are defined annually for the control cycle based on the degree of risk determined and the last cycle run through. In addition, the outsourcing of material functions is reported to the Management Board on an annual basis via the ICS management process.

Furthermore, subsidiaries of Hamburg Commercial Bank are classified annually as to the materiality of their respective processes for the Bank’s ICS. The processes of all subsidiaries classified as material are integrated into the Bank's ICS management processes.

INTERNAL CONTROL SYSTEM WITH REGARD TO THE ACCOUNTING PROCESS

The Finance division is responsible for the process of preparing the consolidated and single-entity financial statements of Hamburg Commercial Bank and the correctness of the Group accounting methods. The internal control system for the accounting process should ensure compliance with the rules to be applied and generally accepted accounting principles. This should maintain a quality standard that ensures a true and fair view of net assets, financial condition and earnings situation. The written rules including all internal instructions and regulations form the essential basis of the ICS.

The accounting process is reviewed on a regular basis by the responsible member of staff in charge of the process and adjusted to the current framework conditions and requirements. In addition the accounting process is audited by the Internal Audit division from a process-independent perspective.

The organisational structure of the Finance division supports the internal control system. A comprehensive quality assurance is performed by another organisational unit with regard to the accounting functions for lending transactions and capital market transactions in Germany and transactions in subsidiaries and foreign branches. This organisational unit is also responsible for consolidating the accounting information and preparing the annual and consolidated financial statements. In addition, this unit centrally monitors amendments to legislation concerning financial statements, in order to ensure uniform application of the standards.

Regulatory requirements

Hamburg Commercial Bank determines the amount of regulatory capital backing for default, market and operational risks as well as for risks resulting from credit valuation adjustments (CVA) of OTC derivatives on the basis of the CRR requirements. In this context, the so-called IRB Advanced Approach is applied for default risk, for which the supervisory authority has issued the relevant authorisation to the Bank. The Credit Risk Standardised Approach (CRSA) is used for a small part of the portfolio. This means that the Bank applies consistent parameters for regulatory reporting (COREP) and the internal default risk management of the IRBA portfolio. Hamburg Commercial Bank determines the amounts allocated to market risk positions in accordance with the prescribed or optional standard procedures. Hamburg Commercial Bank takes account of operational risk under the standard approach. Hamburg Commercial Bank uses the standard method for CVA.

In accordance with the requirements of Part 8 CRR in conjunction with Section 26a (1) Sentence 1 KWG Hamburg Commercial Bank publishes material qualitative and quantitative information on equity capital and risks incurred in a separate Disclosure Report. As an institution that uses the IRB Advanced Approach for nearly the whole portfolio, particular requirements apply to Hamburg Commercial Bank in this context. The document provides more information than that disclosed in this Annual Report on the basis of the accounting principles applied, as it provides a comprehensive insight into the regulatory framework and the Bank's current risk situation based on regulatory figures. The Disclosure Report as at 31 December 2018 is available on our website, www.hcob-bank.com, four weeks following publication of this Annual Report. The Disclosure Report does not form part of the Management Report. With its publication Hamburg Commercial Bank has implemented the requirements of the third pillar of the Basel Accord (market discipline). The requirements regarding the disclosure of risk management objectives and policies in accordance with Article 435 (1) CRR and (2)(e) CRR are implemented in this risk report. The description of the approach required in accordance with Article 438 (a) CRR, under which the institution assesses the adequacy of its internal capital to support current and future activities (capital adequacy process), is also included in this risk report. The same applies to the description of the approaches and methods adopted for determining specific and general credit risk adjustments under Article 442 (b) CRR.

REQUIREMENTS UNDER THE SUPERVISORY REVIEW AND EVALUATION PROCESS

The objective of the Supervisory Review and Evaluation Process is the review of the business model, governance, risk situation as well as the capital and liquidity utilisation. Based on the analyses the supervisory authorities may specify requirements for capital and liquidity utilisation that exceed the existing minimum regulatory requirements.

As part of the supervisory process within the Banking Union, Hamburg Commercial Bank was assigned individual minimum capital ratios by the ECB that are reviewed annually as part of the SREP process. These capital ratio requirements were adhered to at all times during the reporting period. The regulatory disclosure pursuant to the CRR is on a "not in-period" basis, i.e. balance sheet amounts as at the reporting date only included in part. In addition, the minimum regulatory capital ratios are tested under the normative perspective in the ICAAP over a multi-year time horizon in a base and stress scenario in the future. Since January 2018, a CET1 SREP requirement of around 10.2 % and a total SREP capital requirement of 13.7 % (Pillar 2 Requirement "P2R" including the combined capital buffer requirements) have applied to the Bank. The capital buffer requirement was reduced by the supervisory authorities by 0.32 percentage points as at the 2018 year end, as the Bank is no longer classified as systemically important as defined in the capital buffer requirements.

Regulatory capital ratios[1)]

(%)	31.12.2018	31.12.2017
Overall capital ratio	23.3 %	31.4 %
Tier 1 capital ratio	18.4 %	23.2 %
CET1 capital ratio	18.4 %	18.7 %
CET1 capital ratio (full Basel III implementation)	18.4 %	17.8 %

1) Not in-period: regulatory disclosure pursuant to the CRR (balance sheet amounts as at the reporting date only partially included).

Regulatory capital[1)]

(€ bn)	31.12.2018	31.12.2017
Regulatory capital	5.2	7.0
of which Tier 1 capital	4.1	5.2
of which CET1 capital	4.1	4.2
of which Additional tier 1 capital	–	1.0
of which supplementary capital	1.1	1.8

1) Not in-period: regulatory disclosure pursuant to the CRR (balance sheet amounts as at the reporting date only partially included).

Risk weighted assets (RWA)[1)]

(€ bn)	31.12.2018	31.12.2017
Market risks	1.0	2.0
Operational risks	1.7	1.3
Credit risks	19.0	18.6
Other RWA	0.4	0.3
Total RWA	**22.1**	**22.2**

1) Not in-period: regulatory disclosure pursuant to the CRR (balance sheet amounts as at the reporting date only partially included).

The SREP requirement applicable to the financial holding group of HSH Beteiligungsmanagement GmbH as holding company up to the closing of the privatisation was adhered to at all times. As at the 2018 year end the Bank is no longer part of the financial holding group. Adherence to the previous SREP requirements therefore also ceases to apply at the year end.

The regulatory CET1 capital ratio calculated on a not in-period basis for the single entity in accordance with HGB accounting standards was 18.2 % as at 31 December 2018 (previous year: 21.2 %). The decrease in the aggregate RWA in particular had a positive impact in this regard. The corresponding Tier 1 capital ratio reached 18.2 % (previous year: 25.4 %), the corresponding overall capital ratio amounted to 22.9 % (previous year: 30.7 %). The single entity (HGB) regulatory requirements for capital ratios were adhered to at all times during the reporting period.

Risks for the capital ratio trend

Risks may arise from the regulatory environment, for instance from interpretation decisions or audits, in addition to the risks for the capital ratios set out in the stress test section.

It is possible, for example, that additional individual and increased capital requirements could arise from the regular SREP process carried out within the Banking Union. Additional discretionary decisions made by the supervisory authorities and industry-wide capital requirements (capital buffer for systemic and anti-cyclical risks) could therefore result in higher capital requirements. Discretionary decisions made by the supervisory authorities with regard to model risks and validations may result in increases in RWA and thereby adversely impact the capital ratios for future LGD/PD estimates in the internal models.

As part of the restructuring and optimisation of the capital structure all of the Bank's silent participations were cancelled as at the end of 2018. Outstanding hybrid capital instruments will be either cancelled in 2021 at the HGB carrying amount recognised in the 2020 financial year or repaid by the Bank before the redemption date in 2021 as part of a voluntary buy-back offer. The cancellation of the existing silent participations result in a reassessment of the cash flows of the hybrid instruments. The reassessment of the cash flows results in carrying and repayment amounts significantly below the nominal value as well as in non-eligibility of these instruments for the regulatory capital as at the 2018 year end. Individual and groups of investors in hybrid instruments have taken legal action against the Bank and, in addition to establishing that their cancellation is invalid, request that they be written up to their nominal value and are claiming compensation for missed interest payments. In the event that, contrary to expectations, the plaintiffs are successful in court, the income statement and ultimately the future capital ratios could be adversely impacted to a significant extent.

If several of the risks presented (including those described in the stress test section) occur in combination with each other, the owners may be required to take additional measures to strengthen capital at all regulatory levels.

Under CRR II further burdens for the capital ratios could result from the proposed changes to the regulatory requirements – partly referred to as "Basel IV" – probably on a gradual basis from 2022 until 2027.

For Hamburg Commercial Bank, stricter rules concerning counterparty risk resulting from Basel IV will be of particular relevance. Hamburg Commercial Bank extensively uses models approved by the supervisory authorities to map counterparty risk (Internal Ratings Based Approach – IRBA). Under Basel IV, it is planned to significantly restrict the use of IRBA models by basing the capital backing more closely on the standardised approach (CSA floor), by limiting the use of the

IRBA model to certain exposure classes as well as limiting the use of internal risk parameters (Constrained IRB).

ICAAP under the economic perspective/risk-bearing capacity

Hamburg Commercial Bank has implemented the ECB guide for the Internal Capital Adequacy Assessment Process (ICAAP) as at the reporting date. Accordingly, capital adequacy is to be assessed under a normative and an economic perspective. The Bank defines capital adequacy as the ongoing safeguarding of financial stability, in the sense that risks are adequately covered by capital, in order to ensure the implementation of the objectives of the business model. By determining it on a regular basis capital adequacy forms part of the internal reporting and is closely managed and reported to the Bank's supervisory authorities.

The economic perspective serves as a basis for reviewing at a given date whether all material risks are backed by internal capital. Compared to the regulatory perspective (CRR) it is based on a significantly qualified concept of capital and a broadened concept of risk. The measurement of risks is based on refined economic methods and procedures. As part of the monitoring of the risk-bearing capacity Hamburg Commercial Bank regularly compares the total economic capital required for all material risk types quantifiable under internal procedures (overall risk) to the available economic risk coverage potential.

In addition to the regulatory Tier 1 capital modified for economic purposes, the risk coverage potential includes, inter alia, a negative balance comprising unrealised gains and losses on all assets and liabilities. A positive balance and the effects of a positive credit standing are not recognised in compliance with the ICAAP requirements.

Hamburg Commercial Bank analyses its risk-bearing capacity comprehensively on a quarterly basis as well as within the framework of its annual planning process.

The risk coverage potential amounted to € 3.7 billion as at 31 December 2018 (previous year: € 7.5 billion according to regulatory requirements applicable at that time). The decrease is primarily attributable to the amended regulatory requirements described above under the new ECB ICAAP guideline (includes, amongst other things, the discontinuation of the recognition of a positive balance comprising unrealised gains and losses on all assets and liabilities as well as the effects of a positive credit standing).

The overall risk takes into account default risk, market risk, operational risk as well as the liquidity maturity transformation risk as an element of liquidity risk. Economic capital required as an expression of unexpected losses is determined monthly for default, liquidity and market risks in a methodologically consistent manner with a confidence level of 99.9 % and a risk horizon of one year. The economic capital requirements for the individual risk types are aggregated to an overall economic risk. Risk-reducing correlations are not applied for this.

Overall economic risk increased by € 0.2 billion compared to the 2017 year end and amounted to € 1.6 billion as at the reporting date (previous year: € 1.4 billion).

In line with the risk-bearing capacity concept, market risk (value-at-risk, VaR) is scaled up on the basis of the confidence level chosen by the Bank and a one-day holding period to show the economic capital required for market risk positions for the purpose of managing risk-bearing capacity with a risk horizon of one year. The economic capital required for market risk amounted to € 0.2 billion as at 31 December 2018 (previous year: € 0.4 billion).

Hamburg Commercial Bank also uses a VaR approach to quantify the liquidity maturity transformation risk. This long-term/structural liquidity risk is an expression of the danger of increased refinancing costs for the subsequent closure of open liquidity positions. The liquidity value-at-risk (LVaR), as a measure of the economic capital required for liquidity risk, was € 50 million as at 31 December 2018 (previous year: € 46 million). On the other hand, insolvency risk, which is more important for the purposes of managing the liquidity risk in principle, is backed by a buffer of liquid funds. Information on managing insolvency risk is included in the section entitled "Liquidity risk".

Operational risks are determined by means of a modified standard approach, which also takes account of results from the scenario analyses. The corresponding economic capital required amounted to € 0.2 billion as at 31 December 2018 (previous year: € 0.2 billion).

Utilisation of risk coverage potential amounted to 43 % as at the reporting date (previous year: 19 %). The main reasons for the increase in the risk-coverage potential was the conversion to the new accounting standard (IFRS 9) as well as the new regulatory ICAAP requirements and non-inclusion of the risk-reducing second loss guarantee as at Q1 2018. The risk-bearing capacity was ensured at all times during the period under review.

The following table shows the economic risk coverage potential of the HSH Nordbank Group, the economic capital required for the individual risk types, the residual risk coverage potential buffer and the utilisation of risk coverage potential.

ICAAP/risk-bearing capacity of the Group[1]

(€ bn)	31.12.2018[1]	31.12.2017
Economic risk coverage potential	**3.7**	**7.5**
Economic capital required	**1.6**	**1.4**
of which for default risks	1.1	0.8
for market risks	0.2	0.4
for liquidity risks	0.1	–
for operational risks	0.2	0.2
Risk coverage potential buffer	**2.1**	**6.1**
Utilisation of risk coverage potential (in %)	**43**	**19**

[1] The information disclosed as at 31.12.2018 reflects the implementation of the final ICAAP guide published in November 2018.

The results determined under both the economic and normative perspective are reported to the banking supervisory authorities in accordance with the Regulation on Financial Information and Information on the Risk-bearing Capacity (Finanz- und Risikotragfähigkeitsinformationenverordnung, FinaRisikoV).

Scenario calculations

In addition to the above-described economic perspective, compliance with the regulatory capital requirements over a medium-term horizon (at least a 3-year perspective in the base and stress case) under the internal normative perspective is also assessed in accordance with the ECB Guide for the Internal Capital Adequacy Assessment Process (ICAAP). Adherence to the stipulated capital ratios and requirements is checked by means of the quarterly calculation of the regulatory capital ratios as at the reporting date and over a multi-year scenario horizon. These requirements refer explicitly to the capital planning and to dynamic scenarios in the baseline and adverse scenarios (base and downside planning). Whilst all key ratio requirements must be met in principle in the base planning, the capital buffer requirements may also not be complied with temporarily in the downside scenario. The normative approach is not limited to the Pillar I risks recognised by the regulatory capital requirements but also takes account of reciprocal relationships that have an economic effect on the key regulatory ratios.

In addition to stress tests specific to risk types, we also regularly conduct stress tests across all risk types in order to be able to better estimate the effects of potential crises on key parameters such as ICAAP/utilisation of the risk-bearing capacity, regulatory capital ratios and liquidity and thus Hamburg Commercial Bank's overall risk position. Based on observed market developments the Scenario Management Committee approves macroeconomic and segment-specific forecasts for the carrying out of dynamic stress tests. These expected and stress forecasts are also incorporated in different simulation scenarios and presented quarterly to the OBM committee and Overall Management Board.

Significant macroeconomic risks regarding the capital ratios and RWA result from a potential deterioration in the market and risk parameters in the Bank's core markets, including a stronger US dollar. The impact of macroeconomic scenarios, such as a severe economic downturn or a new crisis in the shipping markets, and a historical scenario on the Pillar I and II capital ratios and leverage ratio is regularly calculated.

If the further stabilisation of the shipping industry assumed amongst other things in the planning does not occur or there is a deterioration in the real estate market (especially real estate values) or a significantly weaker macroeconomic environment or significantly stronger USD exchange rate (downside scenario), this would result in a material deterioration in the risk parameters. In the event that this causes a deterioration in the key capital adequacy or SRF parameters or a breach of the SRF guidelines for the relevant MaSan indicators, measures would have to be taken to strengthen the capital ratios after transition into the MaSan early warning phase in order to comply with the internally required parameters and thus the regulatory requirements (Pillar 2 requirement) at the Hamburg Commercial Bank Group level. If capital buffer requirements (Pillar 2 requirement) are not met in such a scenario despite measures being taken, a capital conservation plan would then have to be prepared in accordance with Section 10i (3) of the German Banking Act (KWG). A ratio significantly above the internally set minimum figure of 15 % is expected for the overall capital ratio in the base scenario as well as in the downside scenario for the following year.

In addition, so-called ad hoc stress analyses are performed for purposes of the economic perspective, i.e. the impact of changes in risk parameters is investigated based on the current portfolio for a one year risk horizon.

The results are incorporated in Hamburg Commercial Bank's internal reporting system every quarter and analysed on a regular basis by the Management Board in terms of an action-oriented management dialogue. Besides the review of the capital adequacy for the buffer maintained for risk coverage potential, regulatory capital and liquidity maintained under the economic perspective as at the reporting date and in the different stress scenarios, this analysis is used to discuss the need for options to strengthen the financial stability of Hamburg Commercial Bank.

Hamburg Commercial Bank's recovery plan drawn up in accordance with the Act on the Recovery and Resolution of Credit Institutions (Sanierungs- und Abwicklungsgesetz, SAG) has a comparable objective. It serves both the purpose of the early identification of any resource bottlenecks using appropriate indicators and their elimination in crisis situations by means of pre-defined options. The effectiveness of the options identified, the selected recovery plan warning indicators and related processes are reviewed and substantiated in the recovery plan by means of specific stress scenarios.

The particular purpose of both processes is to ensure that the Bank is able to comply with the regulatory minimum requirements and internal guidelines even under stress conditions. In addition, Hamburg Commercial Bank carries out inverse stress tests at least once a year. Scenarios that could endanger Hamburg Commercial Bank's ability to survive are identified for these. This information is also used by Hamburg Commercial Bank's Management Board as guidance for explaining and deciding upon any action required in the event of developments that threaten the Bank's existence.

In addition to stress tests across all risk types Hamburg Commercial Bank established procedures for the early identification of negative developments at the level of individual risk types, which are discussed in the following sections.

Default risk

Hamburg Commercial Bank breaks down its default risk into credit, settlement, country and equity holding risk.

In addition to classical credit risk, credit risk also includes counterparty and issuer risk. Classical credit risk is the risk of complete or partial loss in the lending business as a result of deterioration in the counterparty's credit standing. Counterparty default risk refers to the risk that a counterparty defaults during the term of a transaction and Hamburg Commercial Bank can only cover itself by entering into a new contract in the market for the residual term at a market price that might be less favourable. Issuer risk denotes the risk that a loss is incurred on a financial transaction as a result of the default or deterioration in the creditworthiness of the issuer.

Settlement risk consists of clearing risk and advance performance risk. Clearing risk arises in the case of possible loss of value if delivery or acceptance claims pertaining to a transaction that is already due, have not been met by both parties. Advance performance risk arises where Hamburg Commercial Bank has performed its contractual obligations but consideration from the contracting party is still outstanding.

Hamburg Commercial Bank understands country risk as the risk that agreed payments are not made or only made in part or delayed due to government-imposed restrictions on cross-border payments (transfer risk). The risk is not related to the debtor's credit rating.

Equity holding risk is the danger of financial loss due to the impairment of equity holdings.

All elements of default risk referred to are taken into account within the context of equity capital management. Additional management measures are in place for risk concentrations and equity holding risks.

Organisation of default risk management

Hamburg Commercial Bank's organisational structure reflects the functional separation of duties between market and back office departments and/or risk controlling, also at Management Board level.

Credit Risk Management is responsible for the risk analysis for the lending business including the preparation and setting of the internal rating and drafting of the credit applications. Furthermore, the organisation of the bodies of rules for the lending business, including the related processes, is the responsibility of Credit Risk Management. Loan Collateral Management is responsible for the settlement of new lending business, the administration of the existing portfolio as well as the valuation and monitoring of collateral. The Special Credit Management business unit is responsible for managing restructuring and liquidation cases and the associated operational recovery and workout activities. If a commitment is classified as a restructuring case, it is transferred from the market department in question to Special Credit Management and to the appropriate restructuring analysis team within Credit Risk Management. The workout commitments are processed in the restructuring analysis teams within Credit Risk Management in close collaboration with the manager from Special Credit Management. Lending decisions for normal and intensive management commitments are made jointly by the market department in question and the back office, while lending decisions on restructuring and workout loans are made jointly by Special Credit Management and Credit Risk Management. A decision against the recommendation made by the back office unit of Credit Risk Management is excluded in each case.

Loan loss provision management falls within the remit of Credit Risk Management.

Hamburg Commercial Bank makes use of the option to dispense with the involvement of the back office departments within the meaning of the MaRisk opening clause for lending transactions in certain types of business and below certain amounts classified as not material in terms of risk.

The trading lines for counterparty and issuer risk are monitored by the Group Risk Management division. As part of the trading line monitoring the potential future exposure on currency, interest rate derivatives is recalculated daily for each client on the basis of a 95 % quantile and compared to the respective trading limit.

The Group Risk Management division is also responsible for the independent analysis and monitoring of risks at the portfolio level, independent reporting and management of country risk. This also includes ensuring portfolio transparency and independent business area analysis (including scenario simulations) and the operation of an early warning system at the individual transaction level for identifying commitments on a timely basis that are beginning to show signs of increased risk.

The principles and regulations contained in Hamburg Commercial Bank's Credit Manual, in particular on lending competencies (definition of decision-making powers for credit decisions made by the Bank and definition of decision-making powers for entering into, changing and terminating equity holdings), on limiting and reporting the concentration of counterparty default risks, the determination of the rating, treatment of collateral, loan monitoring and commitment monitoring, form the basis for the operating activities within the lending business. Credit risks, which are recognised based on the definition of a loan under Article 389 of the Capital Requirements Regulation (CRR), are thereby considered and treated differently based on collateral, loan type, rating category and type of credit risk. The basis is Hamburg Commercial Bank Group's total exposure per group of connected clients (GCC) as defined in Article 4 (1) no. 39 CRR, whereby the bearer of the economic risk is always to be regarded as the relevant borrower.

Hamburg Commercial Bank has defined valuable collateral in order to differentiate between collateralised and non-collateralised loans. The focus is placed on meeting the requirements of the CRR (e.g. availability of a market value, ability to realise the collateral, no correlation to the collateralised loan, legal enforceability, and matching maturities). The range of approved collateral can be expanded following an assessment carried out by a team independent of the Market divisions consisting of specialists from the Credit Risk Management, Group Risk Management and Legal & Tax divisions.

Credit risk management for single risks is supplemented in particular by instructions on commitment monitoring and early identification of risks and the EAD/RWA limit monitoring based on default risk for specific sub-portfolios (real estate, LBO, Shipping amongst others), which was approved in the SRF.

Default risk management

In line with the strategic focus of Hamburg Commercial Bank–as one of the leading bank partners of larger medium-sized enterprises–with lending as its anchor product, default risk accounts for the largest proportion of the Bank's overall risk potential. In order to measure and manage this risk, Group Risk Management uses procedures and methods that are continually reviewed and enhanced to ensure they are appropriate.

Key default risk parameters are the expected and unexpected loss. The expected loss is equivalent to the default which is expected within one year on a given probability of default (PD), loss given default (LGD) and exposure at default (EaD) for a borrower. The EaD is the expected loan amount outstanding taking into account a potential (partial) drawdown of commitments and contingent liabilities that will adversely impact the risk-bearing capacity in the event of a default. The maximum amount, by which an actual loss can exceed the expected loss with a specified probability (99.9 %) within a specified time period (one year) is described as the unexpected loss. PD, LGD and EaD are also relevant risk parameters in this context. Economic capital required is determined for internal management purposes on the basis of the calculation of the equity capital backing in accordance with CRR taking due account of any adjustments that are justified on economic grounds. In addition, institution-specific asset correlations, granularity surcharges for covering existing risk concentrations are taken into account in determining the economic capital required for default risk.

The economic capital required for default risks amounted to € 1.1 billion as at the reporting date (previous year: € 0.8 billion). The increase in the economic capital required for default risk is due to the transition to IFRS 9.

Non-performing exposure (NPE), which is the total of all risk positions of borrowers in default, serves as an important management indicator that has also been defined as a risk guideline in the SRF. The trend in the NPE ratio has been influenced significantly by the introduction of the IFRS 9 accounting standard and the associated fair value accounting. The NPE ratio has decreased significantly in line with expectations. This is due to the disposal of non-performing legacy loans as part of the portfolio transaction, which resulted in a substantial reduction in risk on the Bank's balance sheet. The NPE ratio was 1.6 % as at the reporting date. Further defaults were recognised as a result of adjusting events identified on the basis of knowledge obtained after the reporting date, whereby the NPE ratio remains at around 2.0 % and therefore in line with the strategic objectives even after taking these defaults into account.

In addition, the NPE coverage ratio AC (ratio of total loan loss provisions recognised on the non-performing exposure to the total non-performing exposure) is monitored at the overall bank level as a MaSan indicator. The NPE coverage ratio AC amounted to a solid 57.6 % as at the reporting date. The NPE coverage ratio AC was 61 % at the start of the new year after taking account of the results of the adjusting events and the loan loss provisions recognised for macroeconomic and political risks.

After the portfolio transaction in 2018 Hamburg Commercial Bank AG's NPE ratio decreased significantly at the Group level. Following this substantial improvement in the risk profile of the Bank's loan portfolios the trend of loan loss provisions and the NPE ratio has, in the future, an equivalent weight relative to to the Bank's other relevant management indicators. This also applies in particular in view of the fact that the shipping portfolio, which has hitherto been characterised by a high level of defaults, was significantly reduced.

The syndication of lending transactions also helps to actively shape the composition of the portfolio and align individual financing risks (so-called final takes) to the balance sheet ratios. The Bank subjects all potential new business from a certain volume limit to a market conformity review carried out in a committee and a syndication assessment performed by the credit syndication unit within the Credit Solutions department. The Credit Committee then makes a joint decision together with the credit syndication unit and the deal team sales employees as to whether syndication should be arranged as part of the new business or underwriting process. The Bank's existing portfolio is also reviewed for saleability on a quarterly basis as part of the MaSan procedure (and on an ad hoc basis where appropriate). The Bank amended the syndication process in view of the the rules regarding the business model laid down in IFRS 9 (initial adoption with effect from 01.01.2018). Underwriting financing is recorded based on a model with several accounts so that the final hold is assigned to the "Hold" business model and the syndication portion to the "Other" business model – with a corresponding retroactive effect on the holding category under IFRS 9. Any portfolio syndication activities are checked separately with regard to any non-compliance with the assigned business model.

RATING PROCEDURES, LGD AND CCF

In 2018 Hamburg Commercial Bank AG started a multi-year project to support the regulatory initiative regarding the internal estimate of the risk parameters (Future of the IRB).

IRBA governance was completely overhauled in the previous financial year and further methodological requirements developed (e.g. margin of conservatism, validation requirements). Hamburg Commercial Bank collaborates intensively with other banks in the further development and ongoing validation of various internal rating modules. This is done in the association of Landesbanks via RSU Rating Service Unit GmbH & Co. KG (RSU) and in cooperation with Sparkassen Rating und Risikosysteme GmbH (SR), a subsidiary of the German Savings Bank Association (DSGV).

Hamburg Commercial Bank uses rating modules for banks, corporates, international sub-sovereigns, country and transfer risk, insurance companies, leveraged finance, savings banks standard rating and leasing as well as for special financing for ships, real estate, projects and aircraft. Various qualitative in addition to quantitative characteristics are also used in each rating module. The result is a probability at default (PD) for each borrower and hence allocation to a concrete rating category. The Bank uses an identical rating master scale for all modules which not only allows comparison of differing portfolio segments but also mapping with external ratings.

So-called credit conversion factors (CCF) are calculated empirically and applied to determine the expected drawdown for contingent liabilities and commitments in case of a possible default. The loan amount outstanding weighted by CCF is described as the EaD.

Hamburg Commercial Bank uses a differentiated LGD methodology to forecast the loss given defaults (LGD). Collateral-specific recovery rates and borrower-specific recovery rates are estimated for these based on historic loss information. The respective default amount expected is determined from the EaD using the LGD.

As part of the annual validation process the predictive accuracy of the rating modules is reviewed in the reporting year with regard to the predicted probabilities of default using anonymous, aggregated data and the LGD and CCF procedures are validated in a comparable manner and continually enhanced.

RISK CONCENTRATIONS

Within the framework of regular business segment analyses potential counterparty default risk concentrations, for example with regard to groups of connected clients (GCC), regions or industrial sectors in a broader sense, are identified and their trend is monitored. At the 2018 year end, Hamburg Commercial Bank's material concentrations of credit risk were in the real estate portfolio, which accounted for 24 % of the overall portfolio (previous year: 20 %) and in the shipping portfolio, which accounted for 9 % of the overall portfolio (previous year: 14 %). Other concentration risks relate to the US dollar business, which accounted for 10 % of the overall portfolio (previous year: 15 %). Following the winding down of the portfolio, especially in the area of ship financing denominated in US dollars, the sensitivity of the capital and liquidity ratios to trends in the shipping market and the EUR/USD exchange rate has also decreased and is therefore no longer relevant.

There is an internal process, which ensures compliance with the regulatory requirements, for monitoring large exposure limits in accordance with Article 395 CRR. As a supplementary measure, material counterparty concentrations in the portfolio are identified by means of a risk-based parameter (risk of loss as the sum of the expected and unexpected loss) and reported quarterly to the Management Board and Risk Committee. Net rating-based upper limits are applied to new business to prevent future counterparty concentrations.

Country risk limits are an additional management dimension within the management of risk concentrations. Country limits are set for country risk concentrations at the Hamburg Commercial Bank Group level. Utilisation of the limits is monitored continuously and centrally by country risk management.

EQUITY HOLDING RISK

Hamburg Commercial Bank has significantly reduced its equity holding portfolio and thereby equity holding risk over recent years, thus successfully bringing it in line with the Bank's strategic realignment. New equity holdings are only acquired if they meet Hamburg Commercial Bank's strategic objectives. The opportunities and risks associated with a potential equity holding are analysed extensively prior to the conclusion of the transaction.

A regular company valuation represents an important instrument for monitoring and managing equity holding risk. Impairment tests are performed at least once a year on all equity holdings of Hamburg Commercial Bank. Important equity holdings are subject to a more detailed analysis in this context.

Furthermore, the articles of association and by-laws are formulated so as to ensure that the most intensive management possible can be exercised for the benefit of Hamburg Commercial Bank.

Hamburg Commercial Bank has issued a hard letter of comfort for three companies in the equity holdings portfolio and is therefore liable for the liabilities of these companies. These letters have so far not given rise to any liability on the part of Hamburg Commercial Bank. Hamburg Commercial Bank has concluded a profit-and-loss transfer agreement with a further two equity holdings.

MANAGEMENT OF DEFAULT RISK IN PRICING AND ACTUAL COSTING

Hamburg Commercial Bank applies a uniform method across the Bank for the pricing of lending transactions through calculating the present value of the expected and unexpected losses arising on default risk positions. In addition to liquidity and standard processing costs, the rating, LGD and CCF risk parameters determined internally on an individual transaction basis are incorporated in the pricing by means of the standard risk costs. In the same way, an actual costing (profit centre accounting) is made for all transactions on a monthly basis, taking the above-mentioned cost elements into account. Standard risk costs and the resulting contribution margins are determined based on the current risk parameters of the individual transactions. Furthermore, utilisation of the capital commitment set as part of the Bank's annual plan is determined regularly at the division level for the purposes of managing default risk. When bottleneck resources are overdrawn, new transactions and prolongations are subject to stricter approval requirements.

DEFAULT RISK EXPOSURE

The figures in the following tables showing default risk exposure are based on the exposure at default (EaD). The EaD corresponds to the volume of loan receivables, securities, equity holdings, derivative financial instruments (positive market values after netting) and off-balance-sheet transactions (taking credit conversion factors into account). Risk-mitigating effects (such as recognition of collateral) are not included in EaD. Total EaD amounted to € 56,641 million as at 31 December 2018.

The EaD broken down by internal rating categories is presented in the following table. EaD with an investment grade rating (rating category 1 to 5) accounted for 73 % of the total exposure at the Group level (previous year: 68 %).

Default risk structure by rating category[1)2)]

(€ m)	31.12.2018			
	Core Bank	Non-Core Bank	Other and Consolidation	Total
1 (AAAA) bis 1 (AA+):	13,389	–	3,648	17,037
1 (AA) to 1 (A–)	7,992	–	2,104	10,096
2 to 5	14,005	–	175	14,180
6 to 9	10,642	–	1	10,643
10 to 12	1,848	–	–	1,848
13 to 15	1,539	–	5	1,544
16 to 18 (default categories)	699	183	–	882
Other[3)]	92	–	319	411
Total	**50,207**	**183**	**6,251**	**56,641**

1) The information disclosed as at 31 December 2018 has been prepared in accordance with IFRS 9 and does not include further adjustments on the basis of knowledge obtained after the reporting date, which were recognised as defaults. Information and explanations regarding the comparative period have not been adjusted and are the amounts determined under IAS 39 as at the described reporting date.

2) Mean default probabilities (in %): 1 (AAAA) to 1 (AA+) 0.00–0.02; 1 (AA) to 1 (A–): 0.03–0.09; 2 to 5: 0.12-0.39; 6 to 9: 0.59–1.98; 10 to 12: 2.96-6.67; 13 to 15: 10.00-20.00; 16 to 18: 100.00

3) Transactions, for which there is no internal or external rating available, are reflected in the "Other" line item, such as receivables from third parties of our consolidated equity holdings.

Default risk structure by rating category[1)2)]

(€ m)	31.12.2017				
	Core Bank	Non-Core Bank	Other and Consolidation	Total	Of which covered by the guarantee (in %)
1 (AAAA) to 1 (AA+)	16,255	79	5,615	21,949	6
1 (AA) to 1 (A–)	7,160	239	2,284	9,683	11
2 to 5	16,158	680	444	17,282	11
6 to 9	10,732	1,009	1	11,742	21
10 to 12	1,425	228	–	1,653	54
13 to 15	1,151	845	3	1,999	59
16 to 18 (default categories)	840	6,649	–	7,489	78
Other[2)]	4	88	331	423	–
Total	**53,725**	**9,818**	**8,678**	**72,220**	**20**

1) Mean default probabilities (in %): 1 (AAAA) to 1 (AA+) 0.00–0.02; 1 (AA) to 1 (A–): 0.03–0.09; 2 to 5: 0.12-0.39; 6 to 9: 0.59–1.98; 10 to 12: 2.96-6.67; 13 to 15: 10.00-20.00; 16 to 18: 100.00

2) Transactions, for which there is no internal or external rating available, are reflected in the "Other" line item, such as receivables from third parties of our consolidated equity holdings.

EaD broken down by sectors important for Hamburg Commercial Bank is presented in the following table:

Default risk structure by sector[1)]

(€ m)	31.12.2018			
	Core Bank	Non-Core Bank	Other and Consolidation	Total
Industry	7,930	7	–	7,937
Shipping	4,999	137	–	5,136
Trade and transportation	2,836	–	–	2,836
Credit institutions	3,603	–	3,276	6,879
Other financial institutions	2,135	–	16	2,151
Land and buildings	10,875	39	–	10,914
Other services	4,528	–	401	4,929
Public sector	12,912	–	2,546	15,458
Private households	389	–	13	402
Other	–	–	–	–
Total	**50,207**	**183**	**6,251**	**56,641**

1) The information disclosed as at 31 December 2018 has been prepared in accordance with IFRS 9 and does not include further adjustments on the basis of knowledge obtained after the reporting date, which were recognised as defaults. Information and explanations regarding the comparative period have not been adjusted and are the amounts determined under IAS 39 as at the stated reporting date.

Default risk structure by sector

(€ m)	31.12.2017			
	Core Bank	Non-Core Bank	Other and consolidation	Total
Industry	7,692	977	–	8,669
Shipping	5,056	4,170	–	9,226
Trade and transportation	3,123	322	–	3,445
Credit institutions	6,340	209	4,340	10,889
Other financial institutions	1,904	825	24	2,753
Land and buildings	9,595	2,262	–	11,857
Other services	4,686	392	542	5,620
Public sector	15,042	373	3,757	19,172
Private households	289	286	14	589
Other	–	–	–	–
Total	**53,725**	**9,818**	**8,678**	**72,220**

The following table shows the EaD broken down by residual maturities:

Default risk structure by residual maturity[1)]

(€ m)	31.12.2018			
	Core Bank	Non-Core Bank	Other and Consolidation	Total
Up to 3 months	9,717	–	728	10,445
> 3 months to 6 months	1,864	–	156	2,020
> 6 months to 1 year	2,841	2	196	3,039
> 1 year to 5 years	20,944	4	3,379	24,327
> 5 years to 10 years	9,660	176	1,431	11,267
> 10 years	5,182	–	362	5,544
Other	–	–	–	–
Total	**50,207**	**183**	**6,251**	**56,641**

[1)] The information disclosed as at 31 December 2018 has been prepared in accordance with IFRS 9 and does not include further adjustments on the basis of knowledge obtained after the reporting date, which were recognised as defaults. Information and explanations regarding the comparative period have not been adjusted and are the amounts determined under IAS 39 as at the stated reporting date.

Default risk structure by residual maturity

(€ m)	31.12.2017			
	Core Bank	Non-Core Bank	Other and Consolidation	Total
Up to 3 months	12,813	2,054	525	15,393
> 3 months to 6 months	1,528	403	354	2,285
> 6 months to 1 year	3,322	955	516	4,793
> 1 year to 5 years	20,440	3,096	4,776	28,312
> 5 years to 10 years	10,399	1,773	2,132	14,304
> 10 years	5,223	1,535	374	7,132
Other	–	–	–	–
Total	**53,725**	**9,818**	**8,678**	**72,220**

The following table provides an overview of the foreign exposure by region, which reached € 16.689 million as at 31 December 2018 (previous year: € 23,286 million).

Foreign exposure by region[1)]

(€ m)	31.12.2018			
	Core Bank	Non-Core Bank	Other and Consolidation	Total
Eurozone	7,889	8	868	8,765
Western Europe	3,481	39	905	4,425
Eastern Europe	245	2	–	247
Africa	530	49	–	579
North America	526	–	–	526
Latin America	401	–	–	401
Middle East	28	5	–	33
Asia-Pacific region	1,057	79	–	1,136
International organisations	69	–	508	577
Total	**14,226**	**182**	**2,281**	**16,689**

[1)] The information disclosed as at 31 December 2018 has been prepared in accordance with IFRS 9. Information and explanations regarding the comparative period have not been adjusted and are the amounts determined under IAS 39 as at the described reporting date.

Foreign exposure by region

(€ m)	31.12.2017			
	Core Bank	Non-Core Bank	Other and Consolidation	Total
Eurozone	7,515	2,648	1,226	11,389
Western Europe	3,232	1,557	1,190	5,979
Eastern Europe	296	446	–	742
Africa	543	263	–	806
North America	413	385	–	798
Latin America	262	191	–	453
Middle East	38	334	–	372
Asia-Pacific region	1,210	804	–	2,014
International organisations	129	–	604	733
Total	**13,638**	**6,628**	**3,020**	**23,286**

The basis for the allocation of the transactions to the regions is the country of the customer relevant for transfer risk taking account of any collateral relevant for the transfer risk. The country relevant for transfer risk is the country from where Hamburg Commercial Bank receives the cash flows.

A number of European countries are subject to increased monitoring due to their unfavourable fiscal and economic data. These include in particular Greece, Italy, Portugal and Spain.

As a result of economic developments and the EU sanctions, the exposure to Russia and Turkey is also being monitored more closely.

The following table shows the EaD of the exposures to the European countries shown.

Exposure at Default in selected European countries[1)]

(€ m)	Public sector		Banks		Corporates/Other		Total	
	31.12.2018	31.12.2017	31.12.2018	31.12.2017	31.12.2018	31.12.2017	31.12.2018	31.12.2017
Greece	–	–	–	–	337	940	337	940
Italy	15	19	–	–	270	574	286	593
Croatia	–	–	–	–	87	94	88	94
Portugal	56	180	–	–	96	52	153	232
Russia	–	–	–	1	28	47	28	48
Spain	93	79	30	36	329	918	451	1,033
Turkey	–	–	27	59	31	173	58	232
Cyprus	–	–	–	–	385	434	385	434
Total	**164**	**278**	**57**	**96**	**1,563**	**3,232**	**1,786**	**3,605**

1) The information disclosed as at 31 December 2018 has been prepared in accordance with IFRS 9. Information and explanations regarding the comparative period have not been adjusted and are the amounts determined under IAS 39 as at the described reporting date.

The previously low direct country exposure to the countries shown above was further reduced in 2018. The commitments in the Corporates/Other sector for Greece and Turkey relate primarily to ship financing arrangements, which do not entail transfer risk due to the existing collateral. The exposure to Great Britain (€ 2,215 million) is also being monitored more closely due to a possible Brexit.

LOAN LOSS PROVISIONS

Hamburg Commercial Bank pays the most attention to default risk within the context of risk management. Impairments of a loan commitment are covered by the recognition of specific loan loss provisions for loans and advances and provisions for contingent liabilities in the amount of the potential loss in accordance with Group-wide standards. Furthermore, Hamburg Commercial Bank recognises loan loss provisions under Stages 1 and 2 to cover future risks, the amount of which is not yet known to the Bank.

All restructuring and workout commitments, as well as intensified loan management commitments with a rating greater or equal to 13, are subject every quarter to a comprehensive two-step review process. In a first step, a review is carried out on the basis of objective criteria (so-called trigger events) to determine whether the receivable could be impaired (impairment identification). If this is the case, the loans identified are reviewed in a second step to determine whether a loan loss provision is actually required and the amount thereof (impairment measurement). Loan loss provisions are only recognised for transactions categorised as AC under IFRS 9. As at 31 December 2018, there was no longer any hedging effect of the second loss guarantee (see Note 2).

The 2017 compensation item also includes compensatory claims against the guarantor HSH Finanzfonds AöR resulting from settled losses for transactions for which loan loss provisions had already been recognised. The amount of the loan loss provision is calculated by deducting the present value of all expected future incoming payments from the IFRS carrying amount of the receivable. The expected incoming payments comprise in particular all expected interest and redemption payments, as well as proceeds from the liquidation of collateral. The following table provides an overview broken down by segment.

Changes in loan loss provisions in the lending business

(€ m)	01.01.–31.12.2018								
	Stage 3 loan loss-provisions (former SLLP/ provisions)	Stages 1 and 2 loan loss provisions (former GLLP)	Loss provisions recognised for financial investments	Loan loss provisions (LLP) before currency translation income and compensation	Currency translation income on loan loss provisions	Compen-sation item	Total	Hedging effect of credit derivative second loss guarantee	LLP including hedging effect of credit derivative
Corporate Clients	–45	–9	–	–54	–	–	–54	–	–54
Shipping	–178	–26	–	–204	–1	–	–205	–	–205
Real Estate Clients	5	–60	–	–55	–	–	–55	–	–55
Treasury & Markets	–	14	2	16	–	–	16	–	16
Total Core Bank	**–218**	**–81**	**2**	**–297**	**–1**	**–**	**–298**	**–**	**–298**
Non-Core Bank	**5**	**–**	**–**	**5**	**2**	**–**	**7**	**–**	**7**
Other and Consolidation	**4**	**1**	**–**	**5**	**–**	**–30**	**–25**	**–51**	**–76**
Group	**–209**	**–80**	**2**	**–287**	**1**	**–30**	**–316**	**–51**	**–367**

[1] The information disclosed as at 31 December 2018 has been prepared in accordance with IFRS 9. Information and explanations regarding the comparative period have not been adjusted and are the amounts determined under IAS 39 as at the described reporting date.

Changes in loan loss provisions in the lending business

(€ m)	01.01. –31.12.2017								
	Specific loan loss provisions/ provisions	General loan loss provisions	Loss provisions recognised for financial investments	Loan loss provisions (LLP) before currency translation income and compensation	Currency translation income on loan loss provisions	Compensa-tion item	Total	Hedging ef-fect of credit derivative second loss guarantee	LLP including hedging effect of credit derivative
Corporate Clients	–47	4	–	–43	–	–10	–53	–	–53
Shipping	–115	159	–	44	5	14	63	–	63
Real Estate Clients	3	–	–	3	–	–1	2	–	2
Treasury & Markets	–	1	–	1	–	–	1	–	1
Total Core Bank	**–159**	**164**	**–**	**5**	**5**	**3**	**13**	**–**	**13**
Non-Core Bank	**–1,512**	**99**	**–**	**–1,413**	**39**	**–731**	**–2,105**	**810**	**–1,295**
Other and Consolidation	**6**	**–**	**–**	**6**	**–**	**–**	**6**	**–**	**6**
Group	**–1,665**	**263**	**–**	**–1,402**	**44**	**–728**	**–2,086**	**810**	**–1,276**

Loan loss provisions came to € –287 million as at the reporting date (same period of the previous year: € –1,402 million).

The developments are due to the recognition of specific loan loss provisions in the Shipping division, which for the most part relate to restructuring measures undertaken for a significant loan exposure. Furthermore, the increasing geopolitical uncertainties are reflected in the recognition of general loan loss provisions, which are also partially included in the Stage 3 loan loss provisions in accordance with the IFRS 9 classification. The Bank therefore recognises provisions due to the increasing probability that the downside scenarios will materialise, which is increased by the threat of a disorderly Brexit and the possible escalation of the trade war between the USA and China, and may have an adverse impact on economic developments in Europe and in the industry sectors relevant for the Bank (especially real estate and shipping). In addition, the Bank has recognised appropriate loan loss provisions due to the emission targets for ships that are applicable from 2020. In the previous year, significantly higher amounts allocated for legacy loan exposures, especially in the shipping portfolio of the Non-Core Bank, had a considerable negative impact on the Group net result.

After foreign exchange effects and compensation and taking account of the hedging effect under the credit derivative loan loss provisions amounted to € –367 million (same period in the previous year: € –1,276 million). The loss rate in the Group amounted to 1.0 % in the reporting year (previous year: 4.31 %).

The loss ratio is calculated as the ratio of the actual defaults incurred to the financial instruments not measured at fair value (only AC). The total amount of defaults in 2018 was € 470 million (previous year: € 3,114 million), financial instruments not measured at fair value amounted to € 47,111 million (previous year: € 72,254 million credit exposure). The individual elements of loan loss provisions are shown in the following table:

Total loan loss provisions[1)]

(€ m)	2018	2017
Loans and advances to customers AC	30,057	39,174
Loans and advances to banks AC	3,000	3,838
Volume of impaired loans (gross carrying amount Stage 3)	955	6,813
Total loan loss provisions (Stage 3, formerly SLLP) for loans and advances to customers	–496	–4,355
Total loan loss provisions (Stages 1 and 2, formerly GLLP) for loans and advances to customers	–335	–138
Total loan loss provisions (Stages 1 and 2, formerly GLLP) for loans and advances to banks	–	–1
Total loan loss provisions for balance sheet items	**–831**	**–4,494**
Provisions for Stage 3, formerly individual risks in the lending business	–48	–60
Provisions for Stages 1 and 2, formerly portfolio risks in the lending business	–12	–7
Total loan loss provisions for off-balance sheet items	**–60**	**–67**
Total loan loss provisions (before compensation item)	**–891**	**–4,561**
Compensation item	–	5,181
Total loan loss provisions (including compensation item)	**–891**	**620**

1) Comparability with the previous year is only possible to a limited extent due to the transition from accounting under IAS 39 to accounting under IFRS 9.

Total loan loss provisions determined under IFRS 9 amounted to € –891 million as at 31 December 2018 (previous year under IAS 39: € 620 million after compensation under the second loss guarantee). Total Stage 3 loan loss provisions (formerly SLLP) comprise total loan loss provisions of € –496 million for loans and advances to customers and banks (previous year under IAS 39: € –4,355 million), loan loss provisions for impaired creditworthiness (LECL, stage 3), provisions of € –48 million (previous year under IAS 39: SLLP of € –39 million for contingent liabilities and irrevocable loan commitments) and SLLP of € –21 million for other off-balance sheet transactions for the previous year and amounted in total to € –544 million (previous year under IAS 39: € –4,415 million).

Stage 1 and 2 loan loss provisions (formerly GLLP) amounted in total to € –347 million (previous year under IAS 39: € –146 million) and comprise 12 months LECL, LECL Stage 2 loan loss provisions of € –335 million (previous year under IAS 39: GLLP of € –139 million for loans and advances to customers and banks) and 12 months LECL, Stage 2, provisions of € –12 million (previous year under IAS 39: € –7 million PoWB for contingent liabilities and irrevocable loan commitments).

Details regarding the total loan loss provisions are presented in Notes 15, 27 and 41 in the notes to the Group financial statements.

PLANNING FOR LOAN LOSS PROVISIONS

Loan loss provisions are planned as part of the annual Bank plan under the plan assumptions specified therein and includes the annual changes in the amounts of the specific and Stages 1 and 2 loan loss provisions including new business.

In planning additions to as well as utilisations and reversals of loan loss provisions Hamburg Commercial Bank mainly relies on models that simulate the expected loss at the individual transaction level over the planning period based on parameters specific to the transaction. Scenario analyses based on cash flows and historical data regarding changes in loan loss provisions based on the expected loss are also taken into account.

Market risk

Market risk represents the potential loss that can arise as a result of adverse changes in market values on positions held in our trading and banking book. Market movements relevant to the Hamburg Commercial Bank are changes in interest rates and credit spreads (interest rate risk), exchange rates (foreign exchange risk) as well as share prices, indices and fund prices (equity risk) including their volatilities.

Organisation of market risk management

The Management Board determines the methods and processes for measuring, limiting and managing market risk and budgets a proportion for market risk from a limit that covers all risk types. Against the background of this upper loss limit, the risks of all business bearing market risk are limited by a dynamic system of loss and risk limits.

Market risk was actively managed in the Treasury & Markets division in the reporting year. The Bank Management division performs the central management function for interest rate and foreign exchange risks in the banking book. The Overall Management Board is responsible for selected strategic positions exposed to market risk.

An organisational separation between market risk controlling, financial controlling as well as settlement and control on the one hand and the trading divisions responsible for positions on the other is ensured at all levels in accordance with

MaRisk. All major methodological and operational risk measurement and monitoring tasks are consolidated in the Group Risk Management division.

Market risk management

MARKET RISK MEASUREMENT AND LIMITATION
Our system for measuring and managing market risk is based on the economic daily profit and loss and on a value-at-risk approach. The economic profit and loss is calculated from the change in present values compared to the end of the previous year. The market risk of a position represents the loss in value (in euros) which will not be exceeded until the position is hedged or realised within a predetermined period with a predetermined probability.

The value-at-risk (VaR) is determined by Hamburg Commercial Bank using the historical simulation method. It is calculated for the entire Group based on a confidence level of 99.0 % and a holding period of one day for a historical observation period of 250 equally weighted trading days. The VaR model used and continuously enhanced by Hamburg Commercial Bank contains all of the Bank's significant market risks in an adequate form.

The material market risks at Hamburg Commercial Bank are primarily interest rate risk (including credit spread risk) and foreign exchange risk. In addition to these risk types, the VaR of Hamburg Commercial Bank also covers equity risk for both the trading book and banking book. The basis risk is also taken into account in determining the VaR. Basis risk constitutes the risk of a potential loss or profit resulting from changes in the price/interest rate relationship of similar financial products within a portfolio. Limits are set by a VaR limit for the Bank's overall market risk and by a stop loss limit for any cumulative losses. There are clearly defined and fast processes for limit adjustments and overdrafts. As part of the VaR approach limits are also set for the overall VaR in the trading book, the interest rate VaR in the banking book and the credit spread VaR. The present value basis used in the measurement of market risk is expanded by an earnings-oriented perspective, under which the change in average interest income is simulated in different scenarios up to a five-year time horizon.

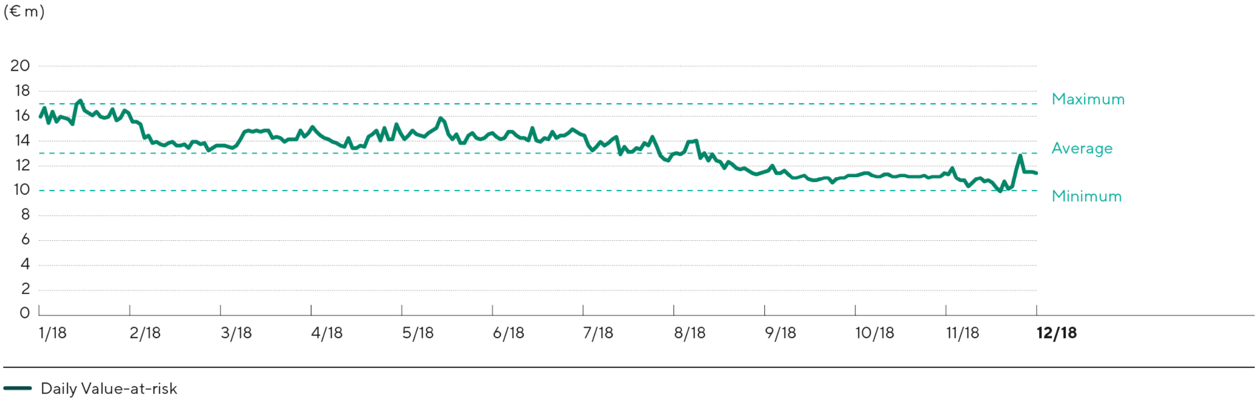
Where necessary, Hamburg Commercial Bank enters into hedging transactions to manage or reduce market risk in order to offset the impact of unfavourable market movements on its own positions. Derivative financial instruments in particular, such as interest rate and cross-currency interest rate swaps, for example, are used as hedging instruments. The effects of the hedging transactions entered into are included in the VaR disclosed. Further information on this and the type and categories of the hedging instruments and hedging relationships entered into by Hamburg Commercial Bank as well as the type of risks hedged is presented in the Notes. In particular we refer to Section I. F) of Note 7 "Accounting policies", Note 10 " Result from hedging", Note 28 "Hedge accounting under IFRS 9" and Note 59 "Report on business in derivatives".

Market risks arising from Hamburg Commercial Bank's lending business and liabilities are transferred to the trading divisions and taken into account in the corresponding risk positions. There they are managed as part of a proactive portfolio management process and hedged through external transactions.

Positions are assigned to the banking and trading books on the basis of clearly defined guidelines, especially with regard to holding periods permitted in the trading book. The assignment of individual positions to the relevant book are clearly identifiable in the market risk systems. Different processes and controls were established to meet the requirements for proper management of the trading book, which are reviewed for appropriateness on a regular basis.

DAILY VALUE-AT-RISK DURING THE YEAR UNDER REVIEW
The following chart shows the movement in the daily VaR for the total trading and banking book positions of Hamburg Commercial Bank over the course of 2018.

Daily Value-at-risk in the course of 2018



The daily market risk of the trading book positions was € 0.5 million and that of the banking book positions € 11.3 million as at 31 December 2018. The overall market risk, which cannot be derived from adding the VaR of the trading and banking book positions due to risk-mitigating correlation effects, amounted to € 11.4 million. Due to the completed integration of the residual risks in the former Non-Core Bank into the Core Bank during the course of 2018 separate disclosure for these two segments is no longer meaningful. Furthermore, in addition to the risk determined by the system, the Value at Risk of the Hamburg Commercial Bank includes a VaR add-on of € 1.4 million for residual risks for corporate bonds, Pfandbriefe and government bonds (only included at the Hamburg Commercial Bank Group level) as at 31 December 2018.

The following table shows the change in overall VaR by individual market risk type. The maximum and minimum represent the range over which the respective risk amount moved over the course of the year under review

Daily value-at-risk of the Group

(€ m)	Interest rate risk[1]		Credit spread risk[1]		Foreign exchange risk		Equity risk		Total[2]	
	2018	2017	2018	2017	2018	2017	2018	2017	2018	2017
Average	5.6	5.2	7.3	15.6	8.9	11.1	1.2	1.2	13.3	20.0
Maximum	7.1	9.7	9.3	26.7	14.9	20.8	1.9	1.6	17.2	33.7
Minimum	3.8	2.9	5.9	8.1	3.3	0.8	0.7	0.8	9.9	9.9
Period end amount	5.8	5.3	6.1	9.1	4.2	14.5	0.8	1.5	11.4	16.7

[1] Credit spread risk is a sub-type of interest rate risk. It is not disclosed as part of interest rate risk but as a separate item due to its significance for Hamburg Commercial Bank.
[2] Due to correlations the VaR does not result from adding up individual values.

The market risk of the Hamburg Commercial Bank is primarily characterised by interest rate and foreign exchange risk arising from the lending business, funding and the trading book, which predominantly contains positions resulting from trading in interest rate and currency derivatives with customers and bond trading. Market risk also includes credit spread risk on securities held in the liquidity buffer and cover pool portfolios that have good credit quality.

Market risk has continued to decrease in 2018. There are significant decreases in credit spread and currency risk across risk types. A key factor in the reduction in the credit spread risk was the winding down of the securities portfolios held in the liquidity buffer, in Treasury and the former Non-Core Bank. Currency risk decreased primarily as a result of the reduction in mapping differences between accounting and risk measurement in the context of the transformation of the privatised bank.

BACKTESTING

Hamburg Commercial Bank performs regular backtests to verify the appropriateness of its VaR forecasts. On the assumption of unchanged positions, the daily profit and loss achieved in theory due to the market developments observed are compared with the VaR values of the previous day, which were forecast using historical simulation. Based on the assumption of the confidence level of 99.0 % applied by Hamburg Commercial Bank, up to four outliers indicate that the forecasting quality for market risks is satisfactory. This threshold was maintained at all times at the Hamburg Commercial Bank Group level in 2018.

STRESS TESTS

In addition to the limit-based management of the daily VaR, stress tests are performed that analyse the effects of unusual market fluctuations on the net present value of the Bank's positions.

Hamburg Commercial Bank makes a distinction for market risk between standardised, historical and hypothetical stress scenarios. Whereas standardised scenarios are defined for specific risk types (e.g. shift in or rotation of the interest rate curve), historical and hypothetical stress tests apply to several market risk factors at the same time. In this regard historical scenarios actually map correlations between risk factors that occurred in the past, whereas hypothetical scenarios are based on fictitious changes in risk factors. With regard to the hypothetical scenarios a distinction is also made between economic scenarios that simulate a downturn in the macroeconomic environment and portfolio-specific scenarios that can represent a potential threat for the value of individual sub-portfolios of Hamburg Commercial Bank. The hypothetical scenarios are periodically reviewed and adjusted where necessary depending on changes in the market environment.

INSTRUMENTS FOR MANAGING MARKET RISK AS PART OF THE ACCOUNTING FOR HEDGING RELATIONSHIPS

The Treasury & Markets division also uses derivative financial instruments to manage market risk arising from loans and advances and liabilities as well as securities. Interest rate swaps and other interest rate or currency swaps are used to hedge the interest rate and foreign exchange risk arising from the underlying transactions. Market risks can be hedged at the micro, portfolio and macro level.

Changes in the value of derivatives are always recognised through profit or loss due to the FVPL classification. If underlying transactions classified as AC or FVOCIR are hedged by derivatives, this gives rise to a distortion in the income statement that is not consistent with the economic facts. One way of avoiding these distortions is to use fair value hedge accounting. In fair value hedge accounting, the changes in value of hedged items which are attributable to the hedged risk are recognised through profit or loss. In so doing, the Bank only takes account of hedges of the fair value against interest rate risk. Fixed-interest rate loans, issued instruments and securities positions are designated as underlying transactions (hedged items), while only external interest rate and interest rate currency swaps are designated as hedging instruments. Hamburg Commercial Bank recognises appropriate hedges of underlying transactions by external derivatives under portfolio fair value hedge accounting as well as micro hedge accounting in individual cases, insofar as the requirements of IFRS 9 are met.

Liquidity risk

Hamburg Commercial Bank's internal liquidity management represents a core component of the Internal Liquidity Adequacy Assessment Process (ILAAP) New ILAAP requirements were published as part of an ECB guide in November 2018. These have already been largely implemented as at 31 December 2018, final implementation will take place in 2019.

A distinction is made in the ILAAP between two approaches - the normative perspective and the economic perspective. The normative perspective is an assessment of the ability to fulfil all regulatory, supervisory and in part internal liquidity requirements and guidelines today and in the future and covers a multi-year assessment period. The objective is the forward-looking assessment of liquidity adequacy. In addition to a baseline scenario, adverse scenarios are also to be taken into account in forecasting the parameters.

Conversely, the economic perspective ensures that all material risks that may negatively affect solvency, are identified, quantified and covered by internal liquidity, so that the business strategy can be pursued continuously and the continuity of the institution is maintained at all times. The objective of the economic perspective is to manage economic risks and ensure liquidity adequacy through stress test programs. Only internal parameters (Pillar II ratios) are considered from today's perspective under the economic perspective, i.e. on the basis of the current balance sheet. Any structural events occurring at the Bank or in the environment are taken into account. A distinction is made between insolvency risk and liquidity transformation risk in the internal risk management process.

Insolvency risk refers to the risk that present or future payment obligations cannot be met in part or in full. The key driver of this liquidity risk is the cash flow structure in the liquidity development report, which is determined by the assets (maturity/currency structure) and liabilities (funding structure by maturity/currency/investor).

Liquidity maturity transformation risk refers to the risk that a loss will result from a mismatch in the contractual maturities of assets and liabilities, the so-called liquidity maturity transformation position, and from the change in the Bank's refinancing surcharge.

Organisation of liquidity risk management
Strategic liquidity management is the responsibility of the Bank Management division. The objective of liquidity management is to ensure the solvency of Hamburg Commercial Bank at all times, at all locations and in all currencies, to adhere to the regulatory liquidity ratios, to manage the marketability of the liquid assets of the liquidity buffer and to avoid concentration risks in the refinancing structure. The Treasury & Markets division is operationally responsible for funding and marketing.

The Group Risk Management division is responsible for the methods used to measure and limit liquidity risk within the Group and performs daily risk measurement and limit monitoring. Bank Management uses the risk measurement results to support it in managing liquidity for all maturity bands and enable it to counter possible risks at an early stage.

The OBM committee is the central committee responsible for managing the resource liquidity and is assisted by the Credit Committee in this task by means of an active portfolio management at the material individual transaction level.

Hamburg Commercial Bank has a liquidity contingency plan and regulated procedures and responsibilities in place in the event of a liquidity crisis. Institution-specific, risk-based and capital market-oriented early warning indicators are also taken into account as part of the contingency process in order to avert a liquidity emergency. The liquidity contingency plan is closely linked to the Recovery Plan as defined in SAG.

Liquidity risk management

MEASUREMENT AND LIMITATION OF LIQUIDITY RISK
The transactions in the Group impacting liquidity are presented as cash flows and the resultant inflows and outflows allocated to maturity bands (liquidity development report) for the purposes of measuring insolvency risk or funding requirements. The difference between inflows and outflows represents a liquidity surplus or deficit (gap) in the relevant maturity bands. The gaps are are shown on a cumulative basis from day one to twelve months in order to map future liquidity requirements. They are compared to the respective liquidity potential which is applied to close the cumulative gaps of the individual maturity bands and consequently represents the respective limit for insolvency risk. The net liquidity position, which shows the extent of the insolvency risk, is determined as the net amount from the gaps and the respective liquidity potential.

In addition to all on-balance sheet business, loan commitments already granted, guarantees, transactions with forward value dates and other off-balance sheet transactions are incorporated in the liquidity development report. Maturity scenarios are used for a number of positions to map economic maturities more effectively. In doing so any possible minimum levels of deposits as well as liquidation periods and realisation amounts of assets, for example, are modelled conservatively as a matter of principle. The modelling assumptions used are periodically reviewed, which is also required under MaRisk.

The liquidity potential available to close gaps is composed of a securities portfolio held as a precaution in the event of a crisis (liquidity buffer), other securities according to how liquid they are and industrial loans eligible for refinancing with central banks. Most of the portfolio of securities is invested in liquid markets and can be liquidated via the refinancing channels, namely central banks, Eurex repo market, bilateral repo market or the cash market.

The components of the liquidity potential – such as the liquidity buffer required under MaRisk for example – are monitored continuously and validated in accordance with internal and external minimum requirements.

The liquidity-value-at-risk (LVaR) as a reflection of liquidity maturity transformation risk is calculated monthly through historical simulation (confidence level of 99.9 %) of the liquidity spreads and their present value effects on transactions, which would be theoretically necessary to immediately close the current maturity transformation position. LVaR limits are set at Group level and are a part of the risk-bearing capacity concept.

LIQUIDITY MANAGEMENT
The short-term liquidity base and regulatory liquidity ratios are operationally managed by the Bank Management division based on general parameters specified by the Treasury & Markets division. In addition to the regulatory requirements the liquidity development report is relevant amongst other things for determining these general parameters. The definition of or change to individual parameters or the framework is decided by the OBM committee or the Management Board. This places Hamburg Commercial Bank in the position to react flexibly to market developments.

Hamburg Commercial Bank uses the so-called expected case liquidity development report and stress case forecast, which contain expected cash flows and are prepared for a period extending beyond the current financial year, as the basis for managing the medium-term liquidity base. This tool is used to forecast how the worst stress case and/or stress case liquidity development report develops over time.

Insolvency risk over more than one year is managed by means of the portfolio/liquidity development report. It shows the pure maturity mismatches in the base case.

The collateral pool of Hamburg Commercial Bank consisting of cash balances, securities and loan receivables that are eligible for funding is coordinated by Bank Management in order to be able to utilise the potential for secured funding in the best possible manner.

In the event that this causes a deterioration in the relevant MaSan indicators under the SRF, measures would have to be taken to strengthen the liquidity position after transition into the MaSan early warning phase in order to comply with the internally required parameters and thus the regulatory requirements (Pillar 2 requirement) at the Hamburg Commercial Bank Group level.

STRESS TESTS

The selection of our stress tests is the result of an analysis of historical events and hypothetical scenarios. The selection is reviewed at least on an annual basis and adapted to current developments where necessary.

Within the different stress modelling processes additional market-specific scenarios (e.g. rating downgrade of Hamburg Commercial Bank, capital market rumours) are assessed for insolvency risk on a monthly basis in addition to the daily calculation of the stress case liquidity development report. A stressed US dollar (gradual appreciation) is taken into account in the scenarios market liquidity crisis and severe economic downturn.

Within the framework of a stress test for the liquidity maturity transformation risk an analysis is carried out to determine how the LVaR changes on increasing liquidity spreads and stressed liquidity gaps.

Furthermore, events that could have a critical impact on Hamburg Commercial Bank's solvency were analysed in the reporting year within the framework of the periodic implementation of inverse stress tests.

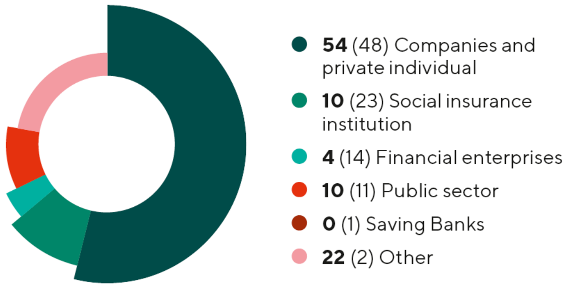
RISK CONCENTRATIONS

Hamburg Commercial Bank has established a monitoring system for managing concentrations of both asset and liability instruments. Special emphasis is placed on deposits that are analysed and reported on with regard to the depositor structure (investor, sectors), maturities (original and residual maturities). Depositor concentration was reduced significantly in 2018 compared to the previous year. The ten largest depositors account for around 17 % of total deposits. (31.12.2017: 29 %). The deposit structure by sector has also developed positively in 2018. The proportion of retail deposits increased to 19 % (31.12.2017: <2 %). The proportion of institutional investors was 3.6 % as at 31 December 2018 (31.12.2017: 85 % based on a broader definition). Based on the maturity structure the proportion of deposits payable on demand of 44.5 % is still high (31.12.2017: 44.3 %).

The following chart shows the structure of our deposits by sector:

Depositor structure as at 31 December 2018

(%, previous year figures in brackets)



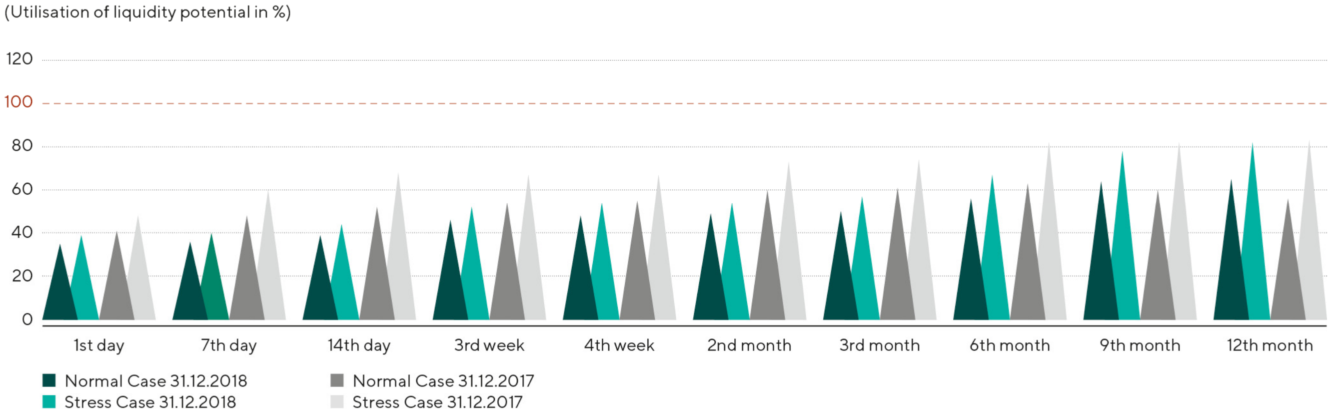
In addition to the analysis of the depositor structure with regard to existing depositor concentrations, risk concentrations are examined with regard to the US dollar asset/liability position. For the purposes of analysing the dependency on the US dollar, a US dollar liquidity development report is additionally prepared and sensitivity analyses and a US dollar stress test are performed. The risk has decreased significantly compared to the previous year due the reduction in US dollar assets.

Quantification of liquidity risk

The following chart shows the relative utilisation levels of the liquidity potential for individual cumulative liquidity gaps in the normal case and stress case as at 31 December 2018 as well as at the end of 2017. Utilisation represents the ratio of the cumulative gap to the total liquidity potential, which also includes the liquidity buffer required under supervisory law.

During 2018 the liquidity buffer to be maintained under MaRisk was reduced from € 9.0 billion to € 6.0 billion due to the decrease in liquidity risks.

Limit on cumulative liquidity gaps



Hamburg Commercial Bank's risk appetite with regard to liquidity risk is reflected, amongst other things, in the definition of a minimum survival period, which describes how long utilisation of a liquidity potential lower than 100 % is to be maintained under the normal and stress cases for insolvency risk.

The liquidity potential had a peak utilisation of 65 % in the twelfth month as at the reporting date in the normal case assessment, which is based on the assumption of business development in an ordinary market environment. All limits within the minimum survival period of twelve months defined by the Bank were thereby adhered to. The stress case liquidity development report (combined scenario – economic downturn and rating downgrade) shows that the liquidity potential was also not exceeded within the minimum survival period of one month established taking account of MaRisk and the minimum survival period of three months derived from the 2017 SREP decision; in fact, the limits as at the end of 2018 are even adhered to for a period of twelve months. Compared to the 2017 year end, utilisation levels have decreased in the normal case and stress case in virtually all maturity bands. The improvements result in particular from the disposal of loan and securities portfolios as well as from liquidity inflows arising from guarantee payments made by the former public shareholders of the Bank. Critical limit utilisation levels were not reported in the normal case nor in the stress case liquidity development report during the period under review.

The results of the market-specific and Bank-specific stress scenarios determined in addition to the stress case liquidity development report show that, as at December 2018, Hamburg Commercial Bank's liquidity requirement was covered by the liquidity potential over twelve months in all scenarios despite the worst- case assumptions. A minimum survival period of three months is thereby maintained in all scenarios. The results show that Hamburg Commercial Bank is prepared accordingly for the crisis scenarios assessed.

In the year under review, the LVaR as an expression of the liquidity maturity transformation risk increased to € 50 million (previous year: € 46 million).

REGULATORY LIQUIDITY RATIOS

The regulatory indicator for liquidity risks is the liquidity coverage ratio (LCR), the purpose of which is to ensure that liquidity is safeguarded in an acute stress period of 30 days. When calculating the LCR the amount of highly liquid assets is compared to the net outflows over the next 30 days. Their basis of calculation is laid down in the CRR and the CRR Delegated Regulation (EU) 2015/61. The minimum threshold of 110 % to be maintained by Hamburg Commercial Bank was maintained at all times in the reporting period. The LCR amounted to 225 % as at 31 December 2018 (previous year: 169 %).

Under the Amending Regulation with regard to the Liquidity Regulation Hamburg Commercial Bank AG has been excluded from its scope of application since 1 January 2018, so that the relevant ratio (LiqV) was calculated for the last time as at 31 December 2017.

The net stable funding ratio (NSFR), which must be adhered to from 2021 at the earliest, is calculated as the ratio of available stable funding resources across all maturities to the stable funding required and must also be at least 100 % after full implementation. As at 31 December 2018 the NSFR of the Bank amounted to 121 % under the QIS (Basel framework) (previous year: 114 %).

Since 31 March 2018 Hamburg Commercial Bank AG has also calculated the adjusted additional liquidity monitoring metrics (AMM) including the preparation of the stipulated liquidity development report on the C66 reporting form in accordance with Implementing Regulation 2016/313,

By means of the AMM the LCP (liquidity capacity period) is determined for the supervisory authorities. In so doing, inflows and outflows from a contractual point of view excluding any prolongation or new business assumptions are compared to the unencumbered liquid funds of the counterbalancing capacity (C 66) less any haircuts The LCP is no longer maintained from the date on which the cumulative cash flows give rise to a need for liquid funds, which exceeds the liquidity position. At this date the Bank's liquidity reserves are no longer sufficient from a purely contractual perspective to meet further payment obligations. The supervisory authorities has stipulated a minimum LCP period of four weeks for the Bank in 2019, which may not be undershot for a period of five banking days. This figure is determined by the Bank on a daily basis and was at least four months as at 31 December 2018.

REFINANCING SITUATION

Hamburg Commercial Bank successfully implemented its funding strategy in the 2018 financial year. In addition to the successful implementation of fundraising, there were inflows from the settlement of losses under the second loss guarantee in the 2018 financial year. Besides the issuing activities, deposits from corporates, institutional investors and retail customers contributed to the refinancing of the business. The regulatory requirements for the liquidity ratios were met at all times during the reporting period. The future refinancing and diversification of the funding structure continue to constitute major challenges. There is still no unrestricted access to the capital markets. In addition, institutional deposits have a comparatively low average duration, and there is a significant, albeit substantially reduced, level of counterparty concentration. Should access to the existing sources of refinancing deteriorate, this would severely limit the funding options and would adversely impact the Bank's rating.

Execution of funding measures in the market can also be made more difficult by potential tensions in the financial markets. A more than expected restrictive monetary policy adopted by the major central banks could also significantly limit the refinancing options and increase funding costs.

Should inclusion in the senior membership of the guarantee scheme of the Federal Association of German Banks not succeed as planned, this could lead to a significant outflow of deposits, triggering a significant increase in funding costs. Also as a result of the different manner in which the deposit guarantee funds work, i.e. institutional protection under the protection system of the German Savings Banks Finance Group versus protection of deposits, there is a risk of liquidity outflows associated with the change in the deposit guarantee fund. Furthermore, non-inclusion in the private guarantee scheme could put pressure on the meanwhile stable rating position.

Hamburg Commercial Bank's liquidity and funding plan is based on assumptions about client behaviour based on the deposit base and durations, especially with regard to the trend of short-term deposits. Even in critical, exceptional situations there is the risk that the relevant behavioural assumptions used for the simulation scenarios prove to be incorrect resulting in considerable unplanned liquidity outflows.

Part of the assets denominated in foreign currency are refinanced via derivatives (for example, via EUR/USD basis swaps). An appreciation in the US dollar results in an increase in the cash collateral to be provided and therefore exerts pressure on the liquidity situation under otherwise similar conditions.

The regulatory liquidity ratios such as the LCR, NSFR and minimum survival period in the combined stress scenario would deteriorate regardless of any intentional control measures taken such as, for example, a reduction in short-term deposits. Additional liquidity requirements could arise under the ECB's SREP process as a result of discretionary decisions.

It is also possible that additional requirements in various prudential regulatory areas such as liquidity may arise from the regular SREP process carried out within the Banking Union within the scope of discretionary decisions of the banking supervisory authorities.

Operational risk

Hamburg Commercial Bank defines operational risk (OpRisk) as the risk of direct or indirect losses caused by the inappropriateness or failure of the internal infrastructure, internal procedures or staff or as a result of external factors (risk categories). This definition includes the risk of loss resulting from legal risk and compliance risk.

For purposes of risk-bearing capacity management, operational risks are determined by applying a modified standardised approach, which also includes results from the scenario analyses. The corresponding economic capital required amounted to € 0.2 billion as at 31 December 2018 (previous year: € 0.2 billion).

Organisation of operational risk management
The management of operational risk at Hamburg Commercial Bank is organised in a decentralised manner. The risks are identified and managed directly in the individual organisational units of the Bank. Accordingly, the division heads are responsible for the management of operational risk and the quality of such management in their areas of responsibility. The operational implementation is supported by OpRisk officers in the individual divisions. The Group Risk Management Division is responsible for OpRisk Controlling.

As a Bank-wide steering committee for operational and other risks in the Group, the OpRisk Committee convenes every quarter and provides support to the Overall Management Board in the implementation of the OpRisk strategy under the chairmanship of the head of Group Risk Management. The objective of the interdisciplinary OpRisk Steering Committee is to promote dialogue between the persons involved at all hierarchy levels and to determine appropriate measures for reducing operational risk.

Operational risk management
The identification, analysis, evaluation and monitoring of operational risk and the promotion of a corresponding risk culture in the Group represents an important success factor for Hamburg Commercial Bank. Different procedures and instruments are used in this process as shown below.

Loss events arising from operational risk are consolidated into a central loss event database for Hamburg Commercial Bank and relevant subsidiaries. The loss events are recorded by the divisions concerned and forwarded to OpRisk Controlling.

In the reporting year 44 % (previous year: 53 %) of the operational loss events reported were incurred in the employee causes category. This risk category includes, for example, processing errors or unauthorised actions. The proportion of operational loss events reported under the Internal Processes risk category amounted to 16 % (previous year: 15 %). These include, for example, deficient or missing processes. The proportion of operational loss events reported under the External Influences category (e.g. criminal acts, regulatory and statutory requirements) amounted to 41 % (previous year: 28 %). The proportion of loss events reported under the Internal infrastructure category (e.g. system failures, functionality or security) amounted to 0 % (previous year: 4 %).

In a further procedure Hamburg Commercial Bank conducts an annual, group-wide risk inventory of operational risk based on defined scenarios. Information about the risk situation of the divisions gained from this inventory supplements the reporting and serves the purpose of preventive management and monitoring of operational risk.

Based on an analysis of the causes of significant loss events and the results of the risk inventory, suitable measures are established in order to avoid future losses as far as possible. The measures identified are to be appropriate under cost-benefit aspects. In doing this, the instruments of risk mitigation consist above all of a large number of organisational safeguarding and control measures which are also applied in the context of the internal control system. OpRisk Controlling monitors the actual implementation of the measures determined using the measures controlling procedures.

Risk indicators are collected on a quarterly basis and incorporated in the OpRisk reporting. The indicators are selected based on the estimated risk situation and are periodically reviewed to ensure that they are up-to-date. The aim is to identify risks at an early stage and prevent their causes by the use of ongoing and comparative analysis of loss events and risk indicators.

In addition to the methods mentioned above, specific procedures and responsibilities have been instituted within Hamburg Commercial Bank for the operational risk elements listed below.

Management of personnel risks
Personnel risk refers to the risk of losses that may occur as a result of the unplanned departure of key personnel of Hamburg Commercial Bank, shortage of skilled staff or poor motivation of employees. This risk could materialise particularly in light of the current reduction in staff. The Human Resources division is therefore focusing increasingly on measures to reduce personnel risk and actively supports the planned reduction in staff.

A large number of personnel management tools for employee retention are used to prevent the unscheduled departure of key personnel. In addition, succession planning is performed and regularly reviewed for relevant positions.

IT risk management
The IT division is responsible for IT risk management. In the IT strategy it has defined as the primary objective of IT risk management to identify IT risks at an early stage and assess them based on protection needs in order to avert or reduce particularly severe losses on the basis of clear responsibilities.

IT-specific risk tools are used by means of which risks concerning projects in the line functions and at outsourcing partners are actively managed and reduced by a monitored implementation of measures.

No significant losses were incurred in the past year in the area of responsibility of the IT division and the risk potential was again significantly reduced.

Business continuity management
Hamburg Commercial Bank is exposed to risks arising from unforeseen events, which may result in business interruption. Group Risk Management has established with the involvement of the relevant divisions processes to limit the risks arising from the fact that the information technology fails or service providers or employees are unavailable. The objective of the business continuity plans established and to be periodically reviewed is to ensure the functional capability of critical business processes and activities, also in the event of an emergency.

Internal control system
Operational risk is closely linked to Hamburg Commercial Bank's internal control system (ICS). A major objective of the ICS is to optimise the internal bank processes in order to avoid losses that may arise as a result of, for example, processing errors. Detailed information on the ICS is set out in the Risk management system section.

Management of legal risk
Legal risk also falls under operational risk. Legal risks include economic risks arising as a result of non-compliance or incomplete compliance with regulations or with the framework defined by case law, in particular commercial law, tax law and company law. In case any of these risks materialises, this may lead to a higher financial burden than planned.

The Legal and Taxes division is responsible for managing these risks. In order to reduce, limit or prevent risk all divisions are given comprehensive legal advice by regularly trained staff and where appropriate by external consultants.

Hamburg Commercial Bank recognised provisions of € 250 million for litigation risks and costs as at the reporting date (previous year: € 98 million). In addition, there are also contingent liabilities arising from legal disputes. A major portion of the provisions for litigation risks relates to the legal proceedings mentioned below.

Since 2005 Hamburg Commercial Bank AG has been involved in legal proceedings with a Turkish shipping group and up to now had to pay a total amount of USD 54 million in the year 2013 due to final decisions made by Turkish courts. The plaintiffs asserted at a later date further claims in the Turkish courts under which damages are asserted based on loss of profit and third party liabilities in connection with measures taken to realise loan collateral provided to the Bank for a loan.

Furthermore, Hamburg Commercial Bank AG is being sued for payment by a former borrower. The claims were increased and filed by the plaintiff in the fourth quarter 2018. The plaintiff is asserting various claims, particularly claims for payment of compensation and for unjustified enrichment in connection with measures taken by the Bank in connection with a non-performing loan. Various lawsuits have already been conducted on key sub-aspects of the underlying facts of the claim.

Furthermore, individual and groups of investors in hybrid financial instruments have taken legal action against the Bank and, in addition to establishing that their cancellation is invalid, request that they be written up to their nominal value and are claiming compensation for missed interest payments.

As a component of legal risk, tax risks mainly result from the fact that the binding interpretation of rules that can be interpreted in specific cases may only be known after several years due to the long period between tax audits. Tax audits are currently being conducted for the years 2008–2011 and 2012–2015. Appropriate provisions have been recognised for the effects of the tax audits.

Hamburg Commercial Bank recognised provisions and liabilities (including interest) totalling € 14 million (previous year: € 44 million) for tax risks. Tax risks arising from tax audits account for a significant proportion of these provisions.

Management of compliance risk
Compliance risk arises as a result of non-compliance with legal regulations and requirements that may lead to sanctions being imposed by the legislator or supervisory authorities, financial losses or to a negative impact on the Bank's reputation.

The Compliance division is responsible for compliance risk management. Compliance with the different legal requirements is also ensured by the respective divisions concerned. Compliance monitors adherence to codes of conduct with respect to the topics of capital markets compliance, prevention of money laundering, terrorism financing and other criminal offences in accordance with Section 25h KWG as well as compliance with financial sanctions and embargoes. In addition, the division performs the compliance function as defined in AT 4.4.2 MaRisk and in this context strives to ensure that the essential legal regulations and standards are implemented at Hamburg Commercial Bank and complied with.

The Code of Conduct summarises the requirements of different legal sources and internal guidelines. It applies to all employees as well as the Management Board of Hamburg Commercial Bank AG and is a mandatory part of the overall Bank's objectives. The specific code of conduct requirements of the Compliance division are set out in detail in internal instructions.

The Bank's staff is regularly trained in compliance-relevant topics. The objective of the training is to firmly anchor compliance as part of the corporate culture, to disseminate relevant standards and changes thereto, and to enable new staff to quickly become familiar with corporate practices and to ensure compliance with such legal requirements in this way.

The Bank receives notification of suspicious cases of misconduct via internal reporting channels and the so-called "whistle-blowing office", and forwards these to the responsible bodies. The whistle-blowing office is staffed by independent ombudsmen from BDO Deutsche Warentreuhand Aktiengesellschaft Wirtschaftsprüfungsgesellschaft and enables anonymous reporting of suspicious cases both by employees of the Bank and external third parties.

Management of model risks
Models are vitally important for the Bank's management processes. The use of models involves of course a degree of uncertainty, which may cause financial losses as a result of inappropriate business decisions and give rise to regulatory risks as a result of the incorrect disclosure of capital, balance sheet and liquidity ratios and reputation risk.

The Bank's model risk management process includes careful development of models, independent validation of models and overarching model governance, which establishes and monitors the framework for dealing with models and model risk.

Other material risks

In addition to operational risk, business strategy risk and reputation risk are included in the other material risks of Hamburg Commercial Bank. In the reporting year Hamburg Commercial Bank adopted a non-financial risk framework in order to better address the diversity of the different risk types, which are commonly referred to as non-financial risks. This framework describes the relevant responsibilities in accordance with the 3 lines of defence method, whereby special attention is paid to so-called cross-cutting themes. In view of the increasing importance of these themes a "non-financial risk" unit reporting directly to the CRO will be created in 2019.

Business strategy risk
Business strategy risk refers to the risk of financial damage being incurred due to long-term strategic decisions based on incorrect assumptions. Should Hamburg Commercial Bank not be successful in identifying changes in markets relevant for it on a timely basis, this could have a negative impact on its competitiveness. Changes to laws and regulations or new regulatory requirements for instance could also jeopardise the implementation of Hamburg Commercial Bank's business model. This risk is managed via the annual review and updating of the business strategy and the closely related overall bank planning process established in the Bank. The Overall Management Board is responsible for the strategy of Hamburg Commercial Bank, whereby the Strategy & Management Board Office is responsible for the process for preparing the business strategy and the Bank Management division for strategy controlling. An action-oriented management dialogue, including on the strategic business objectives, is conducted during the year in the business review meeting.

Reputation risk
Reputation risk is the risk of a direct or indirect loss caused by damage to the reputation of the company. Damage to reputation means a public loss of confidence in Hamburg Commercial Bank or a loss of esteem of the Bank from the viewpoint of individual stakeholder groups (e.g. capital markets, clients, shareholders, investors, the general public, employees).

Hamburg Commercial Bank manages reputation risk particularly by means of preventive measures via the review of specific transactions, on the one hand, and via process-related rules, on the other, in order to prevent the occurrence of reputational damage if possible. The reputation risk strategy that is adopted every year defines the bank-wide principles for managing reputation risk as a supplement to the existing regulations and instructions, such as the Code of Conduct.

Summary of risk assessment and outlook
The 2018 financial year was characterised by the continuing winding down of high-risk, non-strategic lending and capital markets transactions held in the Non-Core Bank's portfolios as well as by the progress made in implementing the business model as the key strategic steps towards the successfully executed change in ownership.

Hamburg Commercial Bank's risk-bearing capacity was maintained at all times during the reporting year both under the new and old regulatory requirements.

Hamburg Commercial Bank is facing major challenges regarding its future development, which are described in detail in the Forecast, Opportunities and Risk Report.

The risk and bank management systems described in this report are aligned to take account of risk on a systematic basis. This also applies to our expectations regarding future market and business developments. We believe that we have appropriately presented the overall risk profile of the Hamburg Commercial Bank Group as well as the opportunities and risks inherent in the future development of our business activities in the Forecast, opportunities and risks report section and in this risk report in an appropriate and comprehensive manner.

Comment on the annual financial statements of Hamburg Commercial Bank AG in accordance with the German Commercial Code (HGB)

Report on earnings, net assets and financial position

Earnings situation

The earnings situation of Hamburg Commercial Bank AG was influenced to a particular degree by transformation effects in the year under review. Within this context, restructuring provi sions had a particular impact on net income. The composition and development of the statement of income can be seen in the following overview.

Statement of Income

(€ m)	2018	2017	Change in %
Net interest income	498	771	-35
Net commission income	-132	-88	-50
of which: Fees for the second loss guarantee	-165	-154	7
Net income from the trading portfolio	33	126	-74
Administrative expenses	-485	-521	-7
of which: Personnel expenses	-181	-202	-10
of which: Operating expenses	-305	-319	-4
Other operating income	-101	-90	-12
Operating result before loan loss provisions/valuation	**-187**	**198**	**>-100**
Loan loss provisions/valuation	-287	-1,166	-75
Operating result after loan loss provisions/valuation	**-474**	**-968**	**51**
Extraordinary result	-340	-69	>-100
Income tax expense	194	-2	>-100
Income from the assumption of losses	327	285	15
Result for the year	**-293**	**-754**	**-61**

Earnings hit hard by restructuring costs for transformation and loan loss provisions, in particular
The following developments in the individual income items were decisive to the Bank’s earnings situation:

Net interest income amounted to € 498 million compared to € 771 million in the previous year. Overall, operating performance is satisfactory. Net operating interest income was moderately above expectations. New business activities are showing mixed development. In a highly competitive environment, Hamburg Commercial Bank selects new business based on strict risk and return requirements. The development of new business margins in the reporting period already points towards a noticeable success story thanks to the consistent focus on earnings, with new business profitability also in line with the current ambition level. The volume of new business, however, remains moderately below expectations. The reason for the decline in net interest income is the previous year's result from the sale of receivables from promissory note loans.

As a result, Hamburg Commercial Bank AG had realised unrealised gains in order to partially compensate for the considerable structural burdens resulting from loan loss provisions on non-performing legacy loans.

The **net commission income** of € -132 million (previous year: € -88 million) was hit, in particular, by the fees for the second loss guarantee in the amount of € -165 million (previous year: € -154 million). This includes non-recurring expenses of € 100 million for the early cancellation of the guarantee. The net commission income of € 33 million adjusted for expenses for government guarantees decreased sharply compared to the previous year (€ 66 million). The decline is mainly attributable to lower income from the lending business and higher expenses from the guarantee business.

Net income from the trading portfolio amounted to € 33 million (previous year: € 126 million). The higher net income in the previous year is attributable to above-average operating income from interest rate transactions. € 4 million was added during the reporting period to the fund for general banking risks in accordance with Section 340e from net income from the trading portfolio (previous year: € 14 million).

Last year **administrative expenses**, after taking the expenses for the bank levy and the deposit guarantee scheme in the amount of € -87 million (previous year: € -41 million) into account, amounted to € 485 million (previous year: € -521 million). The marked increase in the item relating to expenses for the deposit guarantee fund is due to provisions set up for expected one-off payments to be made to the Association of German Banks (*Bundesverband deutscher Banken*) due to the planned change in the guarantee scheme as at 1 January 2022.

Administrative expenses, on the other hand, will fall considerably. Hamburg Commercial Bank AG is continuing to successfully implement its cost-cutting programme, which has been ongoing since 2014 and counteracts the increasing pressure on earnings and margins in the highly competitive banking market and the increasing expenses for regulatory requirements, stringently and in line with its plans. During the reporting period, Hamburg Commercial Bank AG once again made the progress it planned to make in implementing measures for operating expenses. The ongoing cost reduction program will be consolidated with the measures forming part of the transformation project, which aim to reduce costs and increase efficiency, and will be implemented resolutely until an appropriate CIR of 40 % at the most has been achieved.

Personnel expenses, which fell from € -202 million to € -168 million, were mainly affected by a further reduction in the number of employees according to plan as part of the headcount reduction. At the end of the year, the number of employees had fallen by -180 to 1,510 (calculated in full-time equivalents, FTE).

Operating expenses amounted to € -305 million compared with € -319 million in the previous year. Savings were made in particular with regard to legal advice, fees and IT costs due to lower costs for external consultancy. The positive development of the cost-saving measures was partly offset by opposite effects affecting various individual items.

Other operating income amounted to € -101 million (previous year: € -90 million). In addition to income from cost allocations and reimbursement of expenses (€ 32 million) and legal costs paid in advance (€ -18 million), this mainly includes provisions.

Operating result before loan loss provisions/valuation

The operating result after loan loss provisions amounted to € -187 million compared to € 198 million in the previous year. The main reason for the significant change lies in effects resulting from the decline in net interest income.

Mounting geopolitical risks put pressure on loan loss provisions

On the one hand, the development in loan loss provisions as at the reporting date is due to specific loan loss provisions set up in the Shipping division, which are largely related to restructuring measures for a significant loan exposure. On the other hand, the increasing geopolitical and economic uncertainties are reflected in the general loan loss provisions that were set up. By setting up these provisions, Hamburg Commercial Bank is taking precautions in view of the increasing probability of downside scenarios due to the risk of a hard Brexit or the possible escalation of the trade conflict between the US and China, which could have a negative impact on developments in relevant sectors (in particular shipping).

Under "loan loss provisions", and taking into account the guarantee effect, Hamburg Commercial Bank AG reports a negative value of € -287 million (previous year: € -1,166 million). The burden from loan loss provisions after compensation fell significantly from € -1,256 million in the previous year to € -288 million as at the reporting date. In the previous year, significantly higher amounts allocated for legacy loan exposures, especially in the shipping portfolio of the Non-Core Bank, had a considerable negative impact on the net result. The loan loss provisions/valuation result in the securities business fell to € 18 million (previous year: € 44 million). The loan loss provisions/valuation result from equity holdings amounted to € -17 million (previous year: € 68 million).

Extraordinary result driven by restructuring and privatisation expenses

The extraordinary result increased to € -340 million compared to € -69 million in the previous year. Earnings were hit considerably by restructuring and privatisation expenses. Of this amount, € -235 million is attributable to restructuring expenses for personnel measures planned as part of the transformation project, € -44 million to material costs and € -67 million for privatisation (previous year: € -52 million).

High negative net result

Net income before taxes amounted to € -814 million (previous year: € -1,037 million). After taking account of income taxes of € 194 million (previous year: € -2 million) and income from the assumption of losses of € 327 million (previous year: € 285 million Hamburg Commercial Bank AG reports a negative net result of € -293 million (previous year: € -754 million). The net result is in line with expectations, although the earnings drivers were partly influenced by unplanned special factors, such as unplanned considerable loan loss provisions and high restructuring expenses. These burdens were partially offset by tax effects and the assumption of losses.

Income taxes mainly comprise income from the recognition of deferred tax assets on loss carryforwards and income from current taxes in previous years.

Distributions may not be made on silent participations in the event that a net loss for the year or an accumulated loss is determined. Furthermore, based on the corresponding contractual agreement, equity instruments must also share in the net loss for the year or an accumulated loss in the event of a net loss for the year or an accumulated loss. In the 2018 financial year, the silent participations shared in the loss reported by Hamburg Commercial Bank AG in the amount of € 327 million (previous year: € 285 million). Silent participations are placed in the international capital markets (€ 389 million) and with domestic/European institutional investors (€ 205 million). The hybrid capital instruments listed on the capital market participated in the group net loss (incl. group net loss carried forward from the 2017 annual financial statements). The carrying amounts of the hybrid instruments, which are listed on the capital markets, correspond to 22.9 % of the original nominal amount due to the attributed losses on the reporting date.

Net assets and financial position

Balance Sheet

(€ m)	2018	2017	Change in %
Assets			
Cash reserve, debt instruments issued by public authorities, bills eligible for rediscount	5,355	6,617	-19
Loans and advances to banks	2,277	2,770	-18
Loans and advances to customers	31,521	40,349	-22
Securities	10,508	15,035	-30
Trading portfolio	2,157	2,696	-20
Equity holdings in non-affiliated companies and interests in affiliated companies	654	631	4
Other assets	2,124	2,232	-5
Total assets	**54,596**	**70,330**	**-22**
Liabilities			
Liabilities to banks	6,012	8,891	-32
Liabilities to customers	28,427	36,822	-23
Securitised liabilities	10,399	14,086	-26
Trading portfolio	1,163	1,414	-18
Subordinated debt	1,055	1,048	1
Fund for general banking risks	2,366	2,362	0
Equity capital	2,641	3,250	-19
Other liabilities	2,533	2,457	3
Total assets	**54,596**	**70,330**	**-22**
Contingent liabilities	1,869	2,022	-8
Other obligations	7,646	6,724	14
Derivatives held in the banking book (credit equivalents)	449	616	-27
Total off balance sheet business	**9,964**	**9,362**	**6**
Business volume	**64,560**	**79,692**	**-19**

Decrease in total assets

The Group's total assets fell by around one-fifth in the 2018 financial year to € 54,596 million (31 December 2017: € 70,330 million). The following developments were decisive for the decline in total assets:

The cash reserve fell compared with the previous year-end to € 5,355 million (31 December 2017: € 6,617 million). Loans and advances to banks also decreased and amounted to € 2,277 million (31 December 2017: € 2,770 million). Hamburg Commercial Bank AG's active liquidity management, which aims, among other things, to gradually reduce the excess liquidity built up during the privatisation period, led in particular to a decline in balances at central banks.

Loans and advances to customers came to € 31,521 million (31 December 2017: € 40,349 million), also below the level seen in the previous year. The decline is mainly due to the closing of the portfolio transaction. In connection with the closing of the privatisation process, the portfolio transaction agreed to relieve Hamburg Commercial Bank AG of large parts of its non-performing legacy loans and the early termination of the second loss guarantee were implemented at the same time.

The volume of the securities portfolio also fell from € 15,035 million to € 10,508 million due to active liquidity management. Trading portfolio assets decreased to € 2,157 million (31 December 2017: € 2,696 million). Both debentures and other fixed-interest securities in the trading book and the positive fair values of derivative positions declined.

All material line items on the liability side of the balance sheet decreased. Liabilities to banks declined to € 6,012 million compared to € 8,891 million as at 31 December 2017. Call deposits held at other banks, time deposits and repurchase agreements declined due to lower refinancing requirements. In line with the gradual reduction in excess liquidity, liabilities to customers also declined significantly to € 28,427 million (31 December 2017: € 36,822 million).

Securitised liabilities stood at € 10,399 million (31 December 2017: € 14,086 million), also below the level seen in the previous year. Subordinated liabilities and profit participation capital remained at approximately the same level as in the previous year (31 December 2017: € 1,055 million, previous year: € 1,048 million).

At € 2,641 million as at 31 December 2018, reported equity was significantly lower than at the end of the previous year (31 December 2017: € 3,250 million). In addition to the group net loss for the 2018 financial year, this is due to the loss distribution attributable to the silent partners, which resulted in a lower carrying amount. With regard to the development of the regulatory capital ratios, reference is made to the Risk report in the combined management report of Hamburg Commercial Bank.

BUSINESS VOLUME ALSO DOWN

The business volume decreased in line with the decreasing total assets and amounted to € 64,560 million (31 December 2017: 79,692 million). Contingent liabilities, which essentially comprise guarantees and warranties, also fell to € 1,869 million (31 December 2017: € 2,022 million), whereas other commitments, which mainly consist of irrevocable loan commitments, increased slightly to € 7,646 million (31 December 2017: € 6,724 million).

Refinancing

Hamburg Commercial Bank AG successfully implemented its funding strategy in the year under review by using various funding sources. The regulatory requirements for the liquidity ratios were exceeded by far during the reporting period. Further details can be found in the combined management report of Hamburg Commercial Bank.

Hamburg/Kiel, den 15. März 2019

Stefan Ermisch Ulrik Lackschewitz

Dr. Nicolas Blanchard Oliver Gatzke

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Group statement of income

for the period 1 January to 31 December 2018

(€ m)	Note	2018[1]	After adjustment (see Note 3) 2017	Change in %
Interest income from financial assets categorised as AC and FVOCI		923	1,130	-18
Interest income from other financial instruments		1,592	1,657	-4
Negative interest on investments categorised as AC and FVOCI		-21	-30	-30
Negative interest on other cash investments and derivatives		-227	-275	-17
Interest expenses		-1,893	-2,202	-14
Positive interest on borrowings and derivatives		224	296	-24
Net income/loss from hybrid financial instruments		994	304	> 100
Net interest income	(8)	**1,592**	**880**	**81**
Net commission income	(9)	35	65	-46
Result from hedging	(10)	-9	-18	50
Result from financial instruments categorised as FVPL[1]	(11)	-136	254	> -100
Net income from financial investments	(12)	102	62	65
Result from the disposal of financial assets classified as AC	(13)	2	302	-99
Net income from financial investments accounted for under the equity method		–	2	-100
Total income		**1,586**	**1,547**	**3**
Loan loss provisions	(15)	-316	-2,086	-85
Hedging effect of credit derivative second loss guarantee	(2)	-51	810	> -100
Total income after loan loss provisions	(18)	**1,219**	**271**	**> 100**
Administrative expenses	(16)	-402	-481	-16
Other operating result	(17)	-107	21	> -100
Expenses for regulatory affairs, deposit guarantee fund and banking associations	(18)	-89	-49	82
Net income before restructuring and privatisation		**621**	**-238**	**> 100**
Net income from restructuring and privatisation	(19)	-366	-66	> -100
Expenses for government guarantees	(20)	-158	-149	6
Net income before taxes		**97**	**-453**	**> 100**
Income tax expenses	(21)	-20	-75	-73
Group net result		**77**	**-528**	**> 100**
Group net result attributable to non-controlling interests		7	7	–
Group net result attributable to Hamburg Commercial Bank shareholders		70	-535	> 100

[1] In the previous year, under IAS 39, the item Net trading income.

Earnings per Share

(€)	Note	2018	2017
Undiluted	(23)	0.23	-1.77
Diluted	(23)	0.23	-1.77
Number of shares (millions)		**302**	**302**

Group statement of comprehensive income

for the period 1 January to 31 December 2018

Reconciliation with total comprehensive income/loss

(€ m)	2018	2017
Group net result	**77**	**-528**
Income and expense that have been reclassified to the statement of income or may be reclassified at a later date		
Changes in the fair value of financial assets classified as FVOCI as a mandatory requirement (before taxes)		
Unrealised gains and losses (before taxes)	-115	n.r.
Gains and losses (before taxes) reclassified to the statement of income	-103	n.r.
of which from exchange rate effects	1	n.r.
Income taxes recognised	70	n.r.
	-148	**n.r.**
Changes in fair value of AfS financial instruments		
Unrealised gains and losses (before taxes)	n.r.	-26
Gains and losses (before taxes) reclassified to the statement of income	n.r.	1
of which from exchange rate effects	n.r.	-17
Income taxes recognised	n.r.	7
	n.r.	**-18**
Differences resulting from currency translation	19	-57
	19	**-57**
Subtotal	**-129**	**-75**
Income and expenses that will not be reclassified to the statement of income at a later date		
Credit risk-induced changes in the value of liabilities designated at fair value (before taxes)	-9	-3
Income taxes recognised	2	1
	-7	**-2**
Changes resulting from the revaluation of net defined benefit liabilities (before taxes)	63	46
Income taxes recognised	-19	-18
Reclassification of losses arising from the revaluation of net defined benefit liabilities due to disposal	11	–
	55	**28**
Subtotal	**48**	**26**
Other comprehensive income for the period	**-81**	**-49**
Total comprehensive income	**-4**	**-577**
Total comprehensive income attributable to non-controlling interests	7	8
Total comprehensive income attributable to Hamburg Commercial Bank shareholders	-11	-585

Group statement of financial position

as at 31 December 2018

Assets

(€ m)	Note	2018	2017	Change in %
Cash reserve	(24)	5,362	6,625	-19
Loans and advances to banks	(25)	3,167	3,838	-17
Loans and advances to customers	(26)	32,791	39,174	-16
Loan loss provisions	(27)	-831	687	> 100
Credit derivative under the second loss guarantee	(2)	–	1,014	-100
Positive fair values of hedging derivatives	(28)	175	264	-34
Positive adjustment item from portfolio fair value hedges		200	255	-22
Trading assets	(29)	3,094	3,641	-15
Financial investments	(30)	10,100	13,647	-26
Intangible assets	(31)	8	10	-20
Property, plant and equipment	(32)	139	232	-40
Investment property	(33)	40	13	> 100
Non-current assets held for sale and disposal groups	(33)	65	139	-53
Current tax assets	(34)	49	46	7
Deferred tax assets	(35)	713	723	-1
Other assets	(36)	49	74	-34
Total assets		**55,121**	**70,382**	**-22**

Liabilities

(€ m)	Note	2018	2017	Change in %
Liabilities to banks	(37)	5,470	8,271	-34
Liabilities to customers	(38)	28,093	36,205	-22
Securitised liabilities	(39)	9,458	12,444	-24
Negative fair value of hedging derivatives		501	163	>100
Negative adjustment item from portfolio fair value hedges		460	553	-17
Trading liabilities	(40)	2,812	3,875	-27
Provisions	(41)	1,746	1,438	21
Liabilities relating to disposal groups	(45)	–	47	-100
Current tax liabilities	(44)	12	103	-88
Other liabilities	(46)	518	658	-21
Subordinated capital	(47)	1,614	2,252	-28
Equity	(48)	4,437	4,373	1
Share capital		3,018	3,018	–
Capital reserve		75	75	–
Retained earnings		1,012	1,701	-41
Revaluation reserve		238	117	>100
Currency conversion reserve		22	2	>100
Group net result		70	-535	> 100
Total before non-controlling interests		4,435	4,378	1
Non-controlling interests		2	-5	> 100
Total liabilities		**55,121**	**70,382**	**-22**

Group statement of changes in equity

(€ m)	Note	Share capital	Capital reserve
As at 1 January 2017		**3,018**	**75**
Change due to early application of IFRS 9.5.7.7 in conjunction with IAS 1.7 (f)		–	–
Adjusted amount as at 1 January 2017		**3,018**	**75**
Group net result		–	–
Changes resulting from the revaluation of net defined benefit liabilities		–	–
Changes in fair value of AfS financial instruments		–	–
Credit risk-induced changes in the value of liabilities designated at fair value[1]		–	–
Exchange rate changes			
thereof resulting from currency translation		–	–
thereof resulting from changes in scope of consolidation		–	–
Other comprehensive income		–	–
Comprehensive income as at 31 December 2017		**–**	**–**
Addition of the Group retained earnings for the previous year		–	–
Reclassifications		–	–
As at 31 December 2017		**3,018**	**75**
As at 1 January 2018		**3,018**	**75**
Effects from the first-time application of IFRS 9[2]		–	–
Adjusted amount as at 1 January 2018		**3,018**	**75**
Group net result		–	–
Changes resulting from the revaluation of net defined benefit liabilities		–	–
Reclassification of losses arising from the revaluation of net defined benefit liabilities due to disposal		–	–
Credit risk-induced changes in the value of liabilities designated at fair value[1]		–	–
Changes in the fair value of financial assets classified as FVOCI as a mandatory requirement		–	–
Exchange rate changes			
thereof resulting from currency translation		–	–
Other comprehensive income		–	–
Comprehensive income as at 31 December 2018		**–**	**–**
Reclassification of losses arising from the revaluation of net defined benefit liabilities due to disposal		–	–
Compensation for the Group net result for the previous year		–	–
As at 31 December 2018	(50)	**3,018**	**75**

[1] The reclassification of the credit risk-induced changes in the value of liabilities designated at fair value to retained earnings is due to the repurchase of issues/promissory note loans.

[2] Contrary to the presentation as at 30 June 2018, the value for the Group net result is reported under retained earnings.

Retained earnings	Currency conversion reserve	Revaluation reserve	Group net result	Total before non-controllinginterests	Non-controllingin-terests	Total
1,617	**60**	**127**	**67**	**4,964**	**-14**	**4,950**
-9	–	9	–	–	–	–
1,608	**60**	**136**	**67**	**4,964**	**-14**	**4,950**
–	–	–	-535	-535	7	-528
28	–	–	–	28	–	28
–	–	-18	–	-18	–	-18
-1	–	-1	–	-2	–	-2
–	-54	–	–	-54	1	-53
–	-4	–	–	-4	–	-4
27	-58	-19	–	-50	1	-49
27	**-58**	**-19**	**-535**	**-585**	**8**	**-577**
67	–	–	-67	–	–	–
-1	–	–	–	-1	1	–
1,701	**2**	**117**	**-535**	**4,378**	**-5**	**4,373**
1,701	**2**	**117**	**-535**	**4,378**	**-5**	**4,373**
-198	1	276	–	79	–	79
1,503	**3**	**393**	**-535**	**4,457**	**-5**	**4,452**
–	–	–	70	70	7	77
44	–	–	–	44	–	44
11	–	–	–	11	–	11
–	–	-7	–	-7	–	-7
–	–	-148	–	-148	–	-148
–	19	–	–	19	–	19
55	19	-155	–	-81	–	-81
55	**19**	**-155**	**70**	**-11**	**7**	**-4**
-11	–	–	–	-11	–	-11
-535	–	–	535	–	–	–
1,012	**22**	**238**	**70**	**4,435**	**2**	**4,437**

Group cash flow statement

Cash flow statement

(€ m)		2018		2017
Net result for the period		77		-528
Reconciliation with cash flow from operating activities				
Depreciation, impairments and write-ups on loans and advances, property, plant and equipment, financial investments, intangible assets and investment property		335		1,517
a) Loans and advances to customers and banks	320	–	1,456	–
b) Financial investments	-3	–	19	–
c) Property, plant and equipment/intangible assets/investment property	18	–	42	–
Changes in provisions		524		1
Other non-cash expenses/income		436		-1,036
Profit/loss from disposal of financial investments and property, plant and equipment/investment property		-119		-125
a) Financial investments	-102		-124	
b) Property, plant and equipment/investment property	-17	–	-1	–
Other adjustments		-1,620		-1,126
Subtotal		**-367**		**-1,297**
Changes in loans and advances		3,078		10,108
a) to banks	679	–	349	–
b) to customers	2,399	–	9,759	–
Changes in trading assets		327		2,184
Changes in other assets from continuing operations		5,974		1,954
Changes in liabilities		-10,872		-5,204
a) to banks	-2,796	–	-1,229	–
b) to customers	-8,076	–	-3,975	–
Changes in securitised liabilities		-2,624		-3,979
Changes in trading liabilities		-763		-2,285
Changes in other liabilities from continuing operations		-427		-302
Interest and dividends received		2,381		2,946
Interest paid		-1,755		-2,143
Income tax payments		-94		15
Cash flow from operating activities		**-5,142**		**1,997**
Receipts from disposals of		4,144		4,226
a) securities	4,144	–	3,667	–
b) interests in affiliated companies and equity holdings	6	–	78	–
c) property, plant and equipment	-6	–	481	–
Purchases of		-265		-2,133
a) securities	-368	–	-2,111	–
b) interests in affiliated companies and equity holdings	-8	–	-16	–
c) property, plant and equipment	111	–	-6	–
Change from the sale/acquisition of consolidated subsidiaries		–		75
Cash flow from investing activities		**3,879**		**2,168**

Cash flow statement

(€ m)	2018	2017
Payments made (-) from subordinated capital	–	-1,031
Payments made to company owners and minority shareholders		
Cash flow from financing activities	**–**	**-1,031**
Cash and cash equivalents at the beginning of the period	**6,625**	**3,491**
Cash flow from operating activities	-5,142	1,997
Cash flow from investing activities	3,879	2,168
Cash flow from financing activities	–	-1,031
Cash and cash equivalents at the end of the period	**5,362**	**6,625**

Cash and cash equivalents are equivalent to the Cash reserve item in the statement of financial position and comprise cash on hand, balances at central banks, treasury bills, discounted treasury notes and similar debt instruments issued by public-sector bodies and bills of exchange.

The cash flow from operating activities is calculated using the indirect method, whereby the Group net income/loss for the year is adjusted for non-cash expenses (increased) and non-cash income (reduced) and for cash changes in assets and liabilities used in operating activities.

The following cash flows and effects on assets and liabilities resulted from the obtaining or loss of control over subsidiaries during the financial year:

Cash flow

	2018		2017	
(€ m)	Obtaining control	Loss of control	Obtaining control	Loss of control
Amounts paid/received	–	–	–	74
of which: cash and cash equivalents	–	–	–	74
Amount of cash and cash equivalents	–	–	1	–

Assets

	2018		2017	
(€ m)	Obtaining control	Loss of control	Obtaining control	Loss of control
Loans and advances to customers	–	2	–	–
Non-current assets held for sale and disposal groups	–	14	480	77
Other assets	–	–	4	–

Liabilities

	2018		2017	
(€ m)	Obtaining control	Loss of control	Obtaining control	Loss of control
Liabilities to customers	–	22	30	–
Liabilities relating to disposal groups	–	1	–	1
Other liabilities	–	–	2	–

The table below shows a reconciliation of balance sheet values to cash flow from financing activities.

(€ m)	Other subordinated capital	Silent participations	Profit participation capital
Balance sheet value as at 1 January 2018	**1,060**	**1,192**	**–**
Cash changes			–
Other changes – interest paid	-15	–	–
Non-cash changes	–	–	–
Changes due to exchange rate fluctuations	–	13	–
Change in fair value	22	-658	–
Balance sheet value as at 31 December 2018	**1,067**	**547**	**–**

(€ m)	Other subordinated capital	Silent participations	Profit participation capital
Balance sheet value as at 1 January 2017	**2,110**	**1,412**	**14**
Cash changes			
Payments made	-1,017	–	-14
Other changes – interest paid	-13	–	–
Non-cash changes			
Changes due to exchange rate fluctuations	–	-45	–
Change in fair value	-19	-175	–
Other changes	-1	–	–
Balance sheet value as at 31 December 2017	**1,060**	**1,192**	**–**

Balance sheet item reconciliation from IAS 39 to IFRS 9

Introduction

The initial application of IFRS 9 results in changes in the carrying amounts between the closing balance sheet in accordance with IAS 39 as at 31 December 2017 and the opening balance sheet in accordance with IFRS 9 as at 1 January 2018. The differences in carrying amounts will be recognised in equity. The changes relate to financial instruments and are based on the new classification, measurement and impairment provisions set out in IFRS 9 (see the section entitled "Accounting and measurement principles" in the chapter entitled "Application of accounting methods IFRS 9 - Financial instruments"). These provisions are to be applied retrospectively in principle. In accordance with the option provided for in IFRS 9.7.2.15, Hamburg Commercial Bank has opted not to adjust the comparative figures in the consolidated statement of financial position and has prepared a reconciliation from the closing balance sheet in accordance with IAS 39 as at 31 December 2017 to the opening balance sheet in accordance with IFRS 9 as at 1 January 2018.

The reconciliation has been prepared in accordance with the requirements set out in IFRS 7.42L to IFRS 7.42O. The balance sheet carrying amounts in the closing balance sheet in accordance with IAS 39 are reconciled to the balance sheet carrying amounts of the opening balance sheet in accordance with IFRS 9. The information is provided using two tables for each balance sheet item containing financial instruments. For the reconciliation of total loan loss provisions in accordance with IAS 39 to total loan loss provisions in accordance with IFRS 9, a further table was also prepared in line with the requirements of IFRS 7.42P.

In the following tables, it is important to note that the reconciliation tables for the balance sheet items "Loans and advances to banks" and "Loans and advances to customers" are shown before deductions for loan loss provisions, as these are shown in a separate reconciliation table in line with the presentation in the consolidated statement of financial position. By contrast, the reconciliation table for financial investments is shown after deductions for impairment (loan loss provisions) in line with the presentation in the consolidated statement of financial position. In the table "Reconciliation of measurement categories and carrying amounts of financial instruments from IFRS 9 to IAS 39", the balance sheet carrying amounts in accordance with IFRS 9 are reconciled, per financial instrument category and per measurement category in accordance with IFRS 9, to the balance sheet carrying amounts per measurement category under IAS 39. The categories of financial instruments required under IFRS 7.6 were adjusted as at 1 January 2018 to reflect the new classification and measurement provisions in accordance with IFRS 9 (see the section entitled "Accounting and measurement principles" in the chapter entitled "Application of accounting methods IFRS 9 - Financial instruments"). The total amount in the "IAS 39 carrying amount" column corresponds to the value shown in the consolidated statement of financial position for the balance sheet item in question as at 31 December 2017.

The table entitled "Reconciliation of carrying amounts from IAS 39 to IFRS 9 based on the categories of financial instruments under IFRS 7" shows the balance sheet carrying amounts under IAS 39 for each IAS 39 measurement category ("IAS 39 carrying amount" column). The total amount in the "IAS 39 carrying amount" column corresponds to the value shown in the consolidated statement of financial position for the balance sheet item in question as at 31 December 2017. The rows "from" show the values for each measurement and holding category under IAS 39. The rows "to" show the values for each measurement category and category of financial instruments under IFRS 9. The IAS 39 balance sheet carrying amounts for each measurement category under IFRS 9 are visible in the "Reclassifications" column. The balance sheet carrying amounts in accordance with IFRS 9 as at 1 January 2018 are shown in the "IFRS 9 carrying amount" column. The difference between the columns "Reclassifications" and "IFRS 9 carrying amount" column is displayed in the "Remeasurement" column and represents the measurement difference between IAS 39 and IFRS 9. This value corresponds to change in equity which is directly related to the initial application of IFRS 9 ("Equity effect" column). The equity effects resulting from the initial application of IFRS 9 as at 1 January 2018 are explained in the section "Explanatory information" below the reconciliation tables. This section shows, for example, how the equity effect is distributed proportionately among retained earnings and the revaluation reserve, and what the main drivers of the equity effects are.

Reconciliation of balance sheet items in accordance with IFRS 7.42L

Financial assets

RECONCILIATION OF MEASUREMENT CATEGORIES AND CARRYING AMOUNTS OF FINANCIAL INSTRUMENTS FROM IFRS 9 TO IAS 39
Cash reserve

(€ m)	01.01.2018		31.12.2017	
Categories of financial instruments in accordance with IFRS 7 in conjunction with IFRS 9	IFRS 9 measurement category	IFRS 9 carrying amount	IAS 39 measurement category	IAS 39 carrying amount
AC assets	Amortised cost (AC)	6,625	measured at amortised cost (LaR)	6,519
			measured at fair value (AfS)	106
		6,625		**6,625**
Total		**6,625**		**6,625**

RECONCILIATION OF CARRYING AMOUNTS FROM IAS 39 TO IFRS 9 BASED ON THE CATEGORIES OF FINANCIAL INSTRUMENTS UNDER IFRS 7
Cash reserve

(€ m)			31.12.2017	01.01.2018			
			IAS 39 carrying amount	Reclassification	Remeasurement	IFRS 9 carrying amount	Equity effect
From	measured at amortised cost (AC)	Loans and receivables (LaR)	6,519				
To	Amortised cost (AC)	AC assets		6,519	–	6,519	–
			6,519	**6,519**	**–**	**6,519**	**–**
From	measured at fair value	Available for Sale (AfS)	106				
To	Amortised cost (AC)	AC assets		106	–	106	–
			106	**106**	**–**	**106**	**–**
Total			**6,625**	**6,625**	**–**	**6,625**	**–**

RECONCILIATION OF MEASUREMENT CATEGORIES AND CARRYING AMOUNTS OF FINANCIAL INSTRUMENTS FROM IFRS 9 TO IAS 39
Loans and advances to banks

(€ m)	01.01.2018		31.12.2017	
Categories of financial instruments in accordance with IFRS 7 in conjunction with IFRS 9	IFRS 9 measurement category	IFRS 9 carrying amount	IAS 39 measurement category	IAS 39 carrying amount
AC assets	Amortised cost (AC)	3,561	measured at amortised cost (LaR)	3,561
		3,561		**3,561**
FVPL Other	Fair Value through Profit or Loss (FVPL)	79	measured at fair value (AfS)	79
		79		**79**
FVOCI Mandatory	Fair Value through Other Comprehensive Income (FVOCI)	204	measured at amortised cost (LaR)	197
		204		**197**
Total		**3,845**		**3,838**

RECONCILIATION OF CARRYING AMOUNTS FROM IAS 39 TO IFRS 9 BASED ON THE CATEGORIES OF FINANCIAL INSTRUMENTS UNDER IFRS 7

Loans and advances to banks

(€ m)			31.12.2017	01.01.2018			
			IAS 39 carrying amount	Reclassification	Remeasurement	IFRS 9 carrying amount	Equity effect
From	measured at amortised cost (AC)	Loans and receivables (LaR)	3,759	–	–	–	–
To	Amortised cost (AC)	AC assets		3,562	–	3,562	–
	Fair Value through Other Comprehensive Income (FVOCI)	FVOCI Mandatory		197	7	204	7
			3,759	**3,759**	**7**	**3,766**	**7**
From	measured at fair value	Available for Sale (AfS)	79	–	–	–	–
To	Fair Value through Profit or Loss (FVPL)	FVPL Other		79	–	79	–
			79	**79**	**–**	**79**	**–**
Total			**3,838**	**3,838**	**7**	**3,845**	**7**

RECONCILIATION OF MEASUREMENT CATEGORIES AND CARRYING AMOUNTS OF FINANCIAL INSTRUMENTS FROM IFRS 9 TO IAS 39

Loans and advances to customers

(€ m)	01.01.2018		31.12.2017	
Categories of financial instruments in accordance with IFRS 7 in conjunction with IFRS 9	IFRS 9 measurement category	IFRS 9 carrying amount	IAS 39 measurement category	IAS 39 carrying amount
AC assets	Amortised cost (AC)	30,519	measured at amortised cost (LaR)	30,403
		30,519		**30,403**
FVPL Other	Fair Value through Profit or Loss (FVPL)	2,681	measured at amortised cost (LaR)	6,230
			measured at fair value (DFV)	85
			measured at fair value (AfS)	45
FVPL Designated		124	measured at amortised cost (LaR)	8
			measured at fair value (DFV)	118
		2,805		**6,486**
FVOCI Mandatory	Fair Value through Other Comprehensive Income (FVOCI)	2,289	measured at amortised cost (LaR)	1,157
			measured at fair value (DFV)	1,052
		2,289		**2,209**
No category	Receivables under finance leases	76	Receivables under finance leases	76
Total		**35,689**		**39,174**

RECONCILIATION OF CARRYING AMOUNTS FROM IAS 39 TO IFRS 9 BASED ON THE CATEGORIES OF FINANCIAL INSTRUMENTS UNDER IFRS 7

Loans and advances to customers

(€ m)			31.12.2017		01.01.2018		
			IAS 39 carrying amount	Reclassi-fication	Re-measure-ment	IFRS 9 carrying amount	Equity effect
From	measured at amortised cost (AC)	Loans and receivables (LaR)	37,798				
To	Amortised cost (AC)	AC assets		30,403	116	30,519	116
	Fair Value through Profit or Loss (FVPL)	FVPL Other		6,230	-3,679	2,551	-3,679
		FVPL Designated		8	-2	6	-2
				6,238	-3,681	2,557	-3,681
	Fair Value through Other Comprehensive Income (FVOCI)	FVOCI Mandatory		1,157	80	1,237	80
			37,798	**37,798**	**-3,485**	**34,313**	**-3,485**
From	measured at fair value	Designated at Fair Value (DFV)	1,255	–	–	–	–
To	Fair Value through Profit or Loss (FVPL)	FVPL Other		85	–	85	–
		FVPL Designated		118	–	118	–
	Fair Value through Other Comprehensive Income (FVOCI)	FVOCI Mandatory		1,052	–	1,052	–
			1,255	**1,255**	**–**	**1,255**	**–**
From	measured at fair value	Available for Sale (AfS)	45	–	–	–	–
To	Fair Value through Profit or Loss (FVPL)	FVPL Other		45	–	45	–
			45	**45**	**–**	**45**	**–**
	Fair Value through Other Comprehensive Income (FVOCI)	FVOCI Mandatory		–	–	–	–
				45	–	45	–
From	Receivables under finance leases	No IAS 39 category	76				
To	Receivables under finance leases	No category		76	–	76	–
			76	76	–	76	–
Total			**39,174**	**39,174**	**-3,485**	**35,689**	**-3,485**

RECONCILIATION OF MEASUREMENT CATEGORIES AND CARRYING AMOUNTS OF FINANCIAL INSTRUMENTS FROM IFRS 9 TO IAS 39

Loan loss provisions

(€ m)	01.01.2018		31.12.2017	
Categories of financial instruments in accordance with IFRS 7 in conjunction with IFRS 9	IFRS 9 measurement category	IFRS 9 carrying amount	IAS 39 measurement category	IAS 39 carrying amount
AC assets	Amortised cost (AC)	-978	measured at amortised cost (LaR)	-751
		-978		-751
FVPL Other	Fair Value through Profit or Loss (FVPL)	–	measured at amortised cost (LaR)	-199
FVPL Designated			measured at amortised cost (LaR)	-3,544
	1)	–		-3,743
		-978		-4,494
Compensation under the second loss guarantee for financial instruments not assigned to the FVPL category[2]		1,697		5,181
Total		**719**		**687**

[1] In the case of these amounts, the reclassification of the financial assets to fair value measurement means that the loan loss provisions are derecognised and implicitly included as a component of the fair value measurement in the balance sheet carrying amount.

[2] The reclassification of financial assets to fair value measurement leads to transfers from the balance sheet item "loan loss provisions" to the balance sheet item "Compensation item for financial instruments categorised as FVPL under the second loss guarantee" in an amount of € 3,484 million.

RECONCILIATION OF CARRYING AMOUNTS FROM IAS 39 TO IFRS 9 BASED ON THE CATEGORIES OF FINANCIAL INSTRUMENTS UNDER IFRS 7

Loan loss provisions

(€ m)			31.12.2017			01.01.2018	
			IAS 39 carrying amount	Reclassification	Remeasurement	IFRS 9 carrying amount	Equity effect
From	measured at amortised cost (AC)	Loans and receivables (LaR)	-4,494				
To	Amortised cost (AC)	AC assets		-751	-227	-978	-227
	Fair Value through Profit or Loss (FVPL)	FVPL Other		-199	199	–	199
		FVPL Designated		-3,544	3,544	–	3,544
		1)		-3,743	3,743		3,743
			-4,494	**-4,494**	**3,516**	**-978**	**3,516**
	Compensation under the second loss guarantee (excl. financial instruments categorised as FVPL)[2]		5,181	5,181	-3,484	1,697	-3,484
Total			**687**	**687**	**32**	**719**	**32**

[1] In the case of these amounts, the reclassification of the financial assets to fair value measurement means that the loan loss provisions are derecognised and implicitly included as a component of the fair value measurement in the balance sheet carrying amount.

[2] The reclassification of financial assets to fair value measurement leads to transfers from the balance sheet item "loan loss provisions" to the balance sheet item "Compensation item for financial instruments categorised as FVPL under the second loss guarantee" in an amount of € 3,484 million.

RECONCILIATION OF MEASUREMENT CATEGORIES AND CARRYING AMOUNTS OF FINANCIAL INSTRUMENTS FROM IFRS 9 TO IAS 39

Compensation item for financial instruments categorised as FVPL under the second loss guarantee

(€ m)	01.01.2018		31.12.2017	
Categories of financial instruments in accordance with IFRS 7 in conjunction with IFRS 9	IFRS 9 measurement category	IFRS 9 carrying amount	IAS 39 measurement category	IAS 39 carrying amount
FVPL Other	Fair Value through Profit or Loss (FVPL) [1]	3,484	measured at amortised cost (LaR)	–

[1] These amounts relate to the transfer of compensation amounts from the balance sheet item "Loan loss provisions" to the balance sheet item "Compensation item for financial instruments categorised as FVPL under the second loss guarantee". This is due to the reclassification of individual financial assets from the LaR/ AfS categories to the FVPL measurement category.

RECONCILIATION OF CARRYING AMOUNTS FROM IAS 39 TO IFRS 9 BASED ON THE CATEGORIES OF FINANCIAL INSTRUMENTS UNDER IFRS 7

Compensation item for financial instruments categorised as FVPL under the second loss guarantee

(€ m)			31.12.2017	01.01.2018			
			IAS 39 carrying amount	Reclassification	Remeasurement	IFRS 9 carrying amount	Equity effect
From	measured at amortised cost (AC)	Loans and receivables (LaR)	–				
To	Fair Value through Profit or Loss (FVPL)	FVPL Other[1]	–	–	3,484	3,484	3,484
Total			**–**	**–**	**3,484**	**3,484**	**3,484**

[1] These amounts relate to the transfer of compensation amounts from the balance sheet item "loan loss provisions" to the balance sheet item "Compensation item for financial instruments categorised as FVPL under the second loss guarantee". This is due to the reclassification of individual financial assets from the LaR/ AfS categories to the FVPL measurement category.

Reconciliation of impairments in accordance with IFRS 7.42P

Financial assets

Loan loss provisions for loans and advances to banks

		31.12.2017	01.01.2018		
		IAS 39 amount	Reclassification	Remeasurement[1]	IFRS 9 amount
From	measured at amortised cost (LaR)	-1			
To	Amortised cost (AC)		-1	–	-1
		-1	**-1**	**–**	**-1**
Total		**-1**	**-1**	**–**	**-1**

[1] The amounts on the remeasurement of the loan loss provisions under IFRS 9 include the effects resulting from the retroactive application of the modification provisions.

Loan loss provisions for loans and advances to customers

		31.12.2017	01.01.2018			
		IAS 39 amount	Reclassification		Remeasurement[2]	IFRS 9 amount
From	measured at amortised cost (LaR)	-4,493	–		0	0
To	Amortised cost (AC)		-750		-227	-977
	Fair Value through Profit or Loss (FVPL) [1]		-3,743	Derecognition of IAS 39 amount due to reclassification	3,743	–
		-4,493	**-4,493**		**3,516**	**-977**
Total		**-4,493**	**-4,493**		**3,516**	**-977**

[1] In the case of these amounts, the reclassification of the financial assets to fair value measurement means that the loan loss provisions are derecognised and implicitly included as a component of the fair value measurement in the balance sheet carrying amount.

[2] The amounts on the remeasurement of the loan loss provisions under IFRS 9 include the effects resulting from the retroactive application of the modification provisions.

Loan loss provisions for financial investments

		31.12.2017	01.01.2018			
		IAS 39 amount	Reclassification		Remeasurement[2]	IFRS 9 amount
From	measured at amortised cost (LaR)	-4				
To	Amortised cost (AC)		-2		2	–
	Fair Value through Profit or Loss (FVPL) [1]		-2	Derecognition of IAS 39 amount due to reclassification	2	–
	Fair Value through Other Comprehensive Income (FVOCI)		–		-7	-7
		-4	**-4**		**-3**	**-7**
From	measured at fair value (AfS)	-79				
To	Fair Value through Profit or Loss (FVPL) [1]		-79	Derecognition of IAS 39 amount due to reclassification	79	–
		-79	-79		79	–
Total		**-83**	**-83**		**76**	**-7**
Total			**-81**	**Derecognition of IAS 39 amount due to reclassification**		

[1] In the case of these amounts, the reclassification of the financial assets to fair value measurement means that the loan loss provisions are derecognised and implicitly included as a component of the fair value measurement in the balance sheet carrying amount.

[2] The amounts on the remeasurement of the loan loss provisions under IFRS 9 include the effects resulting from the retroactive application of the modification provisions.

Loan loss provisions for compensation under the second loss guarantee (excl. financial instruments categorised as FVPL)

		31.12.2017	01.01.2018			
		IAS 39 amount	Reclassification		Remeasurement[1]	IFRS 9 amount
From	measured at amortised cost (LaR)	5,181				
To	Amortised cost (AC)		1,697		–	1,697
	Fair Value through Profit or Loss (FVPL)		3,484	Transfer to compensation item for financial instruments categorised as FVPL under the second loss guarantee	-3,484	–
	Fair Value through Other Comprehensive Income (FVOCI)		–		–	–
		5,181	**5,181**		**-3,484**	**1,697**
Total		**5,181**	**5,181**		**-3,484**	**1,697**
Total			**-3,484**	**Transfer to compensation item for financial instruments categorised as FVPL under the second loss guarantee**		

[1] The amounts on the remeasurement of the loan loss provisions under IFRS 9 include the effects resulting from the retroactive application of the modification provisions.

Reconciliation of impairments in accordance with IFRS 7.42P

Off-balance-sheet transactions

Provisions in the lending business

	31.12.2017		01.01.2018		
	IAS 39 amount	Reclassification of non-financial instruments acc. to IAS 37		Remeasurement	IFRS 9 amount
Contingent liabilities	11				10
Irrevocable loan commitments	35				26
Other credit risks	21				20
Total	**67**	**-14**		**3**	56

Reconciliation of balance sheet items in accordance with IFRS 7.42L (continued)

Financial assets

RECONCILIATION OF MEASUREMENT CATEGORIES AND CARRYING AMOUNTS OF FINANCIAL INSTRUMENTS FROM IFRS 9 TO IAS 39
Credit derivative under the second loss guarantee

(€ m)	01.01.2018		31.12.2017	
Categories of financial instruments in accordance with IFRS 7 in conjunction with IFRS 9	IFRS 9 measurement category	IFRS 9 carrying amount	IAS 39 measurement category	IAS 39 carrying amount
FVPL Trading	Fair Value through Profit or Loss (FVPL)	1,014	measured at fair value (HfT)	1,014

RECONCILIATION OF CARRYING AMOUNTS FROM IAS 39 TO IFRS 9 BASED ON THE CATEGORIES OF FINANCIAL INSTRUMENTS UNDER IFRS 7
Credit derivative under the second loss guarantee

(€ m)			31.12.2017		01.01.2018		
			IAS 39 carrying amount	Reclassification	Remeasurement	IFRS 9 carrying amount	Equity effect
From	measured at fair value	Held for Trading (HfT)	1,014				
To	Fair Value through Profit or Loss (FVPL)	FVPL Trading		1,014	–	1,014	–

RECONCILIATION OF MEASUREMENT CATEGORIES AND CARRYING AMOUNTS OF FINANCIAL INSTRUMENTS FROM IFRS 9 TO IAS 39
Positive fair value of hedging derivatives

(€ m)	01.01.2018		31.12.2017	
Categories of financial instruments in accordance with IFRS 7 in conjunction with IFRS 9	IFRS 9 measurement category	IFRS 9 carrying amount	IAS 39 measurement category	IAS 39 carrying amount
n.a.	Fair Value through Profit or Loss (FVPL)	264	measured at fair value	264

RECONCILIATION OF CARRYING AMOUNTS FROM IAS 39 TO IFRS 9 BASED ON THE CATEGORIES OF FINANCIAL INSTRUMENTS UNDER IFRS 7
Positive fair value of hedging derivatives

(€ m)			31.12.2017		01.01.2018		
			IAS 39 carrying amount	Reclassification	Remeasurement	IFRS 9 carrying amount	Equity effect
From	measured at fair value	n.a.	264	–	–	–	–
To	Fair Value through Profit or Loss (FVPL)	n.a.		264	–	264	–

RECONCILIATION OF MEASUREMENT CATEGORIES AND CARRYING AMOUNTS OF FINANCIAL INSTRUMENTS FROM IFRS 9 TO IAS 39

Positive adjustment item from portfolio fair value hedges

(€ m)	01.01.2018		31.12.2017	
Categories of financial instruments in accordance with IFRS 7 in conjunction with IFRS 9	IFRS 9 measurement category	IFRS 9 carrying amount	IAS 39 measurement category	IAS 39 carrying amount
No category	n.a.	255	n.a.	255

RECONCILIATION OF CARRYING AMOUNTS FROM IAS 39 TO IFRS 9 BASED ON THE CATEGORIES OF FINANCIAL INSTRUMENTS UNDER IFRS 7

Positive adjustment item from portfolio fair value hedges

(€ m)			31.12.2017			01.01.2018	
			IAS 39 carrying amount	Reclassification	Remeasurement	IFRS 9 carrying amount	Equity effect
From	n.a.	No IAS 39 category	255				
To	n.a.	No category		255	–	255	–

RECONCILIATION OF MEASUREMENT CATEGORIES AND CARRYING AMOUNTS OF FINANCIAL INSTRUMENTS FROM IAS 39 TO IFRS 9

Trading assets

(€ m)	01.01.2018		31.12.2017	
Categories of financial instruments in accordance with IFRS 7 in conjunction with IFRS 9	IFRS 9 measurement category	IFRS 9 carrying amount	IAS 39 measurement category	IAS 39 carrying amount
FVPL Trading	Fair Value through Profit or Loss (FVPL)	3,550	measured at fair value (HfT)	3,550
	[1]	–		91
Total		**3,550**		**3,641**

[1] In the case of these amounts, the abandonment of the intent to trade results in a transfer from the balance sheet item “Trading assets” to the balance sheet item “Financial investments”.

RECONCILIATION OF CARRYING AMOUNTS FROM IAS 39 TO IFRS 9 BASED ON THE CATEGORIES OF FINANCIAL INSTRUMENTS UNDER IFRS 7

Trading assets

(€ m)			31.12.2017			01.01.2018	
			IAS 39 carrying amount	Reclassification	Remeasurement	IFRS 9 carrying amount	Equity effect
From	measured at fair value	Held for Trading (HfT)	3,641				
To	Fair Value through Profit or Loss (FVPL)	FVPL Trading		3,550	–	3,550	–
		FVPL Other (financial investments)[1]		91	–	–	–
				3,641	–	3,550	-

[1] In the case of these amounts, the abandonment of the intent to trade results in a transfer from the balance sheet item “Trading assets” to the balance sheet item “Financial investments”.

RECONCILIATION OF MEASUREMENT CATEGORIES AND CARRYING AMOUNTS OF FINANCIAL INSTRUMENTS FROM IFRS 9 TO IAS 39

Financial investments

(€ m)	01.01.2018		31.12.2017	
Categories of financial instruments in accordance with IFRS 7 in conjunction with IFRS 9	IFRS 9 measurement category	IFRS 9 carrying amount	IAS 39 measurement category	IAS 39 carrying amount
AC assets	Amortised cost (AC)	103	measured at amortised cost (LaR)	101
		103		**101**
FVPL Other	Fair Value through Profit or Loss (FVPL)	645	measured at amortised cost (LaR)	99
			measured at fair value (DFV)	444
			measured at fair value (AfS)	102
	1)	**91**		**–**
FVPL Designated		168	measured at amortised cost (LaR)	–
			measured at fair value (DFV)	168
		904		**813**
FVOCI Mandatory	Fair Value through Other Comprehensive Income (FVOCI)	12,804	measured at amortised cost (LaR)	360
			measured at fair value (AfS)	12,373
		12,804		**12,733**
Total		**13,811**		**13,647**

1) In the case of these amounts, the abandonment of the intent to trade results in a transfer from the balance sheet item "Trading assets" to the balance sheet item "Financial investments".

RECONCILIATION OF CARRYING AMOUNTS FROM IAS 39 TO IFRS 9 BASED ON THE CATEGORIES OF FINANCIAL INSTRUMENTS UNDER IFRS 7

Financial investments

(€ m)			31.12.2017	01.01.2018			
			IAS 39 carrying amount	Reclassifica-tion	Remeasure-ment	IFRS 9 carrying amount	Equity effect
From	measured at amortised cost (AC)	Loans and receivables (LaR)	560	–	–	–	–
To	Amortised cost (AC)	AC assets		101	2	103	2
	Fair Value through Profit or Loss (FVPL)	FVPL Other		99	–	99	–
	Fair Value through Other Comprehensive Income (FVOCI)	FVOCI Mandatory		360	77	437	77
			560	**560**	**79**	**639**	**79**
From	measured at fair value	Designated at Fair Value (DFV)	612	–	–	–	–
To	Fair Value through Profit or Loss (FVPL)	FVPL Other		444	–	444	–
		FVPL Designated		168	–	168	–
			–	**612**	**–**	**612**	**–**
From	measured at fair value	Available for Sale (AfS)	12,475				
To	Fair Value through Profit or Loss (FVPL)	FVPL Other		102	–	102	–
			12,475	**102**	**–**	**102**	**–**
	Fair Value through Other Comprehensive Income (FVOCI)	FVOCI Mandatory		12,373	-6	12,367	-6
			–	**12,475**	**-6**	**12,469**	**-6**
From	measured at fair value	Held for Trading (HfT)/ (trading assets)	–				
To	Fair Value through Profit or Loss (FVPL)	FVPL Other[1)]		91	–	91	–
Total			**13,647**	**13,738**	**73**	**13,811**	**73**

[1)] In the case of these amounts, the abandonment of the intent to trade results in a transfer from the balance sheet item "Trading assets" to the balance sheet item "Financial investments".

RECONCILIATION OF MEASUREMENT CATEGORIES AND CARRYING AMOUNTS OF FINANCIAL INSTRUMENTS FROM IFRS 9 TO IAS 39

Non-current assets held for sale and disposal groups

(€ m)	01.01.2018		31.12.2017	
Categories of financial instruments in accordance with IFRS 7 in conjunction with IFRS 9	IFRS 9 measurement category	IFRS 9 carrying amount	IAS 39 measurement category	IAS 39 carrying amount
AC assets	Amortised cost (AC)	2	measured at amortised cost (LaR)	2
		2		2
FVPL Other	Fair Value through Profit or Loss (FVPL)	12	measured at amortised cost (LaR)	12
		12		12
Total		**26**		**26**

RECONCILIATION OF CARRYING AMOUNTS FROM IAS 39 TO IFRS 9 BASED ON THE CATEGORIES OF FINANCIAL INSTRUMENTS UNDER IFRS 7

Non-current assets held for sale and disposal groups

(€ m)			31.12.2017	01.01.2018			
			IAS 39 carrying amount	Reclassification	Remeasurement	IFRS 9 carrying amount	Equity effect
From	measured at amortised cost (AC)	Loans and receivables (LaR)	26				
To	Amortised cost (AC)	AC assets		2	–	2	–
	Fair Value through Profit or Loss (FVPL)	FVPL Other		12	–	12	–
	Shares in associates	No holding category		12	–	12	–
				26	–	26	–
Total			**26**	**26**	**–**	**26**	**–**

RECONCILIATION OF MEASUREMENT CATEGORIES AND CARRYING AMOUNTS OF FINANCIAL INSTRUMENTS FROM IFRS 9 TO IAS 39

Other assets

(€ m)		01.01.2018		31.12.2017
Categories of financial instruments in accordance with IFRS 7 in conjunction with IFRS 9	IFRS 9 measurement category	IFRS 9 carrying amount	IAS 39 measurement category	IAS 39 carrying amount
AC assets	Amortised cost (AC)	36	measured at amortised cost (LaR)	35
		36		**35**
FVPL Other	Fair Value through Profit or Loss (FVPL)	18	n.a.	18
Total		**54**		**53**

RECONCILIATION OF CARRYING AMOUNTS FROM IAS 39 TO IFRS 9 BASED ON THE CATEGORIES OF FINANCIAL INSTRUMENTS UNDER IFRS 7

Other assets

(€ m)			31.12.2017	01.01.2018			
			IAS 39 carrying amount	Reclassification	Remeasurement	IFRS 9 carrying amount	Equity effect
From	measured at amortised cost (AC)	Loans and receivables (LaR)	35	–	–	–	–
To	Amortised cost (AC)	AC assets		35	1	36	1
			35	35	1	36	1
From	n.a.	No IAS 39 category	18	–	–	–	–
To	Fair Value through profit or loss (FVPL)	FVPL Other		18	–	18	–
Total		**Total**	**53**	**53**	**1**	**54**	**1**

Reconciliation of balance sheet items in accordance with IFRS 7.42L

Financial liabilities

RECONCILIATION OF MEASUREMENT CATEGORIES AND CARRYING AMOUNTS OF FINANCIAL INSTRUMENTS FROM IFRS 9 TO IAS 9
Liabilities to banks

(€ m)	01.01.2018		31.12.2017	
Categories of financial instruments in accordance with IFRS 7 in conjunction with IFRS 9	IFRS 9 measurement category	IFRS 9 carrying amount	IAS 39 measurement category	IAS 39 carrying amount
AC liabilities	Amortised cost (AC)	8,153	measured at amortised cost (LIA)	8,153
		8,153		**8,153**
FVPL Designated	FVPL/FVOCI	118	measured at fair value (DFV)	118
		118		**118**
Total		**8,271**		**8,271**

RECONCILIATION OF CARRYING AMOUNTS FROM IAS 39 TO IFRS 9 BASED ON THE CATEGORIES OF FINANCIAL INSTRUMENTS UNDER IFRS 7
Liabilities to banks

(€ m)			31.12.2017			01.01.2018	
			IAS 39 carrying amount	Reclassification	Remeasurement	IFRS 9 carrying amount	Equity effect
From	measured at amortised cost (AC)	Other liabilities (LIA)	8,153				
To	Amortised cost (AC)	AC liabilities		8,153	–	8,153	–
			8,153	**8,153**	**–**	**8,153**	**–**
From	measured at fair value	Designated at Fair Value (DFV)	118				
To	FVPL/FVOCI	FVPL Designated		118	–	118	–
			118	**118**	**–**	**118**	**–**
Total			**8,271**	**8,271**	**–**	**8,271**	**–**

RECONCILIATION OF MEASUREMENT CATEGORIES AND CARRYING AMOUNTS OF FINANCIAL INSTRUMENTS FROM IFRS 9 TO IAS 39
Liabilities to customers

(€ m)	01.01.2018		31.12.2017	
Categories of financial instruments in accordance with IFRS 7 in conjunction with IFRS 9	IFRS 9 measurement category	IFRS 9 carrying amount	IAS 39 measurement category	IAS 39 carrying amount
AC liabilities	Amortised cost (AC)	35,386	measured at amortised cost (LIA)	35,386
		35,386		**35,386**
FVPL Designated	FVPL/FVOCI	819	measured at amortised cost (LIA)	819
		819		**819**
Total		**36,205**		**36,205**

RECONCILIATION OF CARRYING AMOUNTS FROM IAS 39 TO IFRS 9 BASED ON THE CATEGORIES OF FINANCIAL INSTRUMENTS UNDER IFRS 7
Liabilities to customers

(€ m)			31.12.2017		01.01.2018		
			IAS 39 carrying amount	Reclassification	Remeasurement	IFRS 9 carrying amount	Equity effect
From	measured at amortised cost (AC)	Other liabilities (LIA)	35,386				
To	Amortised cost (AC)	AC liabilities		35,386	–	35,386	–
			35,386	**35,386**	**–**	**35,386**	**–**
From	measured at fair value	Designated at Fair Value (DFV)	819				
To	FVPL/FVOCI	FVPL Designated		819	–	819	–
			819	**819**	**–**	**819**	**–**
Total			**36,205**	**36,205**	**–**	**36,205**	**–**

RECONCILIATION OF MEASUREMENT CATEGORIES AND CARRYING AMOUNTS OF FINANCIAL INSTRUMENTS FROM IFRS 9 TO IAS 39
Securitised liabilities

(€ m)	01.01.2018		31.12.2017	
Categories of financial instruments in accordance with IFRS 7 in conjunction with IFRS 9	IFRS 9 measurement category	IFRS 9 carrying amount	IAS 39 measurement category	IAS 39 carrying amount
AC liabilities	Amortised cost (AC)	10,817	measured at amortised cost (LIA)	10,817
		10,817		**10,817**
FVPL Designated	FVPL/FVOCI	1,627	measured at fair value (DFV)	1,627
		1,627		**1,627**
Total		**12,444**		**12,444**

RECONCILIATION OF CARRYING AMOUNTS FROM IAS 39 TO IFRS 9 BASED ON THE CATEGORIES OF FINANCIAL INSTRUMENTS UNDER IFRS 7
Securitised liabilities

(€ m)			31.12.2017		01.01.2018		
			IAS 39 carrying amount	Reclassification	Remeasurement	IFRS 9 carrying amount	Equity effect
From	measured at amortised cost (AC)	Other liabilities (LIA)	10,817				
To	Amortised cost (AC)	AC liabilities		10,817	–	10,817	–
			10,817	**10,817**	**–**	**10,817**	**–**
From	measured at fair value	Designated at Fair Value (DFV)	1,627				
To	FVPL/FVOCI	FVPL Designated		1,627	–	1,627	–
			1,627	**1,627**	**–**	**1,627**	**–**
Total			**12,444**	**12,444**	**–**	**12,444**	**–**

RECONCILIATION OF MEASUREMENT CATEGORIES AND CARRYING AMOUNTS OF FINANCIAL INSTRUMENTS FROM IFRS 9 TO IAS 39

Negative fair value of hedging derivatives

(€ m)	01.01.2018		31.12.2017	
Categories of financial instruments in accordance with IFRS 7 in conjunction with IFRS 9	IFRS 9 measurement category	IFRS 9 carrying amount	IAS 39 measurement category	IAS 39 carrying amount
n.a.	Fair Value through Profit or Loss (FVPL)	163	measured at fair value	163

RECONCILIATION OF CARRYING AMOUNTS FROM IAS 39 TO IFRS 9 BASED ON THE CATEGORIES OF FINANCIAL INSTRUMENTS UNDER IFRS 7

Negative fair value of hedging derivatives

(€ m)			31.12.2017	01.01.2018			
			IAS 39 carrying amount	Reclassification	Remeasurement	IFRS 9 carrying amount	Equity effect
From	measured at fair value	n.a.	163				
To	Fair Value through Profit or Loss (FVPL)	n.a.		163	–	163	–

RECONCILIATION OF MEASUREMENT CATEGORIES AND CARRYING AMOUNTS OF FINANCIAL INSTRUMENTS FROM IFRS 9 TO IAS 39

Negative adjustment item from portfolio fair value hedges

(€ m)	01.01.2018		31.12.2017	
Categories of financial instruments in accordance with IFRS 7 in conjunction with IFRS 9	IFRS 9 measurement category	IFRS 9 carrying amount	IAS 39 measurement category	IAS 39 carrying amount
No category	n.a.	553	n.a.	553

RECONCILIATION OF CARRYING AMOUNTS FROM IAS 39 TO IFRS 9 BASED ON THE CATEGORIES OF FINANCIAL INSTRUMENTS UNDER IFRS 7

Negative adjustment item from portfolio fair value hedges

(€ m)			31.12.2017	01.01.2018			
			IAS 39 carrying amount	Reclassification	Remeasurement	IFRS 9 carrying amount	Equity effect
From	n.a.	No IAS 39 category	553				
To	n.a.	No category		553	–	553	–

RECONCILIATION OF MEASUREMENT CATEGORIES AND CARRYING AMOUNTS OF FINANCIAL INSTRUMENTS FROM IFRS 9 TO IAS 39

Trading liabilities

(€ m)	01.01.2018		31.12.2017	
Categories of financial instruments in accordance with IFRS 7 in conjunction with IFRS 9	IFRS 9 measurement category	IFRS 9 carrying amount	IAS 39 measurement category	IAS 39 carrying amount
FVPL Trading	Fair Value through Profit or Loss (FVPL)	3,875	measured at fair value (HfT)	3,875
Total		**3,875**		**3,875**

RECONCILIATION OF CARRYING AMOUNTS FROM IAS 39 TO IFRS 9 BASED ON THE CATEGORIES OF FINANCIAL INSTRUMENTS UNDER IFRS 7

Trading liabilities

(€ m)			31.12.2017	01.01.2018			
			IAS 39 carrying amount	Reclassification	Remeasurement	IFRS 9 carrying amount	Equity effect
From	measured at fair value	Held for Trading (HfT)	3,875				
To	Fair Value through Profit or Loss (FVPL)	FVPL Trading		3875	–	3875	–
Total			**3,875**	**3,875**	**–**	**3,875**	**–**

RECONCILIATION OF MEASUREMENT CATEGORIES AND CARRYING AMOUNTS OF FINANCIAL INSTRUMENTS FROM IFRS 9 TO IAS 39

Liabilities relating to disposal groups

(€ m)	01.01.2018		31.12.2017	
Categories of financial instruments in accordance with IFRS 7 in conjunction with IFRS 9	IFRS 9 measurement category	IFRS 9 carrying amount	IAS 39 measurement category	IAS 39 carrying amount
AC liabilities	Amortised cost (AC)	2	measured at amortised cost (LIA)	2
		2		**2**
Total		**2**		**2**

RECONCILIATION OF CARRYING AMOUNTS FROM IAS 39 TO IFRS 9 BASED ON THE CATEGORIES OF FINANCIAL INSTRUMENTS UNDER IFRS 7

Liabilities relating to disposal groups

(€ m)			31.12.2017	01.01.2018			
			IAS 39 carrying amount	Reclassification	Remeasurement	IFRS 9 carrying amount	Equity effect
From	measured at amortised cost (AC)	Other liabilities (LIA)	2				
To	Amortised cost (AC)	AC liabilities		2	–	2	–
				2	**–**	**2**	**–**
Total			**2**	**2**	**–**	**2**	**–**

RECONCILIATION OF MEASUREMENT CATEGORIES AND CARRYING AMOUNTS OF FINANCIAL INSTRUMENTS FROM IFRS 9 TO IAS 39
Other liabilities

(€ m)	01.01.2018		31.12.2017	
Categories of financial instruments in accordance with IFRS 7 in conjunction with IFRS 9	IFRS 9 measurement category	IFRS 9 carrying amount	IAS 39 measurement category	IAS 39 carrying amount
AC liabilities	Amortised cost (AC)	638	measured at amortised cost (LIA)	638
		638		**638**
Total		**638**		**638**

RECONCILIATION OF CARRYING AMOUNTS FROM IAS 39 TO IFRS 9 BASED ON THE CATEGORIES OF FINANCIAL INSTRUMENTS UNDER IFRS 7
Other liabilities

(€ m)			31.12.2017	01.01.2018			
			IAS 39 carrying amount	Reclassification	Remeasurement	IFRS 9 carrying amount	Equity effect
From	measured at amortised cost (AC)	Other liabilities (LIA)	638				
To	Amortised cost (AC)	AC liabilities		638	–	638	–
				638	**–**	**638**	**–**
Total			**638**	**638**	**–**	**638**	**–**

RECONCILIATION OF MEASUREMENT CATEGORIES AND CARRYING AMOUNTS OF FINANCIAL INSTRUMENTS FROM IFRS 9 TO IAS 39
Subordinated capital

(€ m)	01.01.2018		31.12.2017	
Categories of financial instruments in accordance with IFRS 7 in conjunction with IFRS 9	IFRS 9 measurement category	IFRS 9 carrying amount	IAS 39 measurement category	IAS 39 carrying amount
AC liabilities	Amortised cost (AC)	2,252	measured at amortised cost (LIA)	2,252
		2,252		**2,252**
Total		**2,252**		**2,252**

RECONCILIATION OF CARRYING AMOUNTS FROM IAS 39 TO IFRS 9 BASED ON THE CATEGORIES OF FINANCIAL INSTRUMENTS UNDER IFRS 7
Subordinated capital

(€ m)			31.12.2017	01.01.2018			
			IAS 39 carrying amount	Reclassification	Remeasurement	IFRS 9 carrying amount	Equity effect
From	measured at amortised cost (AC)	Other liabilities (LIA)	2,252				
To	Amortised cost (AC)	AC liabilities		2,252	–	2,252	–
				2,252	**–**	**2,252**	**–**
Total			**2,252**	**2,252**	**–**	**2,252**	**–**

EXPLANATORY INFORMATION

The reconciliation statement shows all changes in the carrying amount of financial instruments in the consolidated statement of financial position that are attributable to the initial application of IFRS 9 as at 1 January 2018. This includes explanatory information on significant changes in equity, as shown below.

The reconciliation set out above of the carrying amounts of financial instruments under IAS 39 to the carrying amounts of financial instruments under IFRS 9 for assets results in an "equity effect" in an amount of € +112 million. In addition, IFRS 9 results in a negative equity effect on the "provisions" liabilities item in an amount of € –3 million due to the increased loan loss provisions set up with regard to off-balance sheet transactions. All in all, this results in a total equity effect resulting from the initial application of IFRS 9 in an amount of € +109 million (before taxes).

The total equity effect before taxes from the reconciliation of the carrying amounts of financial instruments under IAS 39 to the carrying amounts of financial instruments under IFRS 9 in the amount of € +109 million comprises € +417 million from the revaluation reserve and € -308 million from retained earnings. This gives rise to the main equity effects of

- € –3,485 million from the balance sheet item "Loans and advances to customers"
- € +3,484 million from the balance sheet item "Compensation item for financial instruments categorised as FVPL under the second loss guarantee"
- € +73 million from the balance sheet item "Financial investments"
- € +32 million from the balance sheet item "Loan loss provisions in the lending business"
- € +7 million from the balance sheet item "Loans and advances to banks"
- € –3 million from the balance sheet item "Provisions" and
- € +1 million from the balance sheet item "Other assets".

Under the balance sheet item "Loans and advances to customers", the changes in carrying amount were recognised as follows: € +351 million in the revaluation reserve and € -3,836 million in retained earnings. Under the balance sheet item "Financial investments", the changes in carrying amount were recognised as follows:€ +60 million in the revaluation reserve and € +13 million in retained earnings. The changes in carrying amount in the balance sheet item "Loans and advances to banks" of € +7 million were recognised in full in the revaluation reserve. The other significant equity effects of € +3,514 million were recognised in retained earnings.

The main drivers of the overall effect on equity in an amount of € + 109 million (before taxes) are the increase in general loan loss provisions as a result of the new loan loss provisions model (level 1 and 2 in the new loan loss provisions model) and effects from the fair value measurement of certain loans and securities resulting from the new classification provisions.

The increase in general loan loss provisions is attributable to the increase in loan loss provisions on the lifetime expected loss (level 2)/the full 12-month expected loss (level 1). The general loan loss provisions have increased by approximately € 146 million, resulting in a negative equity effect in an amount of € -146 million (before taxes) which is deducted from retained earnings.

With regard to the above-mentioned effects from the fair value measurement of certain loans and securities, reclassifications of financial assets from the measurement category amortised cost (AC or LaR) to the category "Fair Value through Other Comprehensive Income" (FVOCI) are one of the main drivers. These relate to promissory note loans and securities based on the "Hold and sell" business model under IFRS 9. This reclassification results in a positive fair value effect and a corresponding increase in equity in the amount of approximately € 165 million before taxes, which is added to the revaluation reserve. Another main driver of the above-mentioned effects from fair value measurement relates to reclassifications of financial assets from the amortised cost (AC/LaR) measurement category to the Fair value through Profit & Loss (FVPL) category. These recategorisations also result in a positive fair value effect at the time of initial application and a corresponding increase in equity in the amount of € 63 million before taxes (net after the reversal of loan loss provisions), which is added to retained earnings. The effect here relates primarily to a portfolio in the lending business of the Non-Core Bank that is allocated to the "Other" business model within the meaning of IFRS 9 and whose sale was agreed on 28 February 2018.

Other effects on transactions that are assigned to the amortised cost (LaR/AC) category under both IAS 39 and IFRS 9 (for example, carrying amount effects due to the modification provisions), lead to a positive equity effect in an amount of approximately € + 27 million (before taxes), which is added to retained earnings.

There are also transfers within equity between retained earnings and revaluation reserves that have no equity effect in net terms. First, there is a reclassification that is deducted from retained earnings and added to the revaluation reserve in the amount of € 291 million (before taxes). This is due to reclassifications from the FVPL measurement category (DFV) to FVOCI due to the revocation of the fair value option for certain financial assets. Second, there is a reclassification that is added to retained earnings and is deducted from the revaluation reserve in the amount of € 39 million (before taxes). This is due, first of all, to reclassifications between the measurement categories FVOCI (AfS) and FVPL in an amount of € 50 million, which was added to retained earnings and deducted from the revaluation reserve. Second, the reclassification amount also includes the gains and losses accrued under IAS 39 in the revaluation reserve in the amount of € 11 million, which result from a historical reallocation of financial instruments in the balance sheet item "Financial investments" from the IAS 39 category AfS to the IAS 39 category LaR. These were reclassified within the context of the initial application of IFRS 9, being added to the revaluation reserve and deducted from retained earnings.

Changes in valuation differences result in an overall reduction in deferred tax assets by € 30 million. € 141 million of this amount is deducted from the revaluation reserve and € 111 million is added the revaluation reserve.

In summary, this results in a total equity effect resulting from the initial application of IFRS 9 in an amount of € +79 million after taxes.

Application of accounting methods IFRS 9 – Financial instruments

General information

IFRS 9 Financial instruments, which was published in July 2014, replaces the existing accounting policies set out in IAS 39 Financial Instruments: Recognition and Measurement. IFRS 9 contains revised guidelines on the classification and measurement of financial instruments, a new model for expected loan defaults for calculating the impairment of financial assets, as well as the new general accounting rules for hedge accounting. IFRS 9 also adopts the guidelines on the recognition and derecognition of financial instruments set out in IAS 39.

For those financial liabilities that Hamburg Commercial Bank has designated for measurement at fair value through profit or loss, the option of early application of the measurement of the credit rating-induced part of the valuation result via Other comprehensive income (OCI) in equity has been applied. As this option was exercised as at 1 January 2017, this is the first time of initial application of IFRS 9. The time of the full initial application of IFRS 9 as at 1 January 2018 therefore represents the second time of initial application.

The introduction of IFRS 9 involved amendments to IFRS 7 Financial Instruments: Disclosures. Pursuant to IFRS 7.44Z, the resulting changes in the disclosure requirements are not to be applied to comparative periods prior to the adoption of IFRS 9. In accordance with this provision, the financial statements of Hamburg Commercial Bank do not include any disclosures for the comparative period in such cases, as disclosure is required for the first time with application of IFRS 9.

Transitional provisions

IFRS 9.7.2.2 et seq. include a number of exceptions to retrospective application upon transition to the new accounting regulations. In such cases, the assessment is based on the facts and circumstances prevailing at the time of initial application. This means that, as far as the definition/classification of Hamburg Commercial Bank's business models is concerned, the business activity and corresponding assessment of the portfolios of financial instruments as at 1 January 2018 are decisive (see also the section entitled "Accounting and measurement principles"). In addition, the decision on the use of the fair value option for financial assets and liabilities can be exercised again upon transition to the new standard. Within this context, Hamburg Commercial Bank has reviewed the requirements relating to the designation of financial instruments using the fair value option based on the circumstances prevailing at the time of initial application and has made corresponding designations.

I. Classification and measurement

With regard to portfolios of financial assets with a carrying amount of € 1,052 million, for which the fair value option through profit or loss was applied under IAS 39 to avoid an accounting mismatch, there was no longer any wish, with regard to IFRS 9.7.2.9 (b), to apply a new designation under IFRS 9, despite the requirements being met (voluntary revocation of the fair value option). These assets were assigned to the "Hold & sell" business model, meaning that they are measured at fair value directly in equity ("FVOCI" category). At the time of initial application as at 1 January 2018, this results in transfers within equity from retained earnings to the revaluation reserve in the amount of € 291 million.

II. Impairment

The retroactive reliable determination of the default risk, in accordance with IFRS 9.7.2.17, at the time of commitment for certain transactions was not possible for all transactions at the time of the first full application of IFRS 9. The affected portfolios are various sub-portfolios with a carrying amount of € 1,355 million for on-balance sheet transactions and a nominal amount of € 1,699 million for off-balance sheet transactions as at 1 January 2018. The lifetime expected credit loss set up in this regard in accordance with IFRS 9.7.2.20 (LECL) amounts to a total of € 45 million as at 1 January 2018. € 15 million of this amount is attributable to level 2 and € 30 million to level 3.

Group Explanatory Notes

General information

1. Accounting principles

Hamburg Commercial Bank AG, which has its registered offices in Hamburg and Kiel, prepares Group financial statements as the ultimate parent company.

Hamburg Commercial Bank AG has issued debt instruments as defined in Section 2 (1) sentence 1 of the German Securities Trading Act (WpHG) on an organised market as defined in Section 2 (11) WpHG and is thus obliged, as a publicly traded company as defined in Regulation (EC) 1606/2002 (IAS Regulation) of the European Parliament and of the Council of 19 July 2002 in conjunction with Section 315e (1) of the German Commercial Code (HGB) to draw up its Group financial statements in accordance with the International Financial Reporting Standards. International accounting standards, hereinafter IFRS or standards, refer to the International Accounting Standards (IAS) and International Financial Reporting Standards (IFRS) and the associated interpretations by the Standing Interpretations Committee (SIC) and the International Financial Reporting Interpretations Committee (IFRIC), published by the International Accounting Standards Board (IASB) and adopted under the IAS Regulation as part of the EU endorsement.

The supplementary provisions of Section 315e HGB are taken into account and are shown individually in Notes 63 and 66.

The Group financial statements are prepared in accordance with IFRS as published by the IASB and adopted as European law by the European Union (EU).

The Group financial statements of Hamburg Commercial Bank are prepared in line with IFRS 10 according to uniform Group-wide measurement and accounting policies. In accordance with IAS 1, the Group financial statements consist of the statement of income, the statement of comprehensive income, the statement of financial position, the statement of changes in equity, the cash flow statement and the explanatory notes, including segment reporting. In addition to the Group financial statements a Group management report in accordance with Section 315 HGB was prepared.

Group income and expenses are accrued on a pro rata temporis basis. They are recognised and disclosed in the period to which they must be assigned economically. Accounting for assets, liabilities, income and expenses takes place on a consistent basis. Deviations are only made in justified exceptional cases which are explained separately in the Notes on the relevant items in the Hamburg Commercial Bank Group financial statements.

Unless explicitly stated otherwise, all amounts are in millions of euros (€ m).

The reporting year corresponds to the 2018 calendar year.

IFRS 7.31 et seqq. contains rules on presenting risks arising from financial instruments. In this regard, IFRS 7.B6 allows for the possibility of disclosing risk in a suitable medium separate from the Group financial statements. Availing itself of this option, Hamburg Commercial Bank has published disclosures about financial instruments as permitted by IFRS 7.31 et seqq. predominantly in the Group risk report within the Group management report. Specifically, this relates to the overall qualitative and quantitative risk information disclosed under IFRS 7.33 et seqq. and the total market risk reporting under IFRS 7.40–42 as well as the description of how liquidity risk is managed as required by IFRS 7.39 (c).

In addition, as part of the supplementary German commercial regulations the Group observed the following German Accounting Standards (GAS) in preparing these Group financial statements and this Group management report:

- GAS 20 Group Management Report
- GAS 17 Reporting on the Remuneration of Members of Governing Bodies.

Apart from the new standards and interpretations stated below, which may have a significant influence on the Group financial statements a number of additional standards and interpretations were adopted which , however, are expected not to have any influence on the Group financial statements.

During the current financial year, the following accounting standards need to be applied for the first time as a matter of principle:

IFRS 9 – Financial Instruments

IFRS 9 replaces the existing guidelines contained in IAS 39 on the recognition and measurement of financial instruments with regard to classification and measurement, impairments and general hedge accounting.

IFRS 9 is be applied for the first time, as a mandatory requirement, in financial years beginning on or after 1 January 2018. Hamburg Commercial Bank has been applying IFRS 9 in full since 1 January 2018.

The changes resulting from IFRS 9 are generally to be applied retrospectively - with the exception of the new hedge accounting requirements. Hamburg Commercial Bank has, however, made use of the option of not adjusting the prior-period figures. In addition, and by way of derogation from the principle of retrospective application, the following classification requirements were to be assessed based on the circumstances at the time of initial application on 1 January 2018:

- the determination of the business model in which the financial asset is held,
- the designation/revocation of the fair value designation of financial assets and liabilities.

The new regulations set out in IFRS 9 resulted in valuation effects to be recognised in equity in the opening balance sheet in retained earnings/the revaluation reserve at the time of initial application. These effects resulting from the initial application of IFRS 9 as at 1 January 2018, the date of first-time application, are explained in the section "Explanatory information" below the reconciliation tables.

The effects of the initial application of IFRS 9 have also had an impact on regulatory figures. Within this context, it is important to remember that the regulatory capital ratios have no longer been shown as a securitisation structure since March 2018, taking into account the regulatory relief effect of the second loss guarantee. As of March 2018, presentation is comparable with the pro forma CET1 capital ratio reported as an additional ratio in the past. The impact of IFRS 9 on the pro forma CET1 capital ratio at the time of first-time application was minimal.

In connection with the introduction of IFRS 9, the new CRR Article 473a came into force with effect from 1 January 2018 via EU Regulation 2017/2395 of 12 December 2017. This Article introduces the option allowing certain initial application effects to be distributed over a transitional period of five years. Hamburg Commercial Bank AG has opted not to apply the transitional provisions pursuant to Article 473a) CRR.

The following sections compare the main changes resulting from the application of IFRS 9 compared with IAS 39. In addition, information is provided on significant specific effects for the Bank and the use of options.

A) CLASSIFICATION AND MEASUREMENT

IFRS 9 introduces a new categorisation model for financial assets. They are classified into measurement categories on the basis of the business model (portfolio level) or the contractual terms or cash flow characteristics (instrument level). Further details on the new classification and measurement rules can be found in Note 7 Accounting policies. The reconciliation of the carrying amounts in the closing balance sheet in accordance with IAS 39 to the carrying amounts in the opening balance sheet in accordance with IFRS 9 is presented in the section entitled "Balance sheet item reconciliation from IAS 39 to IFRS 9".

In derogation from the principles described therein, the following options apply:

- Upon the initial recognition of an equity instrument that falls under the scope of IFRS 9 and is not held for trading, there is the option of measuring the instrument at FVOCI (FVOCI option).
- Financial assets can be designated for measurement at FVPL to eliminate or significantly reduce a measurement or recognition inconsistency (accounting mismatch) (FVPL option).

Further information on the new classification and measurement provisions can be found in the chapter entitled "Application of accounting methods IFRS 9 - Financial instruments".

The new IFRS 9 categorisation model has resulted in different valuation categories compared with IAS 39 for certain portfolios/individual transactions involving financial assets within Hamburg Commercial Bank's portfolio. This has expanded the scope of instruments to be valued at FVPL/FVOCI.

The business model conditions resulted in the following material effects at the time of initial application:

Within the securities portfolio (capital markets business incl. promissory note loans), a large part of the portfolio that is not held for trading and was allocated to the LaR category under IAS 39 (AC valuation category) was reclassified to the FVOCI category under IFRS 9, as the business model is a "Hold and sell" business model.

The "Hold to collect" business model generally applies to the loan portfolio (lending business). No receivables sales are planned as a general rule.

This allocation results in measurement at AC in the same way as under IAS 39 – if the financial instrument also meets the contractual cash flow characteristics criterion.

By way of derogation from the principle of the "Hold to collect" classification of the loan portfolio (lending business), syndication shares from new business syndication are allocated to a separate portfolio that is to be measured at FVPL.

The contractual cash flow characteristics criterion results in the following material effects:

The vast majority of the securities portfolio (capital market business incl. promissory note loans) meets the criterion relating to the cash flow condition. There is only an insignificant amount of structured holdings that are not allocated to the "Other" business model, do not meet the contractual cash flow characteristics criterion and are reclassified from the IAS 39 category LaR (AC measurement category) to the IFRS 9 category FVPL.

As far as the loan portfolio (lending business) is concerned, the overwhelming majority of the instruments are to be classed as basic lending arrangements within the meaning of IFRS 9, i.e. the contractual terms of these transactions satisfy the cash flow condition. In addition, there are loans that breach the contractual cash flow characteristics criterion. The breach of the contractual cash flow characteristics criterion is due to certain detrimental side agreements (e.g. profit participation agreed in the loan agreement) or non-recourse financing. Non-recourse financing involves a substantial property/project risk on the commitment date, i.e. a primary investment risk (asset risk) that constitutes a business risk, meaning that the payments depend, in economic terms, to a considerable degree on the property/project being financed. By way of example, the non-recourse financing of a single-property company is deemed to carry a substantial property risk if, at the time of initial recognition, the loan amount is very high in relation to the value of the property (high loan-to-value ratio), the property company only has limited capital resources available for potential loss absorption and, in addition, there are no mitigating factors such as recoverable third-party collateral in favour of the lender.

For certain financial assets which are designated for measurement at FVPL under IAS 39 to avoid an accounting mismatch, the FVPL option under IFRS 9 was not exercised despite the criteria being met (revocation of the FVPL option). These assets are allocated to the "Hold and sell" business model under IFRS 9, meaning that they are categorised as FVOCI. This resulted in a one-time reclassification within equity at the time of the first-time application of IFRS 9. This affected a portfolio with a carrying amount (fair value) of € 1,052 million as at 1 January 2018. The effective interest rate for the reclassified transactions ranged from 3.54 % to 4.00 %. The effective interest rate was calculated on the basis of the retrospectively calculated gross carrying amount, i.e. the gross carrying amount was not adjusted to reflect the fair value at the time of initial application. Interest income for the period from January to December 2018, calculated using the effective interest method, amounted to € 28 million. This amount includes the adjustment items from the amortisation of accrued hedge adjustments in the period, which are attributable to the fact that the transactions were designated as micro fair value hedges from 1 January 2018.

Hamburg Commercial Bank has not made use of the option relating to the FVOCI categorisation of equity instruments (FVOCI option) within the scope of IFRS 9.

The provisions governing the classification and measurement of financial liabilities remain largely unchanged compared with IAS 39. There are, however, changes to disclosures for financial liabilities designated at fair value. Fair value changes arising from own credit risk are no longer to be disclosed through profit or loss for these liabilities as a general rule, but directly in equity in other comprehensive income (OCI).

Under IFRS 9, the separation rules for embedded derivatives will only apply for host contracts that are financial liabilities or not of a financial nature.

B) IMPAIRMENT

The introduction of IFRS 9 will replaced the existing model used to calculate loan loss provisions/impairments under IAS 39, which is based on incurred losses, with a model based on the expected credit losses. The scope of the new model consistently includes all financial instruments that are recognised at amortised cost or at fair value through other comprehensive income, irrevocable loan commitments and financial guarantees that are not recognised at fair value through profit or loss, leasing receivables and contract assets.

Please refer to Note 7 Accounting policies with regard to the calculation of loan loss provisions in accordance with the new impairment model.

Further information on the new impairment provisions can be found in the chapter entitled "Application of accounting methods IFRS 9 - Financial instruments".

Compared to the existing model under IAS 39, the new impairment model results in loan loss provisions being recognised earlier and in a higher amount.

As well as the new provisions governing impairment, IFRS 9 also contains new requirements governing how contractual modifications are taken into account. In cases involving substantial modifications resulting in the derecognition of the financial instrument in the balance sheet, the provisions continue to apply unchanged as against the IAS 39 provisions. In cases involving modifications not classed as substantial that do not result in the derecognition of the asset in the balance sheet, the gross carrying amount of the asset is adjusted. The new gross carrying amount is given by the present value of the modified cash flows using the financial instrument's original effective interest rate for discounting. The adjustment of the gross carrying amount results in a modification gain or loss that has to be recognised through profit or loss. Non-substantial modifications in the lending business result in receivables correction amounts, i.e. a reduction/increase in the gross carrying amount based on the effective interest rate present value of the cash flows following the contractual modification. The receivables corrections result, in loan loss provision level 3, in a reduction in the loan loss provisions set up (negative receivables correction) or in an increase in the loan loss provisions set up (positive receivables correction). In loan loss provision levels 1 and 2, the impact on loan loss provisions is relatively minor.

C) HEDGE ACCOUNTING

IFRS 9 includes various changes to hedge accounting rules compared to IAS 39. However, new rules for the recognition of (dynamic) portfolio or macro hedges respectively are not included in IFRS 9. As a result, options apply allowing for the continued application of existing IAS 39 provisions. Hamburg

Commercial Bank has made use of the option provided for in IFRS 9.6.1.3 to apply the hedge accounting provisions set out in IAS 39 to portfolio fair value hedges on interest rate change risks.

IFRS 15 – Revenue from Contracts with Customers and Clarifications to IFRS 15

IFRS 15 Revenue from Contracts with Customers sets out a comprehensive framework for determining whether, at what level and when revenue is recognised. The standard is to be applied for the first time, as a mandatory requirement, in financial years beginning on or after 1 January 2018. It replaces the existing guidelines on the recognition of revenue under IAS 11 Construction Contracts and IAS 18 Revenue and the related interpretations. The amendments to IFRS 15 do not have any effect on the recognition of income recognised in connection with financial instruments pursuant to IFRS 9 or leases in accordance with IFRS 16.

Revenue recognition in accordance with IFRS 15 is to match the delivery of goods and services in terms of timing, scope and allocation. The application of a uniform principle-based five-stage model is designated for the assessment of revenue recognition.

At Hamburg Commercial Bank, commission and other income is recognised on an accrual basis at a particular point in time or over a period of time, depending on the performance of the service: commission income that is to be collected at a specific point in time is recognised in the statement of income at the time the service is rendered. This mainly relates to commission from the lending business. Where services are provided over several periods, income from service transactions is recognised in the statement of income on the basis of the extent to which the performance obligation has been fulfilled on the balance sheet date in question.

The application of IFRS 15 does not result in any material changes in the measurement and presentation of such income, either as a result of recognition in the period to which it relates or as a result of the determination of the scope and allocation of the income.

At Hamburg Commercial Bank, IFRS 15 was introduced using the modified retrospective method, according to which the cumulative effects resulting from the first-time application of the standard are recognised as an adjustment to the opening balance sheet value for retained earnings. The first-time application did not result in any cumulative adjustments to retained earnings.

Amendments to IAS 40 – Transfers of Investment Property

The amendment to IAS 40 serves to clarify the cases in which properties start/stop being classified as an "investment property" if they are under construction or development. The previous exhaustive list in IAS 40.57 did not set out clear provisions on the classification of properties that had not yet been completed. The list is now explicitly designated as non-exhaustive, meaning that properties that have not yet been completed now also fall under the scope of the provisions.

IFRIC 22 Foreign Currency Transactions and Advance Consideration

IFRIC 22 addresses a question relating to the application of IAS 21 The Effects of Changes in Foreign Exchange Rates. The Interpretation clarifies the time at which the exchange rate is to be calculated for the translation of foreign currency transactions that include the receipt or payment of advance consideration. According to the Standard, the decisive date for the purpose of determining the exchange rate for the underlying asset, income or expense, is the date of initial recognition of the asset or liability resulting from the advance consideration.

Improvements to IFRS 2014–2016

IAS 28 clarifies that the election to measure an investment in an associate or a joint venture that is held by an entity that is a venture capital organisation, or other qualifying entity, can be exercised differently for each investment.

The short-term exemptions in IFRS 1 Appendix E (IFRS 1.E3 – E7) were also deleted for entities applying the IFRS for the first time.

Hamburg Commercial Bank is not planning the early application of the following new or amended Standards or Interpretations for which application is only mandatory in later financial years. To the extent not indicated otherwise, all effects on the financial statements of Hamburg Commercial Bank are currently under review.

Already endorsed by the EU:
IFRS 16 Leases
IFRS 16 provides a single model regarding how lessees are to recognise leases in their balance sheets. A lessee recognises a right-of-use asset, representing its right to use the underlying asset, and a lease liability, representing its obligation to make lease payments. Exceptions apply to short-term leases and leases for low-value assets. Accounting at the level of the lessor is comparable to the current standard - i.e. the lessor continues to classify leases as finance or operating leases.

IFRS 16 replaces the existing guidelines on leases, including IAS 17 Leases, IFRIC 4 Determining Whether an Arrangement Contains a Lease, SIC-15 Operating Leases – Incentives and SIC-27 Evaluating the Substance of Transactions in the Legal Form of a Lease.

IFRS 16 needs to be applied for the first time in the first reporting period in a financial year starting on or after 1 January 2019. Early application is permitted for companies that apply IFRS 15 Revenue from Contracts with Customers at the time of the initial application of IFRS 16 or before.

Hamburg Commercial Bank is currently in the final phase of an implementation project regarding the introduction of the standard and has largely identified and quantified the accounting effects. Overall, the impact of the application of the standard on Hamburg Commercial Bank’s earnings, net assets and financial position are considered to be insignificant.

Taking materiality aspects into account and making use of the simplified provisions for low-value and short-term leases (IFRS 16.5), the scope of application of IFRS 16 at Hamburg Commercial Bank, as the lessee, is limited to the properties (Group business premises) rented under IAS 17 as part of operating leases to date. Hamburg Commercial Bank expects the recognition of the rights of use and lease liabilities resulting from these property leases to extend the balance sheet by approximately € 10 million as at 1 January 2019. Shifts within the statement of income from current administrative expenses to net interest income (interest expenses for other liabilities) are also considered to be immaterial and are predicted to amount to less than € 1 million p.a. The reduction in administrative expenses and increase in interest expense are due to the splitting of leasing expenses into an interest and a depreciation component.

Calculating the amount of a lease liability and the right of use associated with a lease implies estimates regarding the lease term, particularly against the backdrop of possible termination or renewal options. With regard to the property leases that are relevant, for the purposes of IFRS 16, at Hamburg Commercial Bank, an extension of the term by exercising a contractual extension option (or a shortening of the term by exercising a termination option) cannot be regarded as sufficiently certain without a specific Management Board resolution, which is why the calculation is based exclusively on the contractually agreed term. In order to calculate the net present value of the lease liability, Hamburg Commercial Bank applies a uniform incremental borrowing rate that is commensurate with the term of the lease in the absence of sufficient information on the inherent interest rate of each lease.

Transactions in which Hamburg Commercial Bank acts as the lessor do not result in any accounting effects arising from the introduction of IFRS 16.

Upon the introduction of IFRS 16, Hamburg Commercial Bank will not reassess the existence of a lease as a general rule, making use of the transitional provisions set out in IFRS 16.C3. This excludes what are known as multi-component contracts, for which the assessment criterion has changed significantly in connection with the transition from IAS 17 to IFRS 16 (with regard to the accounting effect). Since this threshold for accounting effects will shift towards the assessment as to whether the matter in question relates to a service or lease relationship or a service or lease component, the multi-component contracts in the Bank’s portfolio were reassessed as part of a portfolio analysis. Hamburg Commercial Bank applies the modified retrospective method, pursuant to IFRS 16.C5 (b) ,to the leases identified, according to which the cumulative effects resulting from the first-time application of the standard are recognised as an adjustment to the opening balance sheet value for retained earnings. In accordance with this method, the comparative figures for previous periods have not been adjusted. The first-time application of the standard as at 1 January 2019 does not have any impact on retained earnings.

Amendments to IFRS 9 Prepayment Features with Negative Compensation
The adjustments relate to a minor adjustment to the assessment criteria relevant to the classification of financial assets. Financial assets with a negative prepayment penalty (”prepayment feature with negative compensation”) can be recognised, subject to certain requirements, at amortised cost or at fair value through other comprehensive income, instead of at fair value through profit or loss.

The amendments need to be applied for the first time in the first reporting period in a financial year starting on or after 1 January 2019.

Amendments to IAS 28 Long-term Interests in Associates and Joint Ventures

The amendments clarify that IFRS 9 is to apply to long-term interests in associates and joint ventures to which the equity method is not applied.

The amendments need to be applied for the first time in the first reporting period in a financial year starting on or after 1 January 2019.

IFRIC 23 Uncertainty over Income Tax Treatments

The tax treatment of certain scenarios and transactions may depend on future recognition by the tax authorities or fiscal courts. IAS 12 Income Taxes sets out provisions governing how current and deferred taxes are to be recognised. IFRIC 23 supplements the provisions set out in IAS 12 regarding how to deal with uncertainty surrounding the income tax treatment of scenarios and transactions.

The interpretation needs to be applied for the first time in the first reporting period in a financial year starting on or after 1 January 2019. Early application is permitted.

The changes do not materially affect the Group financial statements of Hamburg Commercial Bank.

EU endorsement still pending:
Amendments to IAS 1 and IAS 8 Definition of Material

The amendments create a uniform and more precise definition in IFRS of the materiality of the information provided in financial statements, and supplement it to include corresponding examples.

Subject to the still-pending adoption into EU law, the amendments need to be applied for the first time in the first reporting period in a financial year starting on or after 1 January 2019. Early application is permitted.

Amendment to IFRS 3 Business Combinations

The amendments to IFRS 3 relate to the definition of a business. Under IFRS 3, acquisitions are only classified as business combinations pursuant to IFRS 3 (Business Combinations) if the conditions for definition as a business are met. If there is no business involved, the transaction is treated as an asset purchase for accounting purposes. The accounting applied to the acquisition of businesses and that applied to asset purchases differs, among other things, in the recognition of goodwill, the recognition and measurement of contingent consideration, the recognition of transaction costs and deferred taxes.

In order to be considered a business, an acquisition must include inputs and substantive processes that, together, contribute significantly to the ability to produce outputs. Essentially, the changes to the definition of a business relate specifically to the creation of a framework for assessing when a substantive process exists, and to the narrower use of the term "outputs". In addition, companies can opt to perform what is known as a “concentration test”. This involves examining whether the entire fair value of the acquired gross assets is largely concentrated in one asset or a group of similar assets. If such a concentration is identified, it is concluded, without any further assessment being performed, that the acquisition does not relate to a business.

The amendments are applicable – subject to adoption into EU law, which is still pending – for the first time to acquisition transactions whose acquisition date falls on or after the start of the first annual reporting period beginning on or after 1 January 2020. Early application is permitted.

Amendments to IFRS 10 and IAS 28 – Sale or Contribution of Assets between an Investor and its Associate or Joint Venture

The amendments address a known inconsistency between the provisions in IFRS 10 and those in IAS 28 (2011) in the event of the sale of assets to an associate or joint venture and/or the contribution of assets to an associate or joint venture.

Under IFRS 10 a parent must recognise total profit or loss from the sale of a subsidiary on the statement of income when control is lost. In contrast, the currently applicable IAS 28.28 requires that the sale proceeds in the case of sales transactions between an investor and an equity holding measured at equity – whether it is an associate or a joint venture – are only recognised in the amount of the share of the other shareholders in this entity.

In future, the entire profit or loss on a transaction is only to be recognised if the sold or received assets constitute a business operation as defined in IFRS 3. This applies regardless of whether the transaction is structured as a share or asset deal. Conversely, if the assets do not constitute a business operation, it is only permissible to recognise proportionate net income.

Initial application of the amendments has been postponed for an indefinite period of time by the IASB.

Amendments to IAS 19 Plan Amendment, Curtailment or Settlement

The amendments to IAS 19 relate to plan amendment, curtailment or settlement. In accordance with IAS 19.99, the net defined benefit liability has to be remeasured in such cases taking current actuarial assumptions into account. In accordance with the amendments, the current service cost and the net interest for the period after the remeasurement also have to be determined based on the updated actuarial assumptions. In addition, the remeasured net liability (taking into account the adjusted benefits resulting from the intervention) is to be used to determine the net interest expense after the intervention.

Subject to the still-pending adoption into EU law, the amendments need to be applied for the first time in the first reporting period in a financial year starting on or after 1 January 2019. Early application is permitted.

Improvements to IFRS 2015–2017

The Annual Improvements to IFRS 2015-2017 amended four IFRSs.

IFRS 3 clarifies that, when an entity obtains control over a business operation in which it previously held an interest as part of a joint operation, the principles governing successive business combinations are to be applied. The interest previously held by the acquirer is to be remeasured.

IFRS 11 states that a company does not remeasure its previously held interest in a joint operation when it obtains joint control of the business.

IAS 12 is amended in such a way that a company is to account for all income tax consequences of dividend payments in the same way as the income on which the dividends are based.

Finally, IAS 23 states that, in connection with the calculation of the capitalisation rate, if a company has generally borrowed funds to purchase qualifying assets, the costs associated with debt taken out specifically in connection with the qualifying assets are not to be included until the asset is completed.

Subject to the still-pending adoption into EU law, the amendments need to be applied for the first time in the first reporting period in a financial year starting on or after 1 January 2019. Early application is permitted.

The above-mentioned Standards do not materially affect the Group financial statements of Hamburg Commercial Bank.

Going concern assumption

Accounting and valuation are based on the assumption that the Bank is a going concern. The Bank’s corporate planning forms the basis for the going concern assumption

2. Provision of a guarantee facility

I. Second loss guarantee of HSH Finanzfonds AöR

The fundamental information on the hedging effect of the guarantee is presented in the Annual Report as at 31 December 2017.

With the application of the provisions of IFRS 9 as of 1 January 2018, the compensation item of partial guarantee One was divided into two balance sheet items. The compensation item for financial instruments categorised as FVPL is reported in a separate balance sheet item (Compensation item for financial instruments categorised as FVPL under the second loss guarantee). The changes in the compensation item are reported in the income statement under Result from financial instruments categorised as FVPL, as this is where the changes in the valuation of the hedged loans are also shown. For financial instruments that are not categorised at FV held for trading, the compensation item was still within loan loss provisions. The disclosure in the statement of income is made in the corresponding income item Loan loss provisions.

Privatisation of the Bank

As part of the privatisation of the Bank, an agreement was reached between Hamburg Commercial Bank AG, the guarantor HSH Finanzfonds AöR and HSH Beteiligungsmanagement GmbH on 28 February 2018 on the premature termination of the agreement on the provision of a guarantee facility. This means that, on the date on which the cancellation takes effect, Hamburg Commercial Bank AG will no longer be under any obligation to pay guarantee fees, and the guarantor will make a compensation payment to Hamburg Commercial Bank AG to compensate for the loss facility that has not yet been settled/disbursed. In addition, Hamburg Commercial Bank AG had to make a one-off payment of € 100 million to the guarantor to compensate for the monetary benefits associated with the early termination of the guarantee, as well as the premature liquidity effect, in particular state aid law advantages resulting from the fact that premium payments are no longer to be made. This put pressure on the statement of income in 2018.

The cancellation of the guarantee, remuneration and compensation payment, i.e. the guarantee cancellation agreement, depended on the closing of the purchase agreement on the shares in Hamburg Commercial Bank AG (share purchase agreement), corresponding notification sent to the parties to the agreement on the sale of an extensive credit portfolio (portfolio transaction) on 28 February 2018 and, as a result, on the closing of the portfolio transaction.

Accounting impact of the second loss guarantee in the 2018 financial year

With the execution of the share purchase agreement - the "closing" of the privatisation process - on 28 November 2018, the guarantee agreement was also cancelled with a compensation payment of € 5,711 million made by HSH Finanzfonds AöR. Together with the losses already paid in the 2018 financial year, the payments made by HSH Finanzfonds AöR in the 2018 financial year amount to € 6,203 million. The payments led to the complete derecognition of the 3 balance sheet items from the guarantee in the amount of € 6,195 million. Premium payments relating to the credit derivative (CDS) in 2018 will be compensated for in the amount of € 8 million.

The guarantee facility granted by the Free and Hanseatic City of Hamburg and the Federal State of Schleswig-Holstein via HSH Finanzfonds AöR which had a hedging effect for the first time as at 31 December 2010, no longer exists as at 31 December 2018 (previous year: € 6,195 million). Since the guarantee had already been utilised in full as at 31 December 2017, there is no impact on earnings in the statement of income either (previous year: € 82 million).

The guarantor made payments of € 10 billion over the entire term of the guarantee.

Since the 2009 reporting year the Bank has recorded premium expense totalling € 4,024 million for the provision of the second loss guarantee. Of this amount, € 1,135 million is attributable to one-off payments, including € 100 million from the early termination of the guarantee. This figure also includes payments made to HSH Beteiligungs Management GmbH in the amount of € 260 million.

Hedging effect of the guarantee

(€ m)	2018			2017		01.01.2018	2017	
	Balance sheet			Balance sheet			Statement of income	
	Loan loss provisions	Credit derivative	Compensation item for financial instruments categorised as FVPL	Loan loss provisions	Credit derivative	Compensation item for financial instruments categorised as FVPL	Loan loss provisions	Credit derivative
Compensation under the second loss guarantee	1,696	1,014	3,485	1,696	–	3,485	-2,673	–
Payments to HSH Finanzfonds AöR	-1,696	-1,014	-3,485	–	–	–	1,945	–
Fair valuecredit derivative	–	–	–	–	1,014	–	–	810
Hedging effect of the guarantee	–	–0	–	1,696	1,014	3,485	-728	810

3. Adjustments to the prior-year figures

I. Changes in the Group statement of income

A) CHANGES IN THE STRUCTURE OF THE GROUP STATEMENT OF INCOME IN CONNECTION WITH ADJUSTMENTS DUE TO IFRS 9

The structure of this Group statement of income contains changes as against the structure of the Group statement of income as at 31 December 2017. Some of the figures in the Group statement of income as at 31 December 2017 have also been adjusted accordingly in the comparison columns of this Group statement of income.

The changes relate to the structure of the statement of income. The adjustments have to be made under IAS 8.14 because they are either required as a result of the amendments under IFRS 9 or because they allow the financial statements to provide reliable and relevant information about the impact of transactions, other events or conditions on the earnings, net assets and financial position or cash flows of the company. The provisions stipulate that the adjustments also have to be applied to the comparative period.

The structure of the statement of income was adjusted with regard to the following items with the first-time application of IFRS 9.

Net interest income:
Due to the amendments to IAS 1 (IAS 1.82(a)) resulting from IFRS 9, interest income calculated using the effective interest rate method must be shown separately. This means that, with the first-time application of IFRS 9, Hamburg Commercial Bank discloses the following items for corresponding interest income within net interest income:

- Interest income from financial assets categorised as AC and FVOCI
- Negative interest on investments categorised as AC and FVOCI.

Other interest income is included in the items:

- Interest income from other financial instruments
- Negative interest on other cash investments and derivatives

The items reported in previous financial statements

- Interest income
- Negative interest on cash investments and derivatives

have been adjusted to reflect the new structure for the prior-year figures. Interest income amounted to € 3,086 million in the prior-year period from January to December 2017. Of this amount, € 1,130 million was reclassified to the new item Interest income from financial assets categorised as AC and FVOCI and € 1,657 million was reclassified to the new item Interest income from other financial instruments. The remaining amount of € 299 million was reclassified to the new item Result from the disposal of financial assets classified as AC (see the comments in the following section on the Result from the disposal of financial assets classified as AC).

The item Negative interest on cash investments and derivatives amounted to € 305 million in the prior-year period from January to December 2017. Of this amount, € 30 million was reclassified to the new item Negative interest on investments categorised as AC and FVOCI and € 275 million was reclassified to the new item Negative interest on cash investments and derivatives.

Result from financial instruments categorised as FVPL:
In previous financial statements, Net trading income already included not only results from financial instruments classified as HfT, but also results attributable to financial instruments designated at fair value through profit or loss. Since holdings of financial instruments classified as FVPL that are not held for trading have increased significantly under IFRS 9, the item was renamed Result from financial instruments categorised as FVPL with the first-time application of IFRS 9. The item has only been renamed, meaning that the comparative figures for the previous period (formerly Net trading income) did not have to be adjusted.

Result from the disposal of financial assets classified as AC:
Due to the amendments to IAS 1 (IAS 1.82 (aa)) as a result of IFRS 9, a new item was introduced for the separate presentation of the result from the disposal of financial assets measured at amortised cost ("AC" category). In previous financial statements in accordance with IAS 39, corresponding disposal results for receivables/financial investments categorised as LaR were reported under Net interest income, Other operating result or Net income from financial investments.

The previous year's figures for the corresponding items for the period from January to December 2017 were adjusted to reflect the changed structure. Out of

- interest income, € 299 million
- net income from financial investments, € 28 million

- the other operating result, € -25 million

was reclassified to the Result from the disposal of financial assets classified as AC.

Loan loss provisions:
In previous financial statements in accordance with IAS 39, new provisions and the reversal of impairments on financial investments were still shown under Net income from financial investments. Due to the amendment to IAS 1 (IAS 1.82(ba)) resulting from IFRS 9, all impairment results have to be presented separately with the first-time application of IFRS 9. This means that the above-mentioned impairment results can no longer be shown together with other net income from financial investments in one item. In order to comply with this requirement, Hamburg Commercial Bank has decided that, upon the first-time application of IFRS 9, all new provisions and reversals of impairments will be shown in the statement income under a single item, Loan loss provisions, irrespective of the corresponding balance sheet items. This means that the new Loan loss provisions item includes impairment results on financial investments in addition to loan loss provisions in the lending business.

This does not affect the recognition of impairments in the balance sheet. On the assets side, the balance sheet items Loans and advances to banks and Loans and advances to customers are still presented in gross terms, whereas the Financial investments balance sheet item is still presented in net terms. This means that the total loan loss provisions attributable to loans and advances continues to be shown as a separate balance sheet item. The loan loss provisions attributable to financial investments, however, are still offset against the carrying amounts in the balance sheet item Financial investments.

A retrospective adjustment of the previous year's figures in the statement of income to reflect the changed structure is not relevant. IAS 1.82(ba) explicitly refers to impairment results calculated in accordance with the corresponding IFRS 9 provisions. As Hamburg Commercial Bank has not adjusted the previous year's figures retrospectively to reflect IFRS 9, there are no corresponding results for the comparative period.

In the comparative period from January to December 2017, impairment results of € -19 million calculated in accordance with IAS 39 were recognised in Net income from financial investments.

B) FURTHER CHANGES IN THE PRESENTATION OF THE GROUP STATEMENT OF INCOME

The presentation of the statement of income was amended as follows during the reporting period.

1. Since this financial year, expenses paid in advance and charged on by Hamburg Commercial Bank have no longer been reported under Administrative expenses but under the Other operating result. Corresponding income (from charges passed on) was already reported under the Other operating result the past. The uniform presentation of the affected expenses together with the corresponding income provides a more accurate picture of the Group’s earnings situation. The adjustment affects disclosure in the statement of income and statement of financial position as well as the explanatory notes. The changes are implemented for the first time in the Group financial statements as at 31 December 2018.

In the year under review, expenses from expenses paid in advance and charged on amounted to approximately € 25 million. For the prior-year period from 1 January 2017 to 31 December 2017, these adjustments result in a reduction in administrative expenses of approximately € 26 million and an increase in other operating expenses of approximately € 26 million (see Note 17 and Note 16).

2. Since this financial year, regulatory expenses (i.e. levies imposed by supervisory authorities in addition to the bank levy) and expenses for banking associations have no longer been reported under Administrative expenses, but rather together with the expenses for the bank levy and deposit guarantee fund. As a result of this expansion, the previous income statement item “Expenses for bank levy and deposit guarantee fund” will be renamed “Expenses for regulatory affairs, deposit guarantee fund and banking associations”. The change described above, i.e. the aggregation of homogeneous expense items to form one income statement item, provides a more accurate picture of the Group’s earnings situation. The adjustment affects disclosure in the statement of income and statement of financial position as well as the explanatory notes.

The changes are implemented for the first time in the Group financial statements as at 31 December 2018.
In the year under review, expenses for the above-mentioned regulatory expenses and expenses for banking associations amounted to approximately € 8 million. For the prior-year period from 1 January 2017 to 31 December 2017, these adjustments result in a reduction in administrative expenses of approximately € 8 million and an increase in expenses for regulatory affairs, deposit guarantee fund and banking associations of approximately € 8 million (see Note 18 and Note 16).

C) TABLE SHOWING THE ADJUSTMENT OF THE PREVIOUS YEAR’S FIGURES IN THE GROUP STATEMENT OF INCOME

The following table summarises the adjustments to the prior-year figures in the statement of income as explained above:

Statement of income

(€ m)	2017 after adjustment	2017 before adjustment
Interest income from financial assets categorised as AC and FVOCI	1,130	n.r.
Interest income from other financial instruments	1,657	n.r.
Interest income	n.r.	3,086
Negative interest on investments categorised as AC and FVOCI	-30	n.r.
Negative interest on other cash investments and derivatives	-275	n.r.
Negative interest on cash investments and derivatives	n.r.	-305
Interest expenses	-2,202	-2,202
Positive interest on borrowings and derivatives	296	296
Net income/loss from hybrid financial instruments	304	304
Net interest income	**880**	**1,179**
Net commission income	65	65
Result from hedging	-18	-18
Result from financial instruments categorised as FVPL (formerly Net trading income)	254	254
Net income from financial investments	62	90
Result from the disposal of financial assets classified as AC	302	n.r.
Result from the reclassification of financial assets formerly classified as AC	–	–
Result from the reclassification of financial assets formerly classified as FVOCI as a mandatory requirement	–	–
Net income from financial investments accounted for under the equity method	2	2
Total income	**1,547**	**1,572**
Loan loss provisions	-2,086	n.r.
Loan loss provisions in the lending business	n.r.	-2,086
Hedging effect of credit derivative second loss guarantee	810	810
Total income after loan loss provisions	**271**	**296**
Administrative expenses	-481	-515
Other operating result	21	22
Expenses for bank levy and deposit guarantee fund	-49	-41
Net income before restructuring and privatisation	**-238**	**-238**
Net income from restructuring and privatisation	-66	-66
Expenses for government guarantees	-149	-149
Net income before taxes	**-453**	**-453**
Income tax expenses	-75	-75
Group net result	**-528**	**-528**

II. Changes in the Notes

Hamburg Commercial Bank has adjusted the classification of financial instruments with multiple termination rights for the purposes of the 2018 annual financial statements in line with the valuation hierarchy in accordance with IFRS 13. The valuation model underlying the fair value calculation of this financial instruments uses inputs that are unobservable in the market. As a result, the affected financial instruments were allocated to Level 3 in the past. As part of a current analysis of the valuation model used, the impact of the unobservable input on the fair value calculation was classified as insignificant, meaning that these financial instruments will be allocated to Level 2 in future (with an adjustment being made to the corresponding prior-year figures).

As at 31 December 2017, the retrospective adjustment results in a transfer from Level 3 to Level 2 totalling approximately € 1,573 million for financial instruments on the assets side and approximately € 707 million for financial instruments on the liabilities side. These amounts are distributed among the balance sheet items as follows:

Fair values of financial instruments - assets

(€ m) 2017	Assets recognised at fair value			
	Level 2 (before adjustment)	Level 2 (after adjustment)	Level 3 (before adjustment)	Level 3 (after adjustment)
Held for Trading (HfT)	**3,212**	**3,229**	**1,362**	**1,345**
Trading assets	3,212	3,229	348	331
Credit derivative under the second loss guarantee	–	–	1,014	1,014
Designated at Fair Value (DFV)	**178**	**1,734**	**1,689**	**133**
Loans and advances to customers	54	1,170	1,201	85
Financial investments	124	564	488	48
Available for Sale (AfS)	**1,210**	**1,210**	**173**	**173**
Cash reserve	106	106	–	–
Loans and advances to banks	36	36	43	43
Loans and advances to customers	–	–	45	45
Financial investments	1,068	1,068	85	85
No IAS 39 category	**264**	**264**	**–**	**–**
Positive fair value of hedging derivatives	264	264	–	–
Receivables under finance leases	–	–	–	–
Value adjustments from the portfolio fair value hedge	–	–	–	–
Total assets	**4,864**	**6,437**	**3,224**	**1,651**

Fair values of financial instruments - liabilities

(€ m) 2017	Liabilities recognised at fair value			
	Level 2 (before adjustment)	Level 2 (after adjustment)	Level 3 (before adjustment)	Level 3 (after adjustment)
Held for Trading (HfT)	**3,134**	**3,708**	**741**	**167**
Trading liabilities	3,134	3,708	741	167
Designated at Fair Value (DFV)	**1,543**	**1,676**	**1,021**	**888**
Liabilities to banks	11	11	107	107
Liabilities to customers	302	398	517	421
Securitised liabilities	1,230	1,267	397	360
Subordinated capital	–	–	–	–
No IAS 39 category	**163**	**163**	**–**	**–**
Negative fair value of hedging derivatives	163	163	–	–
Value adjustments from the portfolio fair value hedge	–	–	–	–
Total liabilities	**4,840**	**5,547**	**1,762**	**1,055**

4. Consolidation principles

The Group financial statements present the parent company Hamburg Commercial Bank AG together with the consolidated subsidiaries as an economic unit. Subsidiaries also include structured entities that are controlled by Hamburg Commercial Bank. Structured entities are entities in which voting rights and similar rights do not constitute the dominant factor in assessing control. These also include entities whose relevant activities are predetermined by a narrow objective defined in the articles of association/partnership agreement or in other contractual agreements or in which there is a lasting restriction of the decision-making powers of the management. Hamburg Commercial Bank mainly includes ABS conduits and other securitisation and refinancing vehicles as well as investment funds (including private equity funds) within structured entities. Structured entities are included in the scope of consolidation if they are subsidiaries and are material to the presentation of the net assets, financial condition and earnings or to the assessment of the risk situation of the Hamburg Commercial Bank Group. Disclosures of the nature of the risks in connection with shares in consolidated structured entities are included in Note 5 . Reference is made to Note 56 with regard to unconsolidated structured entities.

Control over a subsidiary prevails when Hamburg Commercial Bank is exposed to variable incoming cash flows from the exposure to this entity or has rights to such cash flows and is able to influence the cash flows through its decision-making power over the entity. Hamburg Commercial Bank possesses decision-making power over an entity if it has rights that confer on it, either directly or indirectly via third parties, the current possibility of controlling the entity's relevant activities.

Relevant activities are deemed to be those which materially affect the entity's incoming cash flows depending on the nature and purpose of the entity. Variable incoming cash flows are all those which can vary depending on the entity's performance. Incoming cash flows from the exposure to another entity may accordingly be positive as well as negative. Variable incoming cash flows include dividends, fixed and variable interest, remuneration and fees, fluctuations in the value of investments and other financial advantages.

The assessment as to whether decision-making power exists is made on the basis of the relevant activities of the entity and the powers of Hamburg Commercial Bank to influence them. Voting rights as well as other contractual rights are considered in reviewing the control of relevant activities provided there are no economic or other obstacles to the exercise of the existing rights and Hamburg Commercial Bank would benefit from exercising those rights. The Bank has decision-making power based on voting rights if as a result of equity instruments or contractual agreements Hamburg Commercial Bank holds more than 50 % of the voting rights and this proportion of the voting rights is allied to a substantial decision-making right with regard to the relevant activities. Other contractual rights that may facilitate a controlling influence are primarily rights to appoint members of executive bodies, recall them, to liquidate and to make other decisions. Hamburg Commercial Bank controls a subsidiary if based on the total contractual rights it has the possibility to control the relevant activities of the entity.

A subsidiary is also controlled by Hamburg Commercial Bank if the decision-making power is exercised by third parties in the interests of and for the benefit of Hamburg Commercial Bank. Whether such delegated decision-making power exists is judged by considering the existing powers to appoint members of executive bodies, the legal and de facto scope for making decisions and the structure of the economic incentives. Hamburg Commercial Bank itself does not exercise any delegated powers to make decisions that would benefit third parties.

Due to agreements ceding control, Hamburg Commercial Bank in individual cases holds equity interests in companies exceeding 50 % which are not tied to any corresponding voting rights and therefore do not result in any controlling influence. In such cases, for purposes of defining the scope of consolidation as well as for purposes of preparing the list of shareholdings, the voting rights ratios were adjusted to the extent deemed reasonable under the special circumstances described above. Conversely, Hamburg Commercial Bank possesses a controlling influence in individual cases based on contractual rights, although it holds less than 50 % of the voting rights.

Shares held by third parties in the equity of the subsidiary are shown as non-controlling interests in Group equity, provided these are not shares of external shareholders in consolidated commercial partnerships. Non-controlling interests are that part of the net results for the period and net assets of a subsidiary related to shares not directly held by the parent company or by a Group subsidiary. Non-controlling equity shares in subsidiaries and the resulting profit or loss as well as summarised financial information on subsidiaries with material non-controlling shares are presented in Note 5 . Shares of external shareholders in consolidated commercial partnerships constitute puttable financial instruments, which are to be classified as debt in the Group financial statements under IAS 32 and disclosed under Other liabilities. Changes in value are recognised in Other operating income/expenses in the consolidated statement of income.

Subsidiaries are included by way of full consolidation in the Group financial statements of Hamburg Commercial Bank. In consolidating the capital the carrying amount of the equity holding in each subsidiary is set off against the share of Hamburg Commercial Bank in the subsidiary's equity capital. Goodwill connected to this is accounted for using the acquisition method in accordance with IFRS 3. Intra-Group receivables, liabilities and income are are eliminated within the framework of debt and/or expense and income consolidation for the purpose of the Group financial statements. Expenses and gains arising from the transfer of assets within the Group are eliminated as well.

Shares in subsidiaries which were not consolidated because of their subordinate importance for Hamburg Commercial Bank Group's earnings, net assets and financial position are accounted for as financial instruments at fair value through profit & loss (FVPL) based on the recognition and measurement guidelines of IFRS 9.

Structured entities within the meaning of IFRS 12 are entities designed so that voting rights or similar rights do not represent the dominant factor in terms of assessing whether control is being exercised. Voting rights in such entities only relate to contractually specified administrative functions. Similar rights would refer, for example, to potential voting rights such as options on voting rights. Structured entities like securitisation vehicles are controlled by Hamburg Commercial Bank and included as subsidiaries in the Group financial statements if Hamburg Commercial Bank has decision-making power over the relevant activities and is subject to variable return flows from these activities.

Hamburg Commercial Bank does not classify single asset companies and project companies as structured entities, because as a rule they are not designed to ensure that holding voting rights is only for the purpose of performing contractually governed administrative functions. Structured entities are also characterised by a narrowly defined business purpose, a limited field of activity and comparatively low equity capital. If a company is not controlled by voting rights but by means of contractual rights, it is classified as a structured entity.

Joint arrangements are based on contractual agreements under which two or more partners establish an economic activity under shared management. Joint management is present if the partners have to cooperate in order to steer the relevant activities of the joint arrangement and decisions require unanimous approval from the participating partners. Such a joint arrangement is a joint venture if the partners who exercise joint management hold rights and obligations to the net assets of the arrangement. If, conversely, the partners have direct rights to the assets or liabilities attributable to the joint arrangement for their debts, the arrangement is a joint operation. If a joint arrangement is embodied in a legally independent partnership or corporation with its own assets, so that Hamburg Commercial Bank only has a proportionate claim to the net assets of the company based on its shares in the company, this entity is normally a joint venture. In order to determine whether a joint venture or a joint operation is concerned in the case of joint arrangements, the contractual provisions and the purpose of the joint arrangement are used in addition. If neither the legal form nor the contractual provisions or other facts and circumstances provide an indication that Hamburg Commercial Bank has direct rights to the assets and/or obligations for the debts of the joint arrangement, it is a joint venture.

Associates are companies where Hamburg Commercial Bank AG can exercise a significant but not controlling influence directly or indirectly via subsidiaries. Significant influence refers to the possibility of influencing decisions affecting the financial and business policy of another entity but not controlling it. Significant influence is found in principle if Hamburg Commercial Bank as an investor directly or indirectly through subsidiaries holds 20 % or more of the voting rights. It may also be an associate if Hamburg Commercial Bank has less than

20 % of the voting rights but because of other factors has the possibility of influencing the company's decisions concerning financial and business policy. This in particular includes the representation of Hamburg Commercial Bank in the entity's decision-making body and contractual rights to manage or dispose of assets including investment decisions in the case of investment funds. If Hamburg Commercial Bank only holds rights to approve, agree or veto, significant influence is not presumed to exist.

Interests in joint ventures and associates that are material to the proper presentation of the Group's net assets, financial position and results of operations are consolidated under the equity method. In doing so, the Group's interest in a joint venture / share in an associate is initially measured at cost of acquisition and thereafter increased or decreased depending on the Group's share in the joint venture's/associate's profit or loss. The relevant shares are stated in the statement of financial position under a separate line item.

Interest in joint ventures and associates, respectively, which were not consolidated under the equity method because of their subordinate importance for Hamburg Commercial Bank Group's earnings, net assets and financial position have been accounted for as financial instruments at fair value through profit & loss (FVPL) based on the recognition and measurement guidelines of IFRS 9 and are disclosed under financial investments. Where Hamburg Commercial Bank has no information as of the reporting date which would allow for the fair value of these interests to be reliably determined, measurement is based on acquisition cost.

5. Scope of consolidation

In addition to the parent company, Hamburg Commercial Bank AG, Hamburg/Kiel, the scope of consolidation includes 32 fully consolidated subsidiaries (31 December 2017: 53).

As at December 31, 2017, there are no associates or joint ventures accounted for using the equity method.

The subsidiaries included in the Group financial statements and those subsidiaries, joint ventures and associates that are not included due to their immateriality for the portrayal of the earnings, net assets and financial position of the Hamburg Commercial Bank Group can be found in the list of shareholdings (note 65). The list of shareholdings also includes explanatory information regarding classification as a subsidiary, joint venture or associate that differs from that indicated by voting rights.

The changes in the scope of consolidation during the financial year relate to the following subsidiaries.

Information on subsidiaries – changes to the scope of consolidation

A) ADDITIONS

There were no additions compared with 31 December 2017. While the company CAPCELLENCE Vintage Year 18 Beteiligungen GmbH & Co. KG, which was set up on 18 March 2018 and in which Hamburg Commercial Bank held the majority of voting rights, was included in the scope of consolidation on a fully consolidated basis during the year, due to the collapse merger of this company, on 12 December 2018, with CAPCELLENCE Holding GmbH & Co. KG, Hamburg, CAPCELLENCE Vintage Year 18 Beteiligungen GmbH & Co. KG, Hamburg, is no longer represented in the scope of consolidation as an independent legal entity.

B) DISPOSALS

As a result of the sale of a portfolio of receivables and company shares as part of the portfolio transaction, Hamburg Commercial Bank AG has no longer held any interest, within the meaning of IFRS 10, in the following companies since 29 November 2018, and, by contrast to the situation as at 31 December 2017, the affected former subsidiaries are no longer included in the scope of consolidation:

- Amentum Aircraft Leasing No. Five Limited, Dublin
- Amentum Aircraft Leasing No. Seven Limited, Dublin
- Amentum Aircraft Leasing No. Six Limited, Dublin
- Chasms Navigation Limited, Douglas
- Cregneash Navigation Limited, Douglas
- Curragh Navigation Limited, Douglas
- GODAN GmbH, Hamburg
- Ilex Integra GmbH, Hamburg
- ISM Agency LLC, New York
- Life Insurance Fund Elite LLC, New York
- Life Insurance Fund Elite LLC Trust, Minneapolis
- Mooragh Navigation Limited, Douglas
- RDM Limited, George Town
- Senior Preferred Investments S.A., Luxembourg
- Soderick Navigation Limited, Douglas

A total profit in the amount of € 13.1 million resulted from the deconsolidation of the abovementioned companies and is recognised under the item Other operating income. The profit is mainly the result of the disposal, within the context of deconsolidation, of liabilities to customers which had been recognised in the five single ship companies of the Navigation group, which had no assets and limited liability (non-recourse).

Contrary to the situation as at 31 December 2017, the following companies are also no longer included in the scope of fully consolidated companies:

- FSL Asset Management Pte. Ltd., Singapore
- FSL Holdings Pte. Ltd., Singapore
- FSL Trust Management Pte. Ltd., Singapore

With effect from 28 February 2018, GODAN GmbH, which is wholly owned by Hamburg Commercial Bank AG, sold 100 % of its shares in FSL Holdings Pte. Ltd. to an investor. Within this context, Hamburg Commercial Bank AG also sold its loan receivable from FSL Holdings Pte Ltd. to this investor. As a result of these transactions, Hamburg Commercial Bank has lost control over the FSL Group. In addition to the three subsidiaries mentioned above, the FSL Group also includes the 24.82 % interest in the First Ship Lease Trust reported as held for sale as at 31 December 2017. A profit in the amount of € 2.3 million resulted from the deconsolidation of the FSL Group, which is recognised under the item Other operating income.

2200 Victory LLC, Dover, was not included in the scope of consolidation due to its liquidation on 6 September 2018. The deconsolidation did not have any material effect on income.

In addition, the following subsidiaries, which were previously fully consolidated and were used in the past to process securitisation transactions, were no longer included in the Group financial statements as at 31 December 2018 because the companies were liquidated on 24 and 21 December 2018, respectively:

- Castellum ABF S.A., Luxembourg
- Stratus ABF S.A., Luxembourg

The deconsolidation of the two aforementioned companies had no material effect on income.

C) MODIFICATION OF HOLDINGS IN SUBSIDIARIES

There were no changes in the ownership interests held by Hamburg Commercial Bank in a subsidiary in the period under review that did not lead to a loss of control.

II. Information on shares held in associates and joint ventures accounted for under the equity method

A) GENERAL INFORMATION

At the reporting date, Hamburg Commercial Bank did not hold any shares in associates or joint ventures accounted for using the equity method that are material for the Group's earnings, net assets and financial position.

B) SUMMARISED FINANCIAL INFORMATION

As no shares in associates and joint ventures accounted for using the equity method are reported on the reporting date, only the previous year's figures are shown in the following overview.

Other shares held in associates accounted for under the equity method

(€ m)	2018	2017
Share of the following attributable to Hamburg Commercial Bank:		
Net income/loss for the year	-	2
Other comprehensive income	-	-
Total comprehensive income	-	2
Cumulative carrying amount	**-**	**-**

III. Information on consolidated structured entities

Hamburg Commercial Bank's scope of consolidation includes nine fully-consolidated structured entities. These companies are controlled due to contractual rights and/or principal-agent relationships. Concerning three of these companies, the majority of the voting rights is also held.

The following disclosures represent the type of risks in connection with business relationships with consolidated structured entities:

Hamburg Commercial Bank AG sponsors securitisation vehicles whose business purpose is to issue securities on the capital market and to invest the funds received in connection with these issues in silent participations at Hamburg Commercial Bank AG. Hamburg Commercial Bank has provided these consolidated structured entities with a guarantee facility. This guarantee facility serves to hedge the payment obligations of the structured entities in respect of the holders of the securities. These payment obligations arise if payment claims result for the structured entities against Hamburg Commercial Bank AG from the silent participations held by them.

Hamburg Commercial Bank AG has granted liquidity and credit facilities to consolidated structured entities. In terms of the amounts, these are of minor significance for the Group's financial position.

Hamburg Commercial Bank AG has a contractual obligation to bear the operating expenses for three consolidated structured entities.

During the reporting year, Hamburg Commercial Bank did not provide consolidated or unconsolidated structured entities with any non-contractual support.

As of the balance sheet date there is no current intention to provide a consolidated structured entity any financial or other support within the definition of IFRS 12.17.

6. Management estimates and discretionary decisions

Estimates:
As permitted, estimates and assumptions for the measurement of assets and liabilities have been incorporated into the Group financial statements of Hamburg Commercial Bank. All estimates and judgments necessary for accounting and measurement according to IFRS were undertaken in accordance with the appropriate standard in each case, are continuously reassessed and are based on past experience and other factors including expectations of future events which appear reasonable under the circumstances. In particular, the following topics are affected by estimation uncertainties (see also the explanatory information under Note 7):

- the level allocation and the determination of the amount of loan loss provisions under the impairment provisions set out in IFRS 9 (see the following explanatory information and Note 7)
- the calculation of the future cash flows from the hybrid financial instruments issued by Hamburg Commercial Bank (see the following explanatory information and Note 7)
- allocations to provisions for litigation risks (see the following explanatory information)
- the recognition and measurement of deferred taxes
- the calculation of fair values
- allocations to provisions for pensions and similar obligations and other provisions (see Note 7)

Where there is greater uncertainty regarding estimates relating to other aspects, the underlying assumptions are presented in greater detail in the relevant note.

Discretionary decisions:
With the exception of estimates, major discretionary decisions by management in the application of accounting and measurement methods include:

- the level allocation and the determination of the amount of loan loss provisions under the impairment provisions set out in IFRS 9 (see the following explanatory information and Note 7)

- the calculation of the future cash flows from the hybrid financial instruments issued by Hamburg Commercial Bank (see the following explanatory information and Note 7)
- allocations to provisions for litigation risks (see the following explanatory information)
- the definition of business models and the classification of financial instruments in accordance with IFRS 9 (see the following explanatory information and Note 7)
- determining fair values for certain financial instruments, including a judgement regarding the existence of an active or inactive market;
- use of the fair value option for financial instruments (see the following explanatory information and Note 7);
- assessing whether Hamburg Commercial Bank controls another entity;
- applying the current reclassification rules under IFRS 9.

Within the context of the new impairment provisions, there are both significant estimates and significant discretionary decisions with regard to the level allocation and the calculation of the amount of the loan loss provisions.

The transfer of a financial instrument between levels 1 and 2 and the associated definition of the extent giving rise to a significant deterioration in credit quality (significance threshold) is a central discretionary decision within the context of the new impairment provisions.

When calculating the loan loss provisions levels 1 and 2, Hamburg Commercial Bank estimates the associated credit risk parameters over a one-year period and extrapolates them on the basis of appropriate assumptions over a period of several years. Within this context, there are considerable uncertainties relating to estimates, particularly when including forward-looking macroeconomic scenarios.

The calculation of loan loss provision level 3 represents a further estimation process. In particular, the estimates for various scenarios, including associated probabilities of occurrence and the recoverable amount in the respective scenario, involve discretionary decisions in this respect.

The calculation of the future cash flows from the hybrid financial instruments issued by Hamburg Commercial Bank and allocations to provisions for litigation risks in connection with hybrid capital instruments result both in significant estimates and in significant discretionary decisions in connection with potential buy-back offers. With regard to estimates in the context of IFRS 9.B5.4.6, please refer to Note 7.

Major discretionary decisions in connection with the application of the classification and measurement provisions of IFRS 9 relate to the definition/classification of the Bank's business models and the corresponding allocation of portfolios of financial assets based on the objectives and control activities within the context of the business activity.

In particular, the definition of what constitutes harmless sales and materiality thresholds for harmful sales within the "Hold to collect" business model are discretionary decisions. The business models defined at Hamburg Commercial Bank and the resulting impact on the classification and measurement of financial instruments are shown in brief in the section entitled "Accounting and measurement principles".

The analysis of the contractual cash flows with regard to the contractual cash flow characteristics criterion, as well as the classification of modifications in terms of their materiality, constitute a further discretionary decision (see also the section entitled "Accounting and measurement principles").

Hamburg Commercial Bank applies the fair - value - option through profit or loss for financial assets at its own discretion with regard to the avoidance of an accounting mismatch. The designation of financial liabilities using the fair value - option to avoid an accounting mismatch, or on the basis of management on a fair value basis, is also at the discretion of the Bank.

7. Accounting and measurement principles

I. Financial instruments

A) CATEGORISATION OF FINANCIAL ASSETS AND LIABILITIES

Recognition and initial measurement of financial assets and liabilities

A financial instrument is an agreement which simultaneously creates a financial asset for one company and a financial liability or equity instrument for the other company. Under IFRS 9, all financial assets and liabilities including financial derivatives must be stated in the statement of financial position and measured according to the category to which they are assigned.

Financial assets and liabilities are stated in the statement of financial position if Hamburg Commercial Bank is counterparty under the contract for the corresponding financial instrument. Expected future transactions or contracts are not recognised.

Provided that they fulfil the criteria of IFRS 9, pending transactions in the form of derivatives must always be stated in the statement of financial position as financial assets or liabilities and measured at fair value on the trading date. Spot transactions in non-derivative financial assets (so-called regular way contracts) are recognised as of the settlement date. The change in fair value between the trading date and settlement date is recognised according to the measurement rules for the category of asset. Other non-derivative financial assets which do not result from spot transactions, for example loans granted, are recognised as of the settlement date.

Non-derivative financial liabilities are recognised if one of the two parties to the contract has fulfilled the contract (settlement date).

Initial recognition is measured at fair value, which generally corresponds to the acquisition cost of the financial instrument.

Derecognition of a financial asset takes place on the settlement date. In the case of derivatives, derecognition takes place on the trading date.

Definition of business models

In order to arrive at the classification of financial instruments, financial assets are first of all allocated to business models in accordance with IFRS 9. The Management Board and Supervisory Board of Hamburg Commercial Bank AG are responsible for defining these business models. Financial instruments are allocated to the business models at portfolio level. The internal rules and objectives, which are applied in practice in the strategic management and administration of the portfolios, are decisive when it comes to identifying and allocating the holdings. In addition, the definition and differentiation of the business models take into account how the results of the portfolios are assessed, which risks influence these earnings contributions and how these risks are managed.

Another aspect that is important for the purposes of defining business models at Hamburg Commercial Bank in connection with the assessment of business activity and objectives for the management of the instruments is the analysis of transactions in past periods. This involves determining the frequency, volume and timing of disposals. The reason behind disposal transactions is also taken into account when assessing the disposal activity. If disposals are related, among other things, to the management of credit risk and are motivated by a significant increase in credit risk, they can still be consistent with a business model that serves to collect cash flows by holding the instruments to maturity.

The reclassification of financial assets is only possible in exceptional cases and subject to specific disclosure requirements. Financial liabilities cannot be reclassified.

Analysis of contractual cash flow characteristics

In addition to the appraisal of the business model, the categorisation of financial assets depends on the nature of the cash flows. Within this context, Hamburg Commercial Bank analyses the contractual cash flow characteristics criterion by assessing the contractual cash flows to determine whether they merely relate to payments of principal and interest on the principal amount. The analysis is carried out once at the time of initial recognition at the level of the individual transaction. When identifying and assessing the cash flows accordingly, all characteristics contained in the contractual components must be taken into account.

The contractual cash flow characteristics criterion defines interest as those payments that are consistent with a basic lending arrangement. This means that payments essentially serve as a form of compensation for the time value of money and the credit risk assumed by the counterparty. They can also include compensation for the assumption of liquidity risks and a profit margin. IFRS 9 uses the fair value at the time of initial recognition as a basis for determining the nature of principal repayments on the outstanding nominal amount.

Based on these requirements, all contractually agreed conditions are analysed to determine whether they give rise to opportunities for early termination or extension options, leverage effects or other effects on cash flows that depend on the occurrence of future circumstances. Within this context, Hamburg Commercial Bank examines the contractual structure of the instruments to determine whether they contain components that modify the fair value element of the money and contradict the interest rate characteristics defined under IFRS 9. It also examines whether there are "non-recourse" structures which impose restrictions on the Bank's ability to access the payments to which it is entitled.

The analysis of the contractual cash flow characteristics criterion for contractually linked instruments, which usually arise in securitisation transactions, is subject to special requirements. First, the cash flow characteristics are assessed by looking at the claims from the asset pools underlying the securitisation. In addition, the contractual structure of the securitisation tranche and the structuring of the claims to the cash flows from the underlying assets are examined with regard to the cash flow characteristics and credit risk distribution.

If Hamburg Commercial Bank's analysis of the contractual structure of the financial assets leads it to the conclusion that the payments are not just interest and principal payments, the cash flow criterion is deemed not to have been met.

Reclassification
Reclassifications are made in the event of actual changes in the business model used to manage the assets. Consequently, from the date of the change, all affected instruments are to be allocated to the newly defined business model and reclassified accordingly. No reclassifications have been made to date.

Classification and subsequent measurement of financial assets and liabilities
Financial assets are classified depending on the business model and the structure of the contractual cash flows under IFRS 9. In connection with the first-time application of IFRS 9, Hamburg Commercial Bank has defined the business models "Hold to collect", "Hold & sell" and "Other", which include the business model strategies "Held for trading" and "Other not hold to collect (remaining)" on the basis of its business activities.

Loans in the lending area and securities related to the lending business are assigned to the "Hold to collect" business model. The "Hold & sell" business model mainly comprises the capital markets business. Instruments intended to generate a profit in the short term are managed under the "held for trading" business model. This mainly relates to interest-bearing treasury securities. In addition, syndication shares from underwriting activities subject to a syndication requirement in the lending business are allocated to this category. Derivatives are generally allocated to this business model. Financial assets in the "Other not hold to collect (remaining)" business model relate primarily to equity portfolios in the non-trading portfolio.

Provided that the cash flow criterion is fulfilled, subsequent measurement depends on the business model allocation and is derived from the measurement categories described below. Debt instruments assigned to the "Hold to collect" business model are recognised at amortised cost. "Hold & sell" assets are measured at fair value, with the result from fair value changes being recognised in Other comprehensive income (OCI) within equity. Upon the derecognition of the debt instruments, the cumulative valuation result is derecognised from Other comprehensive income via the statement of income (known as "recycling"). Debt instruments in the "Other not hold to collect (remaining)" business model are subject to measurement at fair value through profit or loss.

Financial assets that do not meet the cash flow criterion are measured at fair value in the statement of income, taking the valuation results into account, irrespective of the business model. These instruments include, first of all, debt instruments that do not pass the cash flow test in the analysis of the contractual structure and second, equity instruments that generally do not meet the criterion.

In the case of structured financial assets, there is no requirement to separate embedded derivatives under IFRS 9. The instruments are to be assessed, depending on the business model, in their entirety based on their contractual structure in the analysis of the contractual cash flow characteristics criterion.

Financial obligations are measured at amortised cost under IFRS 9 in the "Not held for trading" category. Derivatives and instruments that are held for trading are allocated to the "Held for trading" category and are measured at fair value through profit or loss. This measurement standard is also applied, in general, to financial liabilities irrevocably designated within the fair value option, although the amount of the fair value change resulting from the change in the Bank's own credit risk is recognised directly in OCI.

In cases involving structured financial liabilities that are not included in measurement at fair value through profit or loss due to categorisation or designation, derivatives requiring separation must be separated and also measured at fair value through profit or loss. The host contract is recognised at amortised cost.

The financial assets/liabilities of Hamburg Commercial Bank are allocated to the following holding categories in order to arrive at the measurement categories depending on the business model allocation and the results of the cash flow criterion analysis. For the purposes of presentation in the Group financial statements, they are also grouped into reporting categories.

Reporting category	Holding category	Measurement category
AC assets/AC liabilities	AC HTC/ AC LIA	AC
FVOCI Mandatory	FVOCIR HAS	FVOCIR
FVPL held for trading	FVPL HFT	FVPL
FVPL Other	FVPL HTC FVPL HAS FVPL RES	FVPL
FVPL designated	FVPL DFV/ FVPL DFP	FVPL

"AC assets" and "AC liabilities" are subsequently measured at amortised cost. Interest payments are recognised in net interest income. Profits/losses from the disposal of financial assets that are not credit-impaired and prepayment penalties are reported under "Result from the disposal of financial assets classified as AC".

Instruments classified as FVOCI as a mandatory requirement in the "Hold & Sell" business model are stated at fair value and booked directly to equity. Impairments and currency translation results, however, are reported directly in the statement of income. When the instruments are derecognised, the cumulative valuation result recorded under "Other comprehensive income" is rebooked to the statement of income. Realised gains from the disposal of assets assigned to levels 1 and 2 are recorded, in cases involving fixed income securities under the "Financial investments" balance sheet line item, under "Net income from financial investments". Gains from the corresponding disposal of level 3 assets are recognised in the result from loan loss provisions. Interest and prepayment penalties, current results and realised gains on level 1 and level 2 loans are shown in Net interest income. Loan impairments are shown under Loan loss provisions in the statement of income.

For those instruments stated at fair value through profit or loss in the FVPL Held for Trading, FVPL Designated and FVPL Other reporting categories, the fair valuation and the realised gains and losses are reflected via the result from financial instruments categorised as FVPL. Commission results in the FVPL Held for Trading category resulting from non-round tripping transactions in securities and promissory note loans are also shown under this item. Ongoing earnings contributions from instruments stated at fair value through profit or loss, such as dividends, interest results and prepayment penalties, as well as realised gains from the buy-back of own issues in the FVPL Held for Trading category form part of net interest income.

Commission income contributions from derivatives and from loans in all categories are shown under Net commission income. This item also includes commission from securities and promissory note loans in the FVPL Held for Trading category resulting from round tripping transactions. Gains from currency translation is generally a component of the Result from financial instruments categorised as FVPL.

This results in the following distinctions, based on reporting category, for subsequent measurement at Hamburg Commercial Bank:

1. Financial assets valued at amortised cost (AC) are stated, at the time of initial recognition, at cost, equivalent to fair value at the time of initial recognition, and taking transaction costs into account. Financial liabilities are also recognised at fair value at the time of issue, taking transaction costs into account. Fair value at the time of acquisition generally corresponds to the transaction price. This valuation category includes all instruments in the following reporting categories:

a. Financial assets in the "AC assets" reporting category are allocated to the "Hold to collect" business model and meet the cash flow criterion.
b. Those liabilities that neither fall under the trading portfolios nor belong to the FVPL Designated reporting category, are allocated to the "AC liabilities".
c. For instruments on both the assets and the liabilities side, subsequent measurement is at amortised cost; premiums or discounts are amortised according to the effective interest method over the term and are recognised in net interest income.

2. Financial assets in the "FVOCI mandatory" reporting category include all assets in the "Hold & sell" business model for which the cash flow criterion is met. The holdings within Hamburg Commercial Bank relate mainly to marketable interest-bearing securities.

The initial measurement of financial assets in the "FVOCI Mandatory" category is at the fair value, which generally corresponds to the transaction price, plus transaction costs. The subsequent measurement of the financial instruments is at fair value.

Changes in the value of instruments stated at fair value, insofar as these are not attributable to an impairment or currency translation, are recorded under Other comprehensive income (OCI) in equity, after allowing for deferred taxes. By contrast, where hedged instruments are concerned, the fluctuation relating to the hedged risk is recognised in the statement of income under "result from hedging" and is separately disclosed as an adjustment item arising from the portfolio fair value hedge. When the instruments are derecognised, the cumulative valuation result recorded under "Other comprehensive income" is rebooked to the statement of income.

Amortisation of the difference between costs of acquisition and repayment amount for interest-bearing securities is stated under net interest income, using the effective interest method.

3. Financial assets and liabilities valued at fair value through profit or loss (FVPL), include instruments held for trading (FVPL Trading), financial assets that have to be measured at fair value because they do not meet the cash flow criterion (FVPL Other), and those instruments that are voluntarily designated at fair value in a manner that is irrevocable for the future (FVPL Designated).

a. At Hamburg Commercial Bank, the category FVPL Trading includes all financial instruments held for trading that are assigned to the "held for trading" business model accordingly, and all derivatives that are not part of a hedging relationship (hedge accounting). They are initially and subsequently measured at fair value. Transaction costs are recognised through profit or loss on acquisition date. In accordance with IFRS 9.5.1.1 , transaction costs are only included in the initial recognition in the case of financial assets or liabilities not measured at fair value through profit or loss. Where a market price is available in the form of a stock exchange listing, this is used for the purposes of measurement. In other cases, the market price of comparable instruments or recognised measurement models, especially net present value methods and option pricing models, are used to determine fair value.

b. The financial assets in the FVPL Other category are assigned to the "Hold to collect", "Hold & sell" and "Other not hold to collect (remaining)" business models. The instruments in the "Hold to collect" and "Hold & sell" business models within this category do not meet the cash flow criterion.

c. The financial assets and liabilities in the FVPL Designated reporting category relate primarily to securities and loans that form part of an economic hedging relationship with interest rate derivatives and do not meet the requirements for hedge accounting, as well as complex structured registered and bearer securities with embedded interest, currency, equity and other risks. In such cases, the fair value option serves to prevent/reduce any accounting mismatch. In addition, designation within the fair value option can be applied, within Hamburg Commercial Bank, to portfolios of financial liabilities whose management and performance measurement is based on the fair value in line with the documented risk management strategy in order to allow the instruments to be accounted for in line with the internal control system.

Financial instruments in the fair value option are stated at fair value in the statement of financial position and are valued through profit or loss for the purposes of subsequent measurement accordingly.

B) CLASSIFICATION OF FINANCIAL INSTRUMENTS

The classification of financial instruments required for reporting by IFRS 7.6 is similar to the categorisation of financial instruments according to IFRS 9 for the items in the statement of financial position, in order to ensure a uniform and clear picture of the financial position and performance. The following table shows the categories of financial instruments at Hamburg Commercial Bank in accordance with IFRS 9. The table for the categories of financial instruments under IAS 39 which are relevant for the information on comparative periods is presented further below.

Measurement method	Categories	
	IFRS 9 reporting category	Statement of financial position item/sub-item
Financial instruments measured at amortised cost	AC assets	Cash reserve
		Loans and advances to banks
		Loans and advances to customers
		Financial investments
		Non-current assets held for sale and disposal groups
		Other assets
	AC liabilities	Liabilities to banks
		Liabilities to clients
		Securitised liabilities
		Liabilities relating to disposal groups
		Subordinated capital
		Other liabilities
Financial instruments measured at Fair Value through Other Comprehensive Income (OCI)	FVOCI Mandatory	Cash reserve
		Loans and advances to banks
		Loans and advances to customers
		Financial investments
		Non-current assets held for sale and disposal groups
Financial instruments measured at fair value through profit or loss	FVPL held for trading	Trading assets
		Credit derivative under the second loss guarantee
		Non-current assets held for sale and disposal groups
		Trading liabilities
		Liabilities relating to disposal groups
	FVPL designated	Loans and advances to banks
		Loans and advances to customers
		Financial investments
		Non-current assets held for sale and disposal groups
		Other assets
		Liabilities to banks
		Liabilities to clients
		Securitised liabilities
		Liabilities relating to disposal groups
		Subordinated capital
	FVPL Other	Cash reserve
		Loans and advances to banks
		Loans and advances to customers
		Compensation item for financial instruments categorised as FVPL under the second loss guarantee
		Financial investments
		Non-current assets held for sale and disposal groups
		Other assets
	n/a	Positive fair values of hedging derivatives
		Negative fair value of hedging derivatives
Off-balance-sheet transactions	n/a	Contingent liabilities
		Irrevocable loan commitments
		Other obligations

Measurement method	Categories	
	IAS 39 category	Statement of financial position item/sub-item
Financial instruments measured at amortised cost	Loans and receivables (LaR)	Cash reserve
		Loans and advances to banks
		Loans and advances to customers
		Financial investments
		Non-current assets held for sale and disposal groups
		Other assets
	Other liabilities (LIA)	Liabilities to banks
		Liabilities to clients
		Securitised liabilities
		Liabilities relating to disposal groups
		Subordinated capital
		Other liabilities
Financial instruments measured at cost	Available for Sale (AfS)	Financial investments
		Non-current assets held for sale and disposal groups
		Other assets
Financial instruments measured at fair value	Held for Trading (HfT)	Trading assets
		Credit derivative under the second loss guarantee
		Non-current assets held for sale and disposal groups
		Trading liabilities
		Liabilities relating to disposal groups
	Designated at Fair Value (DFV)	Loans and advances to banks
		Loans and advances to customers
		Financial investments
		Non-current assets held for sale and disposal groups
	Available for Sale (AfS)	Cash reserve
		Loans and advances to banks
		Loans and advances to customers
		Financial investments
		Non-current assets held for sale and disposal groups
	n/a	Positive fair values of hedging derivatives
		Negative fair value of hedging derivatives
Financial instruments measured on the basis of other standards	n/a	Receivables under finance leases
Off-balance-sheet transactions	n/a	Contingent liabilities
		Irrevocable loan commitments
		Other obligations
	IFRS 9 category	
Financial instruments measured at fair value	FVPL Designated (FVPL DFP)	Liabilities to banks
		Liabilities to clients
		Securitised liabilities
		Liabilities relating to disposal groups
		Subordinated capital

C) MODIFICATIONS

If a financial instrument, in particular a loan, is altered in its contractual components, then Hamburg Commercial Bank assesses whether this change results in the disposal of the financial instrument, leading to the derecognition of the previous, and the recognition of a new, financial instrument at fair value (substantial modification) or whether, based on the modified contractual cash flows, the gross carrying amount is to be recalculated and a modification result recognised (non-substantial modification).

The result of a non-substantial modification corresponds to the difference between the gross carrying amount immediately prior to the modification and the recalculated gross carrying amount. The modification gain or loss is recognised within loan loss provisions in the statement of income.

Hamburg Commercial Bank has included guidelines in its written regulations regarding how to distinguish between substantial and non-substantial modifications. These stipulate that both qualitative criteria, such as a change in currency or a significant change in Hamburg Commercial Bank's risk position, and the 10 % net present value test as a quantitative criterion are to be used. This test involves comparing the net present value of the contractual cash flows before and after every modification of contractual components. If they differ by 10 % or more, then this is deemed to constitute a substantial modification.

D) LOAN LOSS PROVISION AND IMPAIRMENT OF FINANCIAL INSTRUMENTS

The calculation of loan loss provisions and impairments in accordance with IFRS 9 uses a model that is based on the calculation of expected credit losses. The scope of the model includes financial instruments that are recognised at amortised cost or at fair value through other comprehensive income, irrevocable loan commitments and financial guarantees that are not recognised at fair value through profit or loss, leasing receivables and contract assets.

The basic principle of the model relates to the creation of loan loss provisions depending on changes in the credit quality of the financial instrument since initial recognition over the term. Depending on the extent of the change in credit quality, the financial instrument is assigned to one of the following three levels:

a. Level 1: No significant increase in the loan default risk, 12-month expected loss

For financial instruments whose loan default risk is not significantly increased, the portion of expected credit losses that is attributable to defaults within the next twelve months is recognised under loan loss provisions.

b. Level 2: Significant increase in the loan default risk, lifetime expected loss

For financial instruments whose loan default risk has increased significantly since the time of initial recognition, expected credit losses are recognised over the entire remaining term of the financial instrument.

c. Level 3: Financial assets that are credit-impaired, lifetime expected loss

Financial instruments for which one or more events have occurred that have an adverse impact on the expected future cash flows are assigned to level 3.

Input parameters, assumptions and methods for calculating expected credit losses at levels 1 and 2

Expected credit losses at levels 1 and 2 are calculated based on the following credit risk parameters:

- Probability of default (PD)
- Loss given default (LGD)
- Exposure at default (EAD)

The internal credit risk models which – where necessary – are expanded to include forward-looking information are taken as a basis in this regard.

In the context of credit risk modelling, the default risk over a certain period is described by the PD. In order to assess the loan default risk associated with financial instruments or debtors, specific rating procedures are used that allow statements to be made on the probability of default within one year. As part of the development and validation of these procedures, a check is performed, on the basis of historical observations for different pieces of qualitative and quantitative information, to determine whether these explain the default risk as risk drivers. Using the rating procedures modelled on the basis of historical information, current and forward-looking information on the risk drivers can be condensed to arrive at a preliminary rating as part of the rating process. This information is then adjusted to include assessments of the debtor's creditworthiness to arrive at a final rating.

The rating classifications resulting from rating procedures each correspond to a specific 12-month PD which is used to calculate the loan loss provisions at level 1. At level 2, the 12-month PD is adjusted over a multi-year horizon to arrive at lifetime PDs on the basis of migration matrices. The migration matrices used reflect the observed rating migrations of debtors within a year and are calculated based on an extensive cross-economic historical observation period. The 12-month and lifetime PDs calculated in this manner are enhanced to reflect macroeconomic information where necessary. This involves aggregating internal and external macroeconomic forecasts to arrive at economic scenarios that are used as standard for various bank functions. The impact of the scenarios on the PDs is determined using statistical methods.

The LGD describes the amount of the loss expected in the event of default. Statistical procedures are used, on the basis of historically measured losses, to estimate expected recovery ratios from the realisation of collateral and collection ratios for unsecured loan portions. Together with the market value of the collateral and the amount of the claim, this produces the LGD for the financial instrument in question that is used to calculate the loan loss provisions for level 1. The LGD includes not only the collateral relevant to the financial instrument in question, but also transaction-specific and debtor-specific information such as the seniority of the financial instrument or the debtor's sector. By way of derogation from this type of LGD modelling, procedures based on the simulation of cash flows from the financed object are used for project, ship and aircraft financing. The forward projection of the LGD over the multiannual period is based primarily on the expected collateralisation ratio of the financial instrument, which comprises the expected collateral value and the expected amount of the receivable. The estimate of the collateral value takes into account both expected ageing effects associated with the collateral and forecasted macroeconomic developments, such as property prices, which influence the collateral value. The receivable amount is influenced by repayment and amortisation effects.

The EAD represents the outstanding receivables volume of the financial instrument at the time of default. For the balance sheet business, the outstanding receivables volume corresponds to the gross carrying amount calculated using the effective interest method. As part of EAD modelling, the balance sheet gross carrying amount is adjusted over a 12-month period (level 1) or over a lifetime horizon (level 2) to reflect amortisation and repayment effects. Within this context, fixed cash flows that have been contractually agreed and expectations regarding the exercise of options and their impact on the cash flows are taken into account. The impact of optionalities is determined both on the basis of historical information and on the basis of financial mathematical methods. The gross carrying amounts adjusted in this way over the term are grouped to form an average EAD for each year.

For the off-balance-sheet business in the form of irrevocable loan commitments and financial guarantee contracts, the EAD constitutes the expected future utilisation of the financial instrument up until the time of default. The borrower's expected drawdown behaviour within a year prior to the default event is reproduced via the credit conversion factor (CCF). The EAD for level 1 is calculated by multiplying the CCF by the line that is open on the reporting date. In order to calculate the EAD at level 2, the drawdown behaviour several years prior to the default is also calculated based on drawdown rates. The drawdown rates are modelled subject to the proviso that no default occurs within a year. The multi-year EAD for the year in question for level 2 is calculated by combining the expected drawdown one year before the assumed default event based on the CCF by the expected drawdown behaviour based on the drawdown rates for the prior years.

When calculating expected credit losses, Hamburg Commercial Bank takes into account the maximum contractually agreed term during which the Bank is exposed to a credit risk. Debtor extension options are also taken into account. Longer terms are not taken into account even if this is in line with standard business practice.

One exception relates to current accounts and framework facilities for which there is no set term or repayment structure and in respect of which the Bank does not enforce its option of forcing immediate repayment in daily management. The calculation of the expected losses for these financial instruments is based on the behavioural term. The behavioural term is derived from the existing Credit Risk Management processes that serve to minimise the credit risk. At Hamburg Commercial Bank, a debtor's credit quality is monitored on a regular and ad hoc basis and, if necessary, corresponding credit risk-mitigating measures are taken. As a result, the average monitoring interval is used as the estimate for the behavioural term.

Expected credit losses are calculated at the level of the individual financial instrument. Groups of financial instruments with risk features in common are not grouped for the purposes of calculating the loan loss provisions. The 12-month expected loss is calculated by multiplying the (one-year) credit risk parameters. The lifetime expected loss is calculated by multiplying the period-specific credit risk parameters determined during the term. Discounting to the balance sheet date is based on the effective interest rate in each case.

Incorporation of forward-looking information
Hamburg Commercial Bank uses the same economic forecasts for planning, internal control and loan loss provisions. As at each quarter end date, forecasts for selected parameters are prepared in three scenarios: base, stress and upside. The forecast horizon comprises the current reporting year-end and the next two years. The base scenario reflects the development that is deemed most likely to occur. This can be both an economic upswing and an economic downturn. The other two scenarios reflect more optimistic (upside) or more pessimistic (stress) developments in relation to the base scenario.

The scenario estimates are based on internal Bank economic forecasts, which are discussed within the affected areas, taking into account the forecasts of the Bundesbank and the ECB, as well as Bloomberg consensus estimates. Segment-specific parameters are added to these scenarios.

The estimated parameters cover forward-looking information in the following areas:

- Economy (gross domestic product and inflation rate for various regions)
- Direction of interest rates
- Movement in exchange rates
- Bond market (in particular corporate spreads)
- Oil prices
- Share prices
- Shipping (in particular charter rates and second-hand prices)
- Real estate prices (broken down by location and type of property)
- Aviation

The impact of this forward-looking information on the credit risk parameters PD and LGD is determined using statistical procedures and is taken into account when calculating the expected credit losses. Within this context, PD and LGD are adjusted to reflect base scenario forecasts. Regular checks are also performed to see whether other scenarios have a material non-linear impact on the amount of loan loss provisions. Within the context of what are known as model overlays, risk factors relevant to valuation are taken into account if they were not already included in the calculation parameters used in the models. In this case, the loan loss provisions are corrected either directly or indirectly by altering the credit risk parameters to reflect these effects.

Significant increase in the loan default risk

In order to assess a significant increase in the loan default risk associated with a financial instrument, Hamburg Commercial Bank uses internal ratings. Within this context, Hamburg Commercial Bank constantly furnishes proof that the change in rating and corresponding change in the 12-month PD takes the main risk drivers into account that lead to the change in the lifetime PD, meaning that changes in rating constitute a suitable assessment criterion for the level allocation. The rating of modified financial instruments is determined based on the adjusted conditions.

At Hamburg Commercial Bank, the assessment object that is relevant for the purposes of allocating financial instruments to specific levels is the individual financial instrument as a general rule. The rating of the corresponding debtor that applies at the time of addition is allocated to each financial instrument. One exception relates to securities for which different purchases of the same security are assessed jointly. This involves dividing the purchases in terms of similar credit quality at the time of initial recognition. The securities are then categorised at the level of the ISIN based on the best initial securities rating.

The extent giving rise to a significant deterioration in credit quality (significance threshold) is determined for each portfolio or rating category segment in a manner that is specific to the initial rating and on the basis of a quantile assessment. The outcome shows rating changes as of which the credit quality is deemed to have deteriorated significantly.

The rating expected, based on the time at which a financial instrument was recognised for the first time, for the balance sheet date in question serves as a benchmark for assessing a significant deterioration in credit quality. The expected rating is compared with the current rating to determine whether the change in rating that is defined as significant is exceeded. If this is the case then the financial instrument in question is allocated to level 2. Otherwise, it remains in level 1.

In addition, financial instruments are allocated to level 2 at the latest if forbearance measures have been applied to the financial instrument or if the default has lasted more than 30 days.

The Bank does not make use of the option set out in IFRS 9.5.5.10, which allows financial instruments with a loss risk of loan default to be assigned to level 1. Nor does it make use of the option provided for in IFRS 9.5.5.15 on the constant recognition of loan loss provisions in the amount of the lifetime expected loss for trade receivables, leasing receivables and contract assets.

A financial instrument is transferred from level 2 to level 1 if the loan default risk is no longer significantly increased based on the rating.

Definition of default

The rating models used by Hamburg Commercial Bank have been developed based on the definition of "default" set out in Art. 178 CRR and are validated in this respect on a regular basis. The definition of default is used as standard for internal Credit Risk Management and for supervisory law and IFRS 9 purposes.

The default definition includes the criteria "90 days in arrears" and "unlikeliness to pay".

Based on the “90 days in arrears” criterion, a debtor is deemed to have defaulted if a significant part of its total liabilities is past due on 90 consecutive days, The 90-day period starts on the first calendar day after this is identified. All calendar days are deemed to constitute overdraft days.

The “unlikeliness to pay” criterion is deemed to be satisfied if Hamburg Commercial Bank assumes that there is a high degree of probability that the debtor will not be able to meet his obligations in full unless certain measures are taken. The measures to be taken into account include, in particular, the setting up of loan loss provisions, the opening of, or filing for, insolvency proceedings, the realisation of collateral, deferrals of interest and/or principal payments, restructuring measures.

Financial assets that are credit-impaired within level 3
Differentiating level 3 of the impairment model involves assessing, on each balance sheet date, whether there are objective indications of an impairment that could have a detrimental impact on the expected future cash flows from the financial instrument.

The criteria for impairment are consistent with those that apply to supervisory law default and essentially include major financial difficulties for the borrower and indications that, based on current information, interest payments cannot be made and an improvement in the financial situation cannot be demonstrated. In the case of securities, an initial check is performed as to whether the market value has decreased in the last twelve months, either permanently by at least 10 % or once in the last six months by 20 % below the cost of acquisition.

If one of these criteria is met, they are checked as part of a multi-step risk assessment process to see if there are any indicators for impairment. An indicator for an impairment of a security is, for example, a downgrade to non-investment grade. Where a security is already non-investment grade and the rating deteriorates by another three categories, this would be another indicator.

Loans and securities with objective evidence of impairment are accounted for by setting up specific loan loss provisions for the receivable in question. To calculate the amount of the specific loan loss provision, the net present value of the anticipated cash flows arising from the loan or advance – that is achievable amount – is compared to its carrying amount. The anticipated cash flows may comprise capital repayments, interest payments or the proceeds from disposal of collateral less liquidation costs. The realisable amount is calculated using various scenarios and compared against the carrying amount. If the carrying amount is higher than the realisable amount for the scenario in question, then this scenario results in a loss in the amount of the difference. The specific loan loss provision is set up in the amount of the average losses from among the various scenarios, weighted to reflect the probability of occurrence.

Assessments as to the need for loan loss provisions are frequently made on the basis of information which is partly provisional in nature (e.g. planned restructuring of borrowers, draft reorganisation reports) or are subject to increased volatility (e.g. collateral value of real estate and ships). This results in increased uncertainty regarding estimates of key parameters of loan loss provisions. In such cases the large degree of uncertainty is mainly due to the assessment of expected cash flows which are dependent on borrowers, industries, the assessment of the overall economy among other factors. The assumptions made are subject to a periodic review and are adapted to the changed underlying conditions where necessary

If the estimate of the expected cash flows leads to the complete reversal of a debtor’s specific loan loss provisions, the sustainability of the debtor’s recovery must be determined: a recovery is only deemed to have occurred after various conditions have been fulfilled. These include the condition that the “90 days in arrears” and “unlikeliness to pay” criteria no longer apply, the reversal of the setting of transactions to a non-accrual basis and measures to make up for the debt servicing that was not provided during the default period. In addition, a good conduct period must be observed, which may extend over a period of 12 months or involve payment in accordance with the contract on six consecutive dates.

Recognition of impairment losses in the balance sheet
As the recognition of the impairment depends on the category of financial assets, the following distinctions must be made with regard to measurement:

a. Financial instruments which are measured at amortised cost

Impairments to loans and advances to banks and customers are recorded in separate loan loss provision accounts under the item Loan loss provisions. Loan loss provisions thus created are written off at the time when the amount of the actual default of the receivable is determined or the receivable defaults. Irrecoverable receivables for which no specific loan loss provisions existed are written off directly as is the case for losses in the case of impaired receivables which exceed the recorded loan loss provisions.

b. Financial instruments which are measured at fair value in OCI and are not recognised in the statement of income

In cases involving these financial instruments, the cumulative income previously recognised in equity is reclassified to profit or loss.

If the reasons for impairment no longer apply, a reversal of the write-down up to the amount of amortised cost is made in profit or loss. The effect of the change in fair value is recognised directly in equity in the revaluation reserve in other comprehensive income (OCI).

c. Purchased or originated credit-impaired financial assets (POCI)

Financial instruments that are purchased or originated credit-impaired are assigned to a separate level. The criteria for classification as purchased or originated credit-impaired are the same as for general classification. The general approach pursuant to IFRS 9.5.5.1 does not apply to these financial instruments. No loan loss provisions are set up through profit or loss at the time of initial recognition. The subsequent measurement reflects changes in the cash flows expected by the lender, taking into account the expected loan losses in subsequent periods through profit or loss as loan loss provisions. Reversals of impairment losses are also to be reflected in loan loss provisions. The loan losses expected at the time of initial recognition are distributed over the term of the loan using the credit-adjusted effective interest rate. If the debtor recovers, the debtor is still to be allocated to the level in question. In such cases, however, the calculation method is based on the standard credit risk parameters.

For the off-balance-sheet business, expected losses are also calculated on the basis of the three-stage model and recognised as provisions in the lending business.

E) DETERMINING FAIR VALUE

Under IFRS 13 the fair value represents the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. The fair value of financial instruments is determined on the basis of the listed price on an active market (mark-to-market), or if this is not possible on the basis of recognised valuation techniques and models (mark-to-matrix or mark-to-model). Irrespective of whether and to what extent the inputs applied in determining the fair value are observable in the market, financial instruments are assigned to one of the three fair value hierarchy levels as defined in IFRS 13.

Fair value can be determined using the mark-to-market method if a market price is available at which a transaction could be entered into or has been entered into for a similar financial instrument as at the measurement date. This is generally the case for shares traded on liquid markets. Such an unadjusted market price at the measurement date for the identical instrument is classified as level 1 of the valuation hierarchy under IFRS 13.

If such a market price is not available for the identical instrument, the measurement is carried out using valuation techniques or models.

VALUATION TECHNIQUES AND MODELS

When using valuation techniques the market approach is the preferable method for determining the fair value. The fair value is determined to the extent possible on the basis of prices that come from transactions executed on the measurement date. If the fair value cannot be determined from market or transaction prices for the identical financial instrument, prices of comparable financial instruments or indices, which are representative for the financial instrument, are used as an alternative and adjusted where necessary (mark-to-matrix method). The fair value is assigned to level 2 of the fair value hierarchy if the adjustment to the prices or parameters observable in the market is not material. However, if the adjustment is material and affects unobservable inputs, the fair value is assigned to level 3.

The fair value is determined based on the income approach using a valuation model if the market approach using the mark-to-market or mark-to-matrix method is not possible or is not of sufficient quality. Where available, inputs observable in the market as well as quality assured market data from appropriate pricing agencies or also validated prices from market partners (arrangers) are also used as a primary source for model valuations. Fair values determined by means of model valuations, for which only observable inputs are used or which are only based to an insignificant extent on unobservable inputs, are assigned to level 2 of the fair value hierarchy. If the fair values determined using valuation models are based to a significant extent on unobservable inputs, they are assigned to level 3 of the fair value hierarchy.

The fair value of receivables and liabilities measured at amortised cost is mainly determined by discounting the contractual future cash flows of the financial instruments. In the case of receivables with a default rating, the fair values are determined based on the still to be expected future cash flows.

VALUE ADJUSTMENTS

If the value of a financial instrument measured at fair value as determined by a valuation technique or model does not take adequate account of factors such as bid-offer spreads or closing costs, liquidity, model risks, parameter uncertainties and credit and/or counterparty default risks, the Bank makes corresponding valuation adjustments, which a purchaser of similar positions would also take into account. The methods applied for this draw to some extent on unobservable market parameters in the form of estimates.

Funding costs and benefits arise on the hedging of the risks relating to an uncollateralised OTC derivative with a collateralised OTC derivative. A funding valuation adjustment is determined as part of the method used to determine fair values for derivatives and is included in the fair value of the uncollateralised OTC derivative for funding costs/benefits arising on the provision or receipt of collateral due to the hedging asymmetry of the derivatives.

Hedge relationships (back-to-back transactions) and corresponding risk-compensating effects are taken into account when determining value adjustments to be made for model risks and uncertainties regarding parameters. The value adjustment for the credit risk is determined for OTC derivatives at the level of a group of financial instruments of a business partner (so-called portfolio-based valuation adjustment). This is permitted if the conditions stipulated in IFS 13.49 for a portfolio-based measurement are met.

The portfolio-based valuation adjustment for the credit risk is allocated to assets or liabilities in proportion to the fair value of the asset or liability respectively before the valuation adjustment is taken into account. Allocation only takes place to the assets or liabilities depending on whether there is an excess of assets or liabilities (so-called "relative fair value approach" – net approach).

DAY ONE PROFIT AND LOSS

The use of a valuation model may give rise to differences between the transaction price and the fair value determined using such a valuation model on the initial recognition date. If the applicable market on which the determination of the fair value is to be based differs from the market, in which the transaction was concluded and the valuation model is not based to any great extent on observable parameters, such differences (so-called day one profits and losses) are accrued to day one profit and loss reserve. This reserve is reversed over the term. Implicitly, the time factor is thereby considered significant to the difference accrued and is taken into account accordingly, and it is assumed that this is also the procedure that would be followed by a third-party market participant in its pricing.

MEASUREMENT PROCESSES

The Bank has implemented various processes and controls for the purpose of determining the fair values of financial instruments and has embedded principles regarding the use of measurement methods in a guideline in the written rules of procedure. These measures also ensure that financial instruments to be assigned to level 3 of the fair value hierarchy are measured in accordance with IFRS 13. The Group Risk Management division, which is independent from the Bank's market departments, is responsible for ensuring that the measurement methods applied are in accordance with external accounting requirements. Information available on the methods applied by other market participants is also taken into account in this regard.

Fair values of financial instruments assigned to level 3 are determined again on a periodic basis – but at least on a monthly basis. Any changes in value that have occurred since the previous period are reviewed for plausibility. Where available, observable market information such as transaction prices or attributes of valuation parameters are also used in the internal price validation. If there are material differences between the fair values determined by the Bank and prices offered by counterparties, the valuation model used is subjected to an ad hoc validation process.

F) HYBRID FINANCIAL INSTRUMENTS

The term "hybrid financial instruments" covers silent participations and bonds issued by consolidated subsidiaries measured at amortised acquisition cost. A key common feature of these instruments is that their interest depends on profit and they participate in an annual net loss of the Bank.

IFRS 9.B5.4.6 states that for financial instruments, not to be measured at fair value, the carrying amount of financial assets and liabilities must be adjusted and recognised in profit or loss if the estimated future cash flows associated with the instrument change. The new gross carrying amount is given by the present value of the newly estimated future cash flows using the financial instrument's original effective interest rate for discounting.

Application of IFRS 9.B5.4.6 had an effect in the year under review on the valuation of the hybrid financial instruments issued by Hamburg Commercial Bank, as the actual and the estimated future cash flows differ from the contractual cash flows that were originally intended.

The future cash flows, whose amount and payments dates have to be estimated, are payments of interest and principal which take into account loss participations by investors, where these will not be made up for by the expected redemption date of an instrument.

The loss situation of the reporting period is not viewed in isolation on the measurement of hybrid instruments in accordance with IFRS 9.B5.4.6. Specifically, it involves more than assigning the prorated loss in the period under review. In addition, the possible effects of possible future assignment of loss and the cancellation or postponement of future interest payments must be recognised in profit or loss in the period in which the estimate is changed. This can mean that in future loss-making periods no further loss participations will be recognised in profit or loss, if these future losses correspond to the estimates made previously. The loss participation recognised in profit or loss is accordingly anticipated at present value, rather than being left to the period in which the loss arises. Future loss-related reductions in interest also do not result in full relief to interest expenses, if the reduction in interest has already been taken into account in the estimate. Instead, the reversal of the effect of discounting applied in the year the estimate was changed is recognised in expenses (write-up of the liability due to the passage of time).

The estimation of future cash flows from hybrid financial instruments required in applying IFRS 9.B5.4.6 requires material assumptions which are associated with uncertainties. The assumptions made are subject to a periodic review and are adapted to the changed underlying conditions where necessary The main sources of estimation uncertainty are the assumptions and results of Hamburg Commercial Bank's business planning.

Net income from hybrid financial instruments is shown as a separate item under Net interest income, and in addition to current interest expenses it includes the effects of applying IFRS 9.B5.4.6 (see Note 8). Deferred taxes arise because of the difference between valuation for tax purposes and measurement in the Group financial statements. The associated effects on net income are recognised under income taxes. Hybrid financial instruments are shown either as securitised liabilities or as subordinated capital (see Notes 39 and 47).

G) HEDGE ACCOUNTING

Hamburg Commercial Bank makes use of the option provided for in IFRS 9 of continuing with portfolio fair value hedge accounting subject to the provisions set out in IAS 39. Changes in the value of items in the IFRS 9 measurement categories AC and FVOCI are not recognised through profit or loss. Changes in the value of derivatives are always recognised in profit or loss. If underlying transactions that are not recognised at fair value through profit or loss are hedged by derivatives, this creates a mismatch relating to the measurement/presentation of the results in the statement of income, which does not reflect the economic facts. One way of avoiding these distortions is to use fair value hedge accounting. In fair value hedge accounting, the changes in value of hedged items which are attributable to the hedged risk are recognised in profit or loss.

Hamburg Commercial Bank uses derivatives to hedge market risks resulting from loans, issues and securities portfolios. Individual loans, issues and securities items as well as entire portfolios of such financial instruments are hedged in this way.

The Bank uses portfolio fair value hedge accounting to account for portfolio-based hedging relationships in order to avoid distortions in the statement of income. Currently only hedges of fair value against interest rate risk are taken into account. Fixed-interest rate loans, issued instruments and securities positions are designated as underlying transactions (hedged items), while only interest rate and cross currency interest rate swaps are designated as hedging instruments.

Where portfolios comprising lending, issuing or securities transactions are hedged by derivatives with non-Group counterparties and this hedging arrangement satisfies the requirements of IAS 39, portfolio fair value hedge accounting is applied. In the case of portfolio fair value hedge for interest rate risks, portfolios of assets and liabilities hedged for interest rate risks are taken into account. This involves an iterative procedure. At the start of a hedging period, the financial instruments in the portfolios are allocated to maturity ranges on the basis of their anticipated maturity or interest adjustment dates, and the hedged amount is then determined for each maturity range. The hedging transactions are also allocated at the start of the hedging period. At the end of the hedging period, the hedge is recognised and measured and a new hedge is designated. The changes in the fair values of the hedged amounts of the underlying transactions due to the hedged risk are recognised in a separate item in the statement of financial position (asset or liability reconciling items from the portfolio fair value hedge). The fair value changes which are not attributable to the hedged risk are treated in accordance with the general rules for the corresponding IFRS 9 category.

Using fair value hedge accounting requires a series of conditions to be met. These principally relate to the documentation of the hedge and its effectiveness. Hamburg Commercial Bank documents all hedging relationships in accordance with the requirements of IAS 39, including the hedging instrument, the hedged item (underlying transaction), the hedged risk and the result and method of measuring effectiveness.

Future changes in value of underlying and hedging transactions are simulated using a regression model within the framework of the prospective effectiveness test. Any actual changes in value are used in retrospective effectiveness testing. Hamburg Commercial Bank uses the dollar offset method for the retrospective effectiveness measurement. This tests whether the relationship between the changes in value of underlying and hedging transactions lies within an interval of 80 % to 125 %.

Changes in value of underlyings and hedging transactions in effective hedges which are attributable to the hedged risk are recognised in the Result from hedging.

Income and expenses from the amortisation of reconciling items for the fair value hedge portfolio and proceeds from the closing of the underlying transactions which contributed to reconciliation items are reported as part of the Net interest income.

H) DERECOGNITION

A financial asset is derecognised when all material risks and opportunities associated with ownership of the asset have been transferred, i.e. when contractual claims on cash flows from the asset have been extinguished. Where not all risks and opportunities are transferred, Hamburg Commercial Bank carries out a control test to ensure that no continuing involvement due to opportunities and risks retained prevents it from being derecognised. Financial assets are also derecognised if the contractual rights to cash flows have expired. Financial liabilities are derecognised when they are repaid, i.e. when the associated liabilities are settled or lifted or when due respectively. If the material contractual elements of an asset or liability are altered, this also results in a derecognition.

I) REPURCHASE AGREEMENTS AND SECURITIES LENDING TRANSACTIONS

Hamburg Commercial Bank only enters into genuine repo transactions. Genuine repo transactions, repo agreements or sell-and-buy-back transactions combine the spot purchase or sale of securities with their forward sale or repurchase, the counterparty being the same in both cases.

For genuine repo transactions with assets sold under repurchase agreements, the securities continue to be recognised by Hamburg Commercial Bank, as the interest, credit rating and other material risks associated with the securities continue to be borne by Hamburg Commercial Bank. According to counterparty, the inflow of liquidity from the repo transaction is shown in the statement of financial position as a liability either to banks or customers. Interest payments are recognised under interest expense over the term of the transaction. Outflows of liquidity caused by reverse repos are reported as loans and advances to banks or customers. Correspondingly, the securities bought under repurchase agreements are not carried or measured in the statement of financial position. Agreed interest payments are booked as interest income over the term of the transaction. Receivables arising from repos are not netted against liabilities from repos involving the same counterparty, since the criteria for netting are not met.

The emphasis in repo transactions is on bonds from German public sector issuers and from bank issuers and the Bank's own bonds. Securities lending transactions are carried on the statement of financial position in a similar way to genuine repurchase agreements. Lent securities remain in the securities portfolio, while borrowed securities are not capitalised on the statement of financial position. Cash collateral furnished for securities lending transactions is shown as a receivable, while collateral received is shown as a liability. Repo and securities lending transactions are carried out primarily in bonds.

J) FINANCIAL GUARANTEE CONTRACTS

Pursuant to the definitions set out in IFRS 9, a financial guarantee is a contract that requires the issuer of the contract to make specified payments to reimburse the holder of the contract for the loss that the holder incurs because a specified debtor fails to make payment when due under the original or amended terms of a debt instrument. A credit derivative is treated as a financial guarantee if the requirements set out in IFRS 9 are met. Credit derivatives that do not meet the definition of a financial guarantee are allocated, in accordance with the general valuation rules, to the FVPL Trading category and are measured at fair value.

Financial guarantees at Hamburg Commercial Bank are provided in the form of warranties, bank guarantees and letters of credit. Corresponding contingent liabilities are based on past events that may result in possible liabilities in the future. These liabilities arise as a result of the occurrence of unspecified future events where the amount required to meet them cannot be estimated with sufficient reliability. Financial guarantees are recognised at the higher amount resulting from the calculation of the expected losses in accordance with the impairment provisions set out in IFRS 9 and the premium capitalised at the time of initial recognition, which corresponds to the fair value, less the cumulative earnings contributions recognised in accordance with IFRS 15, with provisions having to be set up if necessary.

If the premium payment to Hamburg Commercial Bank is distributed over the term of the financial guarantee, the guarantee will be stated as zero and the premium payment recognised on an accrual basis. If Hamburg Commercial Bank is the holder of a contract, the financial guarantee will be presented as collateral for the Group.

II. Notes on selected items relating to financial instruments in the statement of financial position

CASH RESERVE

Cash on hand, balances with central banks, treasury bills and discounted treasury notes are stated under cash reserve.

The instruments reported under this item are allocated to the holding categories AC HTC, FVOCIR HAS and FVPL RES within Hamburg Commercial Bank under IFRS 9 and are measured accordingly.

RECEIVABLES

Loans and advances to banks and customers mainly comprise money market transactions, loans and promissory note loans, but also securities which are registered securities and non-negotiable bearer debentures. Financial assets are allocated to the AC HTC, FVOCIR HAS and FVPL RES, FVPL DFV, FVPL HAS and FVPL HTC holding categories, resulting in the corresponding subsequent measurement.

Loans and receivables in the “AC assets” reporting category are reported in gross terms, i.e. before the deduction of impairments. Impairments are shown in the separate item Loan loss provisions, which is shown under Loans and advances as a deduction. Financial instruments in the FVPL Other, FVPL Designated and FVOCI Mandatory reporting category are reported in net terms. Accrued interest is also allocated to this item in the statement of financial position. Where loans and receivables have been acquired or incurred with the intention of trading, they are stated under trading assets.

Depending on their classification, interest income from loans and advances to banks and customers is recognised under interest income from AC and FVOCI financial assets or interest income from other financial instruments, lending and money market transactions. Premiums and discounts are accrued using the effective interest rate method.

If, in the case of non-genuine securitisation transactions, loans and advances are not derecognised and the risk on such loans and advances remains fully with Hamburg Commercial Bank, any necessary loan loss provisions are recognised solely on our original loans and advance amounts.

POSITIVE AND NEGATIVE MARKET VALUE OF HEDGING DERIVATIVES

This item shows the market value of derivatives which have a positive or negative fair value and which are used in hedge accounting. Only interest rate and cross currency interest rate swaps are taken into account as hedging instruments currently. If a derivative is only partially designated under hedge accounting, this item contains the corresponding share of that derivative’s fair value. In these cases, the remainder is stated under Trading assets or Trading liabilities.

RECONCILING ASSET AND LIABILITY ITEMS FROM THE FAIR VALUE HEDGE PORTFOLIO

The asset-side reconciling item from portfolio fair value hedge accounting contains the value change of the hedged object to be attributed to the hedged risk from portfolio fair value hedges for assets. Similarly, the liability-side reconciling item from portfolio fair value hedge accounting contains the value change of the hedged object to be attributed to the hedged risk from portfolio fair value hedges for liabilities.

TRADING ASSETS AND TRADING LIABILITIES

Only financial assets in the FVPL HFT holding category are reported under Trading assets. These include primary financial instruments held for trading purposes, particularly fixed income securities and pro rata interest, and also equities and other trading portfolios such as precious metals. Loans and loan commitments with hard syndication conditions are also reported here. A significant component continues to be derivatives with a positive market value which are either trading derivatives or not designated as a hedging derivative because they do not meet the requirements of hedge accounting.

The valuation results from changes in fair value are recognised in the Result from financial instruments categorised as FVPL. Interest income and expenses, as well as dividend income, is recognised as Net interest income and commission income and expenses are recognised in Net commission income.

In a similar way to trading assets, trading liabilities only include financial obligations belonging to the FVPL HFT holding category, which includes derivatives with a negative market value which are either trading derivatives or which have not been designated as hedging derivatives because they do not meet the requirements of hedge accounting. Delivery commitments from short sales of securities and pro rata interest from these are also stated in this category.

FINANCIAL INVESTMENTS

Financial investments include all securities not acquired for trading purposes (debentures and equities) and equity holdings under commercial law. The equities and equity holdings are mainly categorised as FVPL RES. The dominant business model for debentures is Hold & Sell, meaning that most of them are categorised as FVOCIR HAS.

The products included in this item include fixed-interest securities including accrued interest, equities and other non-fixed-interest securities, holdings in unconsolidated affiliated companies, and holdings in joint ventures and associates not carried at equity.

All realisation effects from FVOCIR HAS securities are reported in Net income from financial investments, while realisations of AC HTC securities are reported in the Result from the disposal of financial assets classified as AC. All valuation results associated with impairments in these two holding categories are shown under Loan loss provisions. The effects on earnings resulting from the measurement and disposal of FVPL items within financial investments are shown in the Result from financial instruments categorised as FVPL.

If a decision had been made on the disposal of financial investments and this disposal had been initiated as at the balance sheet date, and it is highly probable that it can be completed within the following 12 months, these financial investments are reclassified as "Non-current assets held for sale and disposal groups".

FINANCIAL INVESTMENTS ACCOUNTED FOR USING THE EQUITY METHOD

Shares in associates included in the Group financial statements under the equity method are reported in this item. Such ownership interests are measured in accordance with the guidelines of IAS 28 in conjunction with IFRS 11.

For the impairment testing of financial investments accounted for under the equity method the total carrying amount of the investment measured under the equity method is assessed for impairment as a single asset in accordance with IAS 36. Its realisable amount is always compared with the carrying amount for this purpose, if there are indications on applying IFRS 9 that the investment could be impaired.

The realisable amount is defined as the greater of fair value less costs to sell and value in use (for information on the calculation of the value in use, please refer to Note 7.III.01.).

LIABILITIES

Liabilities that are not instruments defined as trading liabilities include financial obligations in the "AC liabilities" and "FVPL Designated" reporting categories. As a result, the relevant holding categories are AC LIA and FVPL DFP. The relevant instruments are recognised as Liabilities to banks, Liabilities to customers, Subordinated liabilities and Securitised liabilities.

Financial liabilities are recognised at fair value at the time of issue plus transaction costs, which generally corresponds to the transaction price. In subsequent periods, debt classed as AC liabilities are measured at amortised cost applying the effective interest method. Changes in the value of these financial instruments are only recognised when the relevant instrument is sold. Differences between acquisition costs and the repayment amount (e.g. premiums and discounts) are allocated within Net interest income through profit or loss in line with the effective interest rate method. Valuation results resulting from financial instruments in the "FVPL Designated" reporting category are recognised in the Result from financial instruments categorised as FVPL.

Repurchased own debentures are set off against securitised liabilities. For repurchased debentures in the DFV liabilities holding category, the credit risk-induced valuation effects that could potentially be realised are also reported in the statement of changes in equity. Realisation does not take place immediately, because Hamburg Commercial Bank keeps the repurchased shares for renewed sale.

SUBORDINATED CAPITAL

Subordinated liabilities, silent participations and profit-sharing certificates are shown under Subordinated capital, due to their different nature compared with other liabilities. Silent participations are structured as so-called hybrid financial instruments without exception and so are some profit-sharing certificates (cf. Note 7.I.E). No obligation to other creditors for premature redemption of subordinated liabilities is possible. In the case of liquidation or insolvency, subordinated liabilities may only be repaid after the claims of all senior creditors have been met.

Based on their contractual structure and financial character, the participations of the typical silent partner represent debt, which is why they are stated under subordinated capital.

Subordinated capital categorised as AC liabilities is recognised and measured initially at fair value (taking the transaction costs into account) and at amortised acquisition cost subsequently. Premiums and discounts are allocated on a constant effective interest rate basis via Net interest income.

Valuation results resulting from subordinated capital in the "FVPL Designated" reporting category are recognised in the Result from financial instruments categorised as FVPL.

Current gains and losses from measuring subordinated capital categorised as DFV are stated under the revaluation reserve.

See Note 7.I.E. with regard to the treatment of hybrid financial instruments in the year under review.

III. Notes on other items in the statement of financial position

INTANGIBLE ASSETS

Software acquired or developed in-house and acquired goodwill are accounted for under Intangible assets. In accordance with IAS 38.21, Hamburg Commercial Bank capitalises software development costs if the production of the in-house software is likely to generate an economic benefit and the costs can be reliably determined. If the criteria for capitalisation are not met, expenses are recognised in profit or loss in the year they are incurred. Subsequent costs are only to be capitalised if they lead to a significant improvement of the software in the form of an expansion of the software's functionality. Since Hamburg Commercial Bank does not apply the full goodwill approach, goodwill arises on acquisition of subsidiaries, when the cost of acquisition exceeds the Group's share in the remeasured net assets (shareholders' equity) of the company acquired.

The initial measurement of intangible assets is made at acquisition or production costs in accordance with IAS 38.24. They are subsequently measured at amortised acquisition or production cost.

Software developed in-house is subject to linear depreciation over two to ten years.

If there are indications of impairment, intangible assets are subject to an impairment test. For this test the carrying amount of these intangible assets is compared with the realisable amount. The realisable amount is defined as the greater of fair value less costs to sell and value in use. An asset is impaired if its carrying amount exceeds its realisable amount. Intangible assets with an indefinite useful life, intangible assets not ready for use as well as goodwill are subject to an annual impairment test even if there are no signs which suggest impairment.

Examination of the value of goodwill is carried out on the basis of cash-generating units. Cash-generating units of Hamburg Commercial Bank for non-strategic investments are defined based on the internal management level (global head structure). Each global head unit forms an own cash-generating unit. A company is regarded as a non-strategic investment if underlying subsidiaries are integrally involved in the business activities of the respective global heads. However, if the value in use is expected to be realised by cash inflows or an increase in value of a subsidiary alone, then the subsidiary itself continues to be a cash-generating unit (so-called strategic investment). Where the anticipated benefit can no longer be determined, a write-down is made.

The value in use of a cash generating unit is determined on the basis of forecast and discounted net cash flows. Net cash flows are usually determined on the basis of Group planning for a detailed planning period of five years. For subsequent periods the planned cash flows of the last year of the plan are taken into account allowing for a growth trend. The planned cash flows are based on a risk-adequate discount rate.

PROPERTY, PLANT AND EQUIPMENT

Land and buildings, plant and equipment and leasing assets under operating leases where Hamburg Commercial Bank acts as lessor are stated under this item. Property, plant and equipment is stated at cost of acquisition or production less linear depreciation in line with its expected useful life. Subsequent costs of acquisition or production are capitalised provided they increase the economic utility of the asset concerned. Interest paid to finance acquisition costs of property, plant and equipment is recorded as an expense in the period concerned.

Physical wear and tear, technical obsolescence and legal and contractual restrictions are taken into consideration when determining useful life. For property, plant and equipment, linear depreciation is calculated over the following periods:

Classes of property, plant and equipment

	Useful life in years
Buildings	50
Leasehold improvements	Calculation of residual life is based on the remaining term of the rental agreement.
Other operating equipment	3–15
Leasing assets	Customary useful life

Property, plant and equipment is reviewed at each reporting date for signs which suggest impairment. If this is the case, the recoverable amount is compared with the carrying amount. If the carrying amount exceeds the recoverable amount, a write-down is recognised in profit or loss under administrative expenses.

Gains and losses from the disposal of property, plant and equipment are shown under Other operating income in the statement of income. Repairs, servicing and other maintenance costs are recorded as an expense in the period concerned.

INVESTMENT PROPERTY

Under the item Investment property properties are disclosed that are held to earn rental income or make capital gains but are not used for own operations. For mixed use properties a percentage allocation of the carrying amount is made. Owner-occupied properties are reported under Property, plant and equipment; rented-out or empty parts are reported as Investment property. The properties are recognised at acquisition cost and depreciated on a straight-line basis. A useful life of 50 years is used for depreciation purposes. At the balance sheet date, checks are performed to determine whether there are any indications of impairment. If this is the case, the recoverable amount is compared with the carrying amount. If the carrying amount exceeds the recoverable amount, a write-down is recognised in profit or loss under administrative expenses.

The capitalised income method is used in determining the fair value of investment properties, using market data from internal certified appraisers. The fair value is disclosed in Note 32.

NON-CURRENT ASSETS HELD FOR SALE AND DISPOSAL GROUPS AND LIABILITIES RELATING TO DISPOSAL GROUPS

Non-current assets whose carrying amounts will be predominantly or primarily realised through a sale and not through continuing use must be classified as held for sale in accordance with IFRS 5 on the condition that a sale has already been decided on and initiated as of the reporting date, and is extremely likely to be completed within the following twelve months.

A disposal group is a group of assets which are sold to the same purchaser in a single transaction and at a single price. A disposal group can also include liabilities, if these are taken over by the purchaser together with the assets. Hamburg Commercial Bank recognises as disposal groups and liabilities relating to disposal groups specifically the assets and liabilities of consolidated subsidiaries which meet the requirements of IFRS for classification as held for sale.

Non-current assets and disposal groups held for sale are to be measured at the lower of carrying amount or fair value less sale costs. Financial instruments continue to be measured according to the requirements of IFRS 9.

PROVISIONS

Provisions are created where the Group has existing legal and actual obligations resulting from previous events and it is likely that meeting the obligation will require an outflow of resources and a reliable assessment of the amount of the obligation can be made. Provisions are examined and redetermined at least quarterly.

Pension provisions

The majority of employees of Hamburg Commercial Bank AG as well as employees of several domestic subsidiaries are entitled to benefits from different staff pension plans, which include both defined contribution and defined benefit plans.

In the case of defined contribution plans, contractual relationships with Provinzial NordWest Lebensversicherung AG for direct insurance policies partly financed by employees exist. As the insurance company is required to be a member of Protektor Lebensversicherungs-AG, the insured employees are protected against its insolvency, meaning that Hamburg Commercial Bank AG is not burdened even in the event of Provinzial NordWest Lebensversicherung AG's insolvency. These direct insurance policies represent insured benefits and are treated as defined contribution plans.

In the case of the defined benefit plans, the amount of benefit depends on various factors, such as age, salary and length of service. Pension plans include specifically retirement and disability pensions and survivor benefits. They are based primarily on employment contracts of Landesbank Schleswig-Holstein Girozentrale, the retirement plan of Hamburgische Landesbank Girozentrale, retirement pension guidelines of the Hamburgische Landesbank Girozentrale relief fund, the pension plan of Hamburgische Landesbank Girozentrale and Section 2 (4) of the Investment Bank Act in the version of 23 January 1998. The pension payment amount depends on the final salary paid immediately prior to retirement, the salary trend up to retirement is irrelevant (no performance components). The pension plans provide for on-going pension payments and no capital payments. Minimum guarantees are not provided for. Pension provisions for defined benefit plans are equivalent to the net present value of the pension entitlements earned as of the reporting date, factoring in anticipated wage and salary increases and the trend in annuities. Calculations are based solely on actuarial reports based on IAS 19, which are prepared by independent actuaries using the projected unit credit method.

These defined benefit plans were closed in 2002.

Hamburg Commercial Bank AG also participates in a multi-employer plan which is run by BVV Versorgungskasse des Bankgewerbes e.V. Contributions are regularly paid with participation from the employees. The BVV tariffs provide for fixed pension payments with profit participation. For BVV, employers have a subsidiary liability for the liabilities of their employees. Hamburg Commercial Bank AG classifies the BVV plan as a defined-benefit joint pension scheme provided by a number of employers. As the BVV relief fund does not fully allocate its assets neither to the beneficiaries nor the member companies and as the information available for its accounting treatment as a defined benefit plan is insufficient to be able to allocate the assets and pension commitments to the current and former employees of the individual member companies, the plan is treated as a defined contribution plan for accounting purposes. It appears unlikely that there will be any call based on the statutory subsidiary liability.

The remeasurement of net defined benefit liabilities is disclosed under Other net income and under Equity in retained earnings in the year in which they arise. Pension provisions are discounted as long-term liabilities. The interest expense included in expense for retirement pensions is recognised as part of Net interest income.

The following assumptions are made in calculating direct benefit pension liabilities:

Actuarial assumptions

	2018	2017
Discount rate		
Domestic	2.13 %	1.87%
Foreign (weighted)	2.13 %	1.87%
Salary growth (weighted)	2.0%	2.0%
Adjustment rate for pensions		
Domestic		
Employment contract 1/ old pension provision rules	individual	individual
New pension provision rules (weighted)	2.0%	2.0%
Employment contract 4 (weighted)	2.0%	2.0%
Mortality, disability, etc.	Based on the 2018 G tables of K. Heubeck	Based on the 2005 G tables of K. Heubeck

Actuarial assumptions are subject to a sensitivity analysis as described in Note 42.

Defined benefit pension plans are partly financed from assets and qualified insurance policies used exclusively for pensions (plan assets). Plan assets are measured at fair value and recognised in the statement of financial position as reducing provisions.

Other provisions

Other provisions include provisions in the lending business, for restructuring, litigation risks and costs, for personnel expenses (without pensions) and other provisions.

Provisions in the lending business are created, among other reasons, for any sudden calls to pay under warranty bonds, guarantees and letters of credit. The parameters used for the calculation are presented in the section Loan loss provisions and impairment of financial instruments (Note 7.I.D).

Provisions for restructuring are created to the extent Hamburg Commercial Bank has developed and communicated a sufficiently detailed plan for such measures and had started to implement such plan. As soon as the obligation is sufficiently certain or can be quantified – e.g. through the signing of agreements – it is transferred to Other liabilities or Provisions for pensions and similar obligations as a matter of principle.

The ongoing expenses associated with the restructuring programmes initiated to date, as well as the expenses resulting from the provisions set up in connection with the Bank's restructuring, a resolution on which was passed in December 2018, are recognised in the statement of income under Net income from restructuring and privatisation. This item also includes the expenses incurred in connection with the privatisation of Hamburg Commercial Bank. The expenses incurred in the 2018 financial year are explained in more detail in Note 19.

Provisions for litigation costs comprise expected payments for court costs as well as for non-court costs in connection with litigation such as, e.g. attorneys' fees and other costs. For litigation in progress, only costs for the current jurisdictional level may be included within the provision.

Provisions for litigation risks are to be created when Hamburg Commercial Bank AG or any of its consolidated subsidiaries is the defendant in an action and the probability that the Bank will lose the action is presumed to be greater than 50 %. Provisions include only payments for probable liability for damages and fines as well as costs of litigation at the current level of appeal. The general measurement rules on provisions apply. The mandatory disclosures defined in IAS 37.86 are made for litigation risks that are not considered likely to arise, but which cannot be entirely excluded, unless in individual cases prerequisites according to IAS 37.92 occur and the disclosure can be omitted.

Under Provisions for personnel expenses, in general all outstanding benefits within the personnel expenses are presented with the exception of pension obligations. At Hamburg Commercial Bank, these include, in particular, provisions for variable performance-related pay, partial retirement and long-term credits for hours. Provisions for anniversary payments and partial retirement are accounted for based on actuarial expert reports.

In accordance with IAS 37, provisions are mainly determined based on the best estimate of management. The most likely amount necessary to meet the obligations identifiable on the reporting date is recognised. Long-term provisions are reported at present value to the extent discounting effects are significant. For discounting purposes, interest rates that are valid on the reporting date and are term-appropriate are used based on risk-free interest curves. Addition of accrued interest to be performed during the reporting year is reported under Net interest income.

INCOME TAXES

Current tax assets and liabilities are stated at the amount of the anticipated refund from, or payment to, the tax authorities, applying the tax provisions of the countries in question.

Deferred tax assets are created for all deductible timing differences between the value of an asset or liability as measured by IFRS standards and its assigned value in tax terms, provided it is probable that taxable income will be available against which such differences can be utilised. Deferred tax liabilities are created for all taxable temporary differences. Deferred taxes on tax loss carryforwards are stated as the amount likely to be used in future. Deferred taxes are calculated using the tax rates and rules anticipated to be valid at the time when the deferred tax assets are to be realised. The effects of tax rate changes on deferred taxes are taken into account on adoption of the legislative amendment. Deferred tax assets are recognised and measured as deferred income tax claims and deferred tax liabilities as deferred income tax liabilities.

Hamburg Commercial Bank prepares tax results planning for the purpose of assessing deferred tax asset impairment.

Expenses and income from deferred taxes are in principle recognised on an accrual basis in the statement of income under Income taxes, separate from actual tax expenses and income. In doing so, the accounting treatment of the underlying situation is taken into account. Deferred taxes are recognised in the statement of income if the item in the statement of financial position itself is recognised in profit or loss. Deferred taxes are charged or credited directly to equity in OCI, if the underlying item itself is charged or credited directly to equity (IAS 12.61A).

At each reporting date Hamburg Commercial Bank makes an assessment as to whether the realisation of future tax benefits is sufficiently probable to recognise deferred tax assets. Amongst other things, this requires a management assessment of the tax benefits that arise from the existing tax strategies and future taxable income as well as the consideration of other positive and negative factors. The deferred tax assets disclosed could decrease, if the estimates of the planned taxable income and the tax benefits achievable under the existing tax strategies are revised downwards or if changes to current tax legislation restrict the timing and extent of the realisability of future tax benefits.

OTHER ASSETS AND OTHER LIABILITIES

All remaining assets and liabilities not allocable to any other item are stated under Other assets or Other liabilities. These include accrued expenses and income amongst other things.

The general recognition and measurement criteria for assets are observed. Initial recognition is at cost. For financial instruments included in this item, the provisions of IFRS 9 apply.

IV. Leasing transactions

Pursuant to IAS 17, the term "lease" refers to the transfer of use for an agreed period in return for a fee. A distinction is made between finance and operating leases. The allocation depends on whether substantially all risks and rewards are transferred to the lessee or not.

A finance lease is considered to be present where the economic risks and rewards as defined by IAS 17 lie with the lessee; consequently, the leased asset is reported in the latter's statement of financial position. All other leasing arrangements are classified as operating leases. The classification is made at the beginning of each lease.

FINANCE LEASES

In the case of finance leases, Hamburg Commercial Bank acts solely as lessor and recognises a receivable in the amount of the net investment value either under Loans and advances to banks or Loans and advances to customers, depending on the lessee.

Leasing rates due are divided into a repayment part which is not recognised in profit or loss and an interest part which is. The part taken to profit or loss is recognised in Net interest income.

Impairments of finance lease receivables attributable to changes in credit risk are recognised in Loan loss provisions. Impairments not attributable to changes in credit risk, such as the impairment of the non-guaranteed residual value of a leasing receivable, are recognised in other operating expense.

OPERATING LEASES

As lessor, Hamburg Commercial Bank states leasing objects as assets measured at amortised cost under Property, plant and equipment or as Investment property. Leasing instalments received are stated under Other operating income, and the corresponding depreciation stated in Administration expenses. Hamburg Commercial Bank reports rental expenses from contracts where Hamburg Commercial Bank acts as lessee as rental expenses under administration expenses.

V. Currency translation

The consolidated financial statements of Hamburg Commercial Bank are drawn up in euros. The euro is the functional currency of the overwhelming majority of the individual financial statements included in the Group financial statements. However some Group companies have another functional currency.

The following principles are applied when translating foreign currency items within single entity financial statements and for translating the financial statements of Group companies which do not draw up their accounts in euro.

PRESENTATION OF FOREIGN CURRENCY TRANSACTIONS IN THE GROUP FINANCIAL STATEMENTS

Initial measurement of assets and liabilities from all foreign currency transactions takes place at the spot rate for the transaction.

In subsequent measurement, monetary items are translated based on the spot mid-rate as of the reporting date. Non-monetary items that are stated in the statement of financial position at fair value are translated using the spot mid-rate applicable at the time of measurement and any other non-monetary items at the historical rate.

Expenses and income in foreign currency arising from the measurement of items in the statement of financial position are translated using the rates applied for translating the items in question. The transaction rates are used for all other expenses and income.

For monetary and non-monetary items measured at fair value, currency translation differences are always recognised in the statement of income of the period when the result arose.

TRANSLATION OF FINANCIAL STATEMENTS PREPARED IN FOREIGN CURRENCY FOR INCLUSION IN THE CONSOLIDATED FINANCIAL STATEMENTS

Assets and liabilities from financial statements denominated in foreign currencies are translated at the period-end rate. Average rates for the reporting period are used to translate expenses and income. With the exception of the revaluation reserve reported to be included in the financial statements, which is translated at the closing rate, equity is translated at historic rates (date of the transaction).

Any differences arising from this method of translation are reported under OCI and under Equity in the Currency reserve.

Notes on the Group statement of income

8. Net interest income

Net interest income

(€ m)	2018	2017[1]
Interest income from		
Lending and money market transactions categorised as AC and FVOCI	567	n.r.
Fixed-interest securities categorised as AC and FVOCI	129	n.r.
impaired financial assets	227	n.r.
Interest income from financial assets categorised as AC and FVOCI	**923**	**n.r.**
thereof attributable to financial assets measured at AC	829	n.r.
thereof attributable to financial assets measured at fair value in OCI as a mandatory requirement	94	n.r.
Interest income from		
Other lending and money market transactions	209	n.r.
Other fixed-interest securities	24	n.r.
Trading transactions	6	n.r.
Derivative financial instruments	1,339	n.r.
Current income from		
Equities and other non-fixed-interest securities	6	7
Equity holdings	8	15
Other holdings	–	2
Interest income from other financial instruments	**1,592**	**24**
Negative interest on investments categorised as AC and FVOCI	**-21**	**n.r.**
thereof attributable to financial assets measured at AC	-21	n.r.
Negative interest on other cash investments and derivatives	**-227**	**n.r.**
Interest income from		
Lending and money market transactions	n.r.	1,030
Fixed-interest securities	n.r.	215
Trading transactions	n.r.	4
Derivative financial instruments	n.r.	1,420
Unwinding	n.r.	94
Interest income	**n.r.**	**3,062**
of which attributable to financial instruments not classified as HfT or DFV	n.r.	1,398
Negative interest	**n.r.**	**-305**
Interest expenses for		
Liabilities to banks	91	118
Liabilities to customers	382	424
Securitised liabilities	146	220
Subordinated capital	15	17
Trading transactions	–	1
Other liabilities	19	18
Derivative financial instruments	1,240	1,404
Interest expenses	**1,893**	**2,202**
thereof attributable to financial liabilities not measured at fair value through profit or loss	414	n.r.
of which attributable to financial instruments not classified as HfT or DFV	n.r.	490
Positive interest on borrowings and derivatives	**-224**	**-296**
thereof attributable to financial liabilities not measured at fair value through profit or loss	-16	n.r.
Net income from reestimating interest and repayment cash flows	1,085	413
Net income from discounting and compounding	-91	-109
Net income/loss from hybrid financial instruments	**994**	**304**
thereof attributable to financial liabilities not measured at fair value through profit or loss	994	n.r.
of which attributable to financial instruments not classified as HfT or DFV	n.r.	304
Total	**1,592**	**880**

[1] In contrast to the presentation in the statement of income, the presentation of net interest income for the previous year is not broken down in accordance with IAS 1.82(a), as a breakdown by product type is not possible for 31 December 2017.

Regarding the adjusted prior-year net interest income figures, see Note 3 Adjustments to the prior-year figures.

Interest income and expenses relating to trading and hedging derivatives are disclosed under interest income and expense from/for trading and hedging derivatives.

Net interest income includes income and expenses arising from the amortisation of the adjustment items for portfolio fair value hedge relationships and corresponding proceeds from the closing of the underlying transactions which contributed to the adjustment item.

For receivables subject to specific loan loss provisions, both the interest income and the loan loss provisions have to be adjusted by multiplying them by the original effective interest rate in Net interest income. This procedure corresponds to the previous unwinding.

The negative interest from investments categorised as AC and FVOCI results from lending and money market transactions. The negative interest on cash investments and derivatives results in full from derivative financial instruments. The negative interest in the previous year was mainly due to derivative financial instruments.

The positive interest for the current year and the previous year result primarily from derivative financial instruments.

The term hybrid financial instruments covers silent participations, profit participation capital and bonds measured at amortised cost, the return on which is profit-related and which participate in the net loss for the year and accumulated losses of the Bank. As a measure for regulatory capital restructuring and optimisation (Liability Management Exercise), the Bank has terminated all silent participations it had issued in the year under review with effect from 31 December 2020. This applies both to hybrid instruments contracted bilaterally with institutional investors and to those placed on the international capital market.

The total of current participation in losses (not allowing for reversals of impairment losses) relating to the 2018 financial year was € 327 million (previous year: € 285 million).

The net income from hybrid financial instruments includes the effects on earnings resulting from the application of IFRS 9 B5.4.6 (previous year: IAS 39.AG8).

The difference between the valuation for tax purposes and measurement under IFRS 9 B5.4.6 (previous year: IAS 39.AG8) results in deferred tax expenses of € 113 million (previous year: € 7 million in deferred tax income).

9. Net commission income

Net commission income

(€ m)	2018	2017
Commission income from		
Lending business	37	53
Securities business	5	7
Guarantee business	10	10
Payments and account transactions as well as documentary business	23	25
Other commission income	7	12
Commission income	**82**	**107**
Commission expense from		
Lending business	4	3
Securities business	2	3
Guarantee business	26	27
Payments and account transactions as well as documentary business	5	6
Other commission expenses	10	3
Commission expenses	**47**	**42**
Total	**35**	**65**

Financial instruments that are not measured at fair value through profit or loss account for € 42 million of Net commission income. In the previous year, € 68 million of Net commission income was attributable to financial instruments not categorised as HfT or DFV.

The premium expense resulting from a synthetic securitisation transaction (see 2017 Annual Report under Note 3 II) is reported under Net commission income and amounted to € 26 million in the reporting period (previous year: € 26 million). The transaction was ended in December 2018.

10. Result from hedging

The change in value attributable to the hedged risk for designated underlying and hedging transactions in effective hedging relationships is reported under the item Result from hedging. The item contains the profit contributions from micro and portfolio fair value hedges. Hedge accounting is used solely for interest rate risks.

Result from hedging

(€ m)	2018	2017
Fair value changes from hedging transactions	-18	-54
Micro fair value hedge	-11	–
Portfolio fair value hedge	-7	-54
Fair value changes from underlyings	9	36
Micro fair value hedge	13	–
Portfolio fair value hedge	-3	36
Total	**-9**	**-18**

11. Result from financial instruments categorised as FVPL

The result from financial instruments categorised as FVPL includes the realised result and the valuation result of financial instruments in the FVPL Trading, FVPL Designated and FVPL Other categories. The interest income and expense and results from current dividends in these holding categories are reported under Net interest income. The comparative period comprises the realised result and the valuation result of financial instruments classified as HfT and DFV.

Gains and losses arising from currency translation are generally disclosed in this statement of income line item. In derogation of the above, the results from the translation of loan loss provisions denominated in foreign currency are disclosed in the Loan loss provisions.

Other products comprises the income from foreign exchange transactions, credit derivatives and commodities.

Result from financial instruments categorised as FVPL

(€ m)	2018	2017
Bonds and interest rate derivatives		
FVPL Held For Trading	-4	n.r.
FVPL Designated	31	n.r.
FVPL Other	-178	n.r.
Total	**-151**	**n.r.**
HfT	n.r.	173
DFV	n.r.	19
Total	**n.r.**	**192**
Equities and equity derivatives		
FVPL Held For Trading	3	n.r.
FVPL Designated	1	n.r.
FVPL Other	-40	n.r.
Total	**-36**	**n.r.**
HfT	n.r.	–
DFV	n.r.	-1
Total	**n.r.**	**-1**
Other products		
FVPL Held For Trading	2	n.r.
FVPL Designated	1	n.r.
FVPL Other	-32	n.r.
Total	**-29**	**n.r.**
HfT	n.r.	63
DFV	n.r.	–
Total	**n.r.**	**63**
Compensation under the second loss guarantee	80	
Total	**-136**	**254**

The Result from financial instruments categorised as FVPL includes net income from foreign currency of € -10 million (previous year: € 76 million).

During the reporting period € -4 million (previous year: € 13 million) of the changes in fair value of the financial assets categorised as FVPL Designated related to changes in the credit spread rather changes in market interest rates. In cumulative terms, a total of € -8 million (previous year: € 3 million) is attributable to changes in the credit spread.

12. Net income from financial investments

Under IFRS 9, this item shows the realised results of financial assets categorised as FVOCI and equity holdings recognised at fair value as of the year under review.

In the prior-year reporting period, this item included, in addition to any realised gains and losses from financial investments classified as loans and receivables (LaR) and available for sale (AfS), write-downs and write-ups and general loan loss provisions. In the case of financial investments classified as AfS, write-ups were only recognised in the statement of income for debt instruments up to a maximum of the amortised cost.

Regarding the adjusted prior-year figures, see Note 3 Adjustments to the prior-year figures.

Net income from financial investments

(€ m)	2018	2017
Realised results from financial assets categorised as FVOCI	102	
Total	**102**	
Classified as AfS		
+ Realised gains/losses (–)		82
– Write-downs		68
Total		**14**
Classified as LaR		
– Write-downs		1
+ Write-ups		45
Total		**44**
– Addition to general loan loss provisions (LaR portfolios)		**–**
+ Reversal of general loan loss provisions (LaR portfolios)		**4**
Total		**4**
Total	**102**	**62**

13. Result from the disposal of financial assets classified as AC

This item includes all realised results from the sale and premature repayment of, as well as substantial modifications to, financial assets categorised at amortised cost.

Under IAS 39, the result of receivables that were purchased or originated credit-impaired was reported in the result from loan loss provisions. If the result was mainly based on interest components, it was reported under Net interest income. Otherwise, it was disclosed under Other operating result.

The disposals in the reporting period relate to sales and premature repayments. The sales executed are compatible with the "Hold to collect" business model.

Regarding the adjusted prior-year figures, see Note 3.

Result from the disposal of financial assets classified as AC

(€ m)	2018	2017
Gains from the disposal of financial assets classified as AC		
Loans and advances to customers	8	274
Financial investments	–	28
Total gains	**8**	**302**
Losses from the disposal of financial assets classified as AC		
Loans and advances to customers	6	–
Total losses	**6**	**–**
Total	**2**	**302**

14. Net income from financial investments accounted for under the equity method

As at 31 December 2018, Hamburg Commercial Bank does not hold any shares in associates or joint ventures that are included in the Group financial statements using the equity method.

This means that as at 31 December 2018, the Group had no pro rata net income from financial investments accounted for under the equity method. As a result, only the previous year's result is shown in the following overview.

Net income from financial investments accounted for under the equity method

(€ m)	2018	2017
Pro rata net income for the period	–	2
Total	**–**	**2**

15. Loan loss provisions

This item shows the change in loan loss provisions for all loans and advances to banks, loans and advances to customers and financial investments, as well as leasing receivables, categorised as AC or FVOCI.

	2018
Loans and advances to banks	
Insignificant increase in the loan default risk (level 1/12-month ECL)	1
Result from the change in loan loss provisions on loans and advances to banks	1
Loans and advances to customers	
Insignificant increase in the loan default risk (level 1/12-month ECL)	-32
Significant increase in the loan default risk (level 2/lifetime ECL)	-46
Impaired credit rating (level 3/lifetime ECL)	-224
loans that are purchased or originated credit-impaired (POCI)	–
Result from the change in loan loss provisions on loans and advances to customers	**-302**
Financial investments	
Significant increase in the loan default risk (level 2/lifetime ECL)	2
thereof FVOCI	2
Result from the change in loan loss provisions for financial investments	**2**
Off-balance-sheet business	
Insignificant increase in the loan default risk (level 1/12-month ECL)	2
Significant increase in the loan default risk (level 2/lifetime ECL)	-4
Impaired credit rating (level 3/lifetime ECL)	-8
Provisions in lending business in accordance with IAS 37	11
Result from changes in provisions in the lending business	**1**
– Direct write-downs	19
+ Payments received on loans and advances previously written down	30
Result from other changes to loan loss provisions	**11**
Result from changes in loan loss provisions before currency translation gains or losses and compensation	**-287**
Currency translation gains or losses on loan loss provisions denominated in foreign currency	**1**
Compensation under the second loss guarantee	**-30**
Total loan loss provisions	**-316**

In the reporting period, changes in loans and advances to banks and customers relate only to transactions categorised as AC.

As part of the allocation to loan loss provisions for loans and advances to customers in accordance with the expected credit loss model, adjustments were also made as at 31 December 2018 in the form of model overlays (for a definition, see Note 7). These relate to risk factors relevant to valuation that are not already included in the credit-risk-based calculation parameters used in the expected credit loss models/the expert estimates.

On the one hand, these risk factors relate to the need for a stronger weighting of downside scenarios given the current economic uncertainties with a potential impact on the sectors relevant to the Bank (in particular shipping and real estate).

On the other hand, they relate to the impact, as estimated by Hamburg Commercial Bank, of the emission requirements for ships that will apply from 2020.

Under IAS 39, changes in loan loss provisions for loans and advances to banks and loans and advances to customers in the LaR category were reported under the item Loan loss provisions in the lending business.

Loan loss provisions in the lending business

(€ m)	2017
– Expense from additions to loan loss provisions	2,307
+ Income from the reversal of loan loss provisions	764
Result from changes in loan loss provisions	**-1,543**
– Expenses from allocations to provisions in the lending business	46
+ Income from reversals of provisions in the lending business	83
Result from changes to provisions in the lending business	**37**
– Direct write-downs	49
+ Payments received on loans and advances previously written down	153
Result from other changes to loan loss provisions	**104**
Result from changes in loan loss provisions before currency translation gains or losses and compensation	**-1,402**
Currency translation gains or losses on loan loss provisions denominated in foreign currency	**44**
Compensation under the second loss guarantee	**-728**
Total loan loss provisions in the lending business	**-2,086**

Net changes in loan loss provisions in the lending business

(€ m)	2017
Specific loan loss provisions	-1,771
General loan loss provisions	228
Net change in loan loss provisions in the lending business	**-1,543**
Provisions for specific risks	2
Provisions for portfolio risks	35
Net change in provisions in the lending business	**37**

16. Administrative expenses

Administrative expenses

(€ m)	2018	2017
Personnel expenses	198	230
Operating expenses	186	215
Depreciation on property, plant and equipment, leasing assets, investment properties and amortisation on intangible assets	18	36
Total	**402**	**481**

Regarding the adjusted prior-year figures for operating expenses, see Note 3 Adjustments to the prior-year figures.

Personnel expenses

(€ m)	2018	2017
Wages and salaries	165	180
Social security contributions	25	28
of which employer contributions to government-sponsored pension plans	13	14
Expenses for pensions and support	8	22
Total	**198**	**230**

Please refer to Note 42 for detailed information on expenses for pensions and support as well as expenses for defined contribution plans.

Operating expenses

(€ m)	2018	2017
IT costs	78	80
Costs for information services	9	10
Costs for external services and project work	37	47
Legal service costs	14	22
Expenses for land and buildings	11	12
Obligatory contributions and expenses related to corporate law	1	1
Costs of advertising, PR and promotional work	5	5
Expenses on plant and equipment	1	1
Other expenses	30	37
Total	**186**	**215**

Depreciation on property, plant and equipment and amortisation on intangible assets are broken down as follows:

Depreciation

(€ m)	2018	2017
Scheduled depreciation on		
Plant and equipment	3	3
Property	3	3
Acquired software	3	3
Software developed in-house	2	2
Unscheduled depreciation on		
Assets held for sale and disposal groups	7	25
Total	**18**	**36**

Of the scheduled depreciation on property € 1 million is attributable to investment properties.

The unscheduled depreciation on Assets held for sale was recognised for assets that form part of a disposal group that has been set up. Further information in this regard can be found in Note 33.

The total unscheduled depreciations are attributable to the Non-Core Bank segment.

17. Other operating income

Other operating income

(€ m)	2018	2017
Income		
from reversal of other provisions and release of liabilities	16	34
from cost allocations and reimbursement of expenses	29	38
from the disposal of property, plant and equipment	18	11
from interest on receivables from the tax office	7	1
from leasing transactions	5	25
from legal disputes	5	5
from investment property (rental income)	4	–
from single ship companies (charter rates)	–	18
income from write-ups on property, plant and equipment	–	9
from the reversal of provisions for processing fees in the lending business	–	2
Other income	33	46
Total income	**117**	**189**
Expenses		
from additions to other provisions	167	71
from expenses paid in advance for transaction fees, legal fees, servicing	25	26
for interest expenses pursuant to Section 233 AO	8	11
from the disposal of property, plant and equipment	–	10
for investment property	1	3
Other expenses	38	45
Total expenses	**239**	**166**
Income/loss arising on the deconsolidation of companies	15	-2
Total	**-107**	**21**

Regarding the adjusted prior-year figures, see Note 3 Amendment to the prior-year figures. Income from the disposal of property, plant and equipment is explained in Note 33.

Allocations to other provisions mainly relate to the Bank's legal risks.

With regard to the income or loss arising from the deconsolidation of companies please refer to our explanations in Note 5.

18. Expenses for regulatory affairs, deposit guarantee fund and banking associations

Expenses for regulatory affairs, deposit guarantee fund and banking associations

(€ m)	2018	2017
Expense for European bank levy	31	36
Expenses for deposit guarantee fund	50	5
Expenses for banking supervisory authority	4	4
Expenses for banking associations	4	4
Total	**89**	**49**

Since 31 December 2018 and with retrospective effect for the previous year, the Bank has reported regulatory expenses (European bank levy and contributions paid to the supervisory authorities), the deposit guarantee fund and membership fees paid to banking associations under this item.

The marked increase in the item relating to expenses for the deposit guarantee fund is mainly due to provisions set up for expected one-off payments to be made to the Association of German Banks (*Bundesverband deutscher Banken*) due to the planned change in the guarantee scheme. Details regarding the changes to the prior-year figures, see Note 3 .

19. Net income from restructuring and privatisation

Net income from restructuring and privatisation

(€ m)	2018	2017
Personnel expenses due to restructuring	259	-
Operating expenses due to restructuring	46	25
Income from reversals of provisions from restructuring	5	11
Net income from restructuring	**-300**	**-14**
Expenses from privatisation	66	52
Net income from restructuring and privatisation	**-366**	**-66**

In connection with its successful privatisation on 28 November 2018, Hamburg Commercial Bank approved an extensive restructuring programme, which includes the planned reduction in the number of employees and extensive projects to support the Bank's realignment.

Additional expenses associated with the privatisation are also reported under this item. In the year under review, the expenses from privatisation mainly related to measures to prepare for, and implement, the privatisation transaction and the associated expenses for external consulting. Transformation measures will also have an impact in subsequent years.

20. Expenses for government guarantees

Expenses for government guarantees

(€ m)	**2018**	2017
HSH Finanzfonds AöR	**158**	149
Total	**158**	**149**

In June 2013, the guarantee granted by the Federal State of Schleswig-Holstein and the Free and Hanseatic City of Hamburg was replenished to € 10 billion. As of 1 January 2016, the Bank was calculating the base premium at a rate of 2.2 % p.a. on the portion of the guarantee that had not yet been drawn. The share of the premium relating to partial guarantee Two (CDS) is disclosed under the line item Hedging effect of credit derivative under the second loss guarantee in the amount of € 6 million (previous year: € 5 million). Expenses in 2018 include a one-time amount of € 100 million for the early cancellation of the guarantee. This was paid to the guarantor on the cancellation date.

21. Income tax expense

Income tax expense

(€ m)	2018	2017
Corporate tax and solidarity surcharge		
Domestic	1	22
Trade income tax		
Domestic	–	20
Current income taxes	**1**	**42**
Income tax from previous years	-15	5
Subtotal current income tax	**-14**	**47**
Income from deferred tax		
from temporary differences	202	-53
from losses carried forward	-168	83
from consolidation	–	-2
Subtotal deferred income tax	**34**	**28**
Income tax expense (+)/income (–)	**20**	**75**

The income from current taxes in previous years mainly results from the adjustment of provisions for 2016 and 2017. The adjustments are based on the tax returns submitted in 2016/the new information available for 2017. The adjustment made to the provisions for tax risks recognised in the balance sheet due to a change in risk assessment resulting from the findings of the current tax audit is also included.

Income of € 330 million resulted from the reversal of a correction to deferred tax assets on temporary differences due to a lack of recoverability from the previous year.

Deferred taxes on tax loss carryforwards are measured on the basis of a recoverability analysis, which is based on the corporate plan. Based on this corporate planning, income from the recognition of deferred taxes on loss carryforwards at the head office amounted to € 159 million in the year under review. Expenses of € 7 million resulting from the reversal of deferred tax assets on loss carryforwards arose for the Singapore branch. At the Luxembourg branch, deferred tax assets of € 16 million were recognised on loss carryforwards. These are offset by corresponding deferred tax liabilities on temporary differences.

The expense relating to deferred taxes on temporary differences in the year under review is mainly attributable to the decrease in temporary differences at the head office.

Reconciliation of income taxes

(€ m)	2018	2017
Group net result	77	-528
Income tax expenses	20	75
Income before taxes incl. income from transfer of losses	97	-453
Domestic income tax rate to be applied in %	31.97	31.97
Imputed income tax expenses in the financial year	**31**	**-145**
Tax effects due to		
appreciation/depreciation of deferred taxes on losses carried forward	313	-64
Differing effective tax rates in Germany and abroad	-42	-21
Non-deductible expenses	70	54
Corrections to trade taxes	-11	-9
Changes in tax rate	–	-7
Taxes for previous years	10	3
Tax-free income	-21	-1
Appreciation/depreciation of deferred taxes on temporary differences and miscellaneous	-330	265
Total tax expense (+)/income (–)	**20**	**75**

In calculating taxes for 2018, a rate of 31.97 % (previous year: 31.97 %) was used for domestic taxes.

The main effects in the reconciliation of the notional to the actual tax expense include the lack of recoverability of newly incurred loss carryforwards and the income from the reversal of the write-down of deferred taxes on temporary differences due to the lack of recoverability from the previous year (€ 330 million).

In addition, there were material reconciliation effects resulting from non-tax-deductible expenses, tax-exempt income, trade tax corrections and taxes from previous years at various domestic and foreign Group units.

22. Net gains and losses from financial instruments

Net gains and losses from financial instruments include both realised gains and measurement gains within the Result from financial instruments categorised as FVPL and Net income from financial investments, the hedging effect of the credit derivative under the second loss guarantee as well as loan loss provisions with regard to credit business shown on the statement of financial position. Neither Net interest nor Net commission income is included in this item.

Net gains and losses from financial instruments

(€ m)	2018	2017
FVPL Held For Trading, Other, Designated	-186	n.r.
AC assets and liabilities	-315	n.r.
FVOCI Mandatory	103	n.r.
Total	**-398**	**n.r.**
DFV	n.r.	18
AfS	n.r.	–
LaR	n.r.	-2,047
HfT	n.r.	1,046
Total	**n.r.**	**-983**

23. Earnings per share

To calculate Earnings per share, the Group net result attributable to Hamburg Commercial Bank shareholders is divided by the weighted average number of ordinary shares outstanding during the year under review. As in the previous year, Hamburg Commercial Bank AG has not issued any diluted forms of capital as at 31 December 2018, i.e. the diluted and undiluted earnings are the same. The calculation was based on non-rounded values.

Earnings per share

	2018	2017
Attributable Group net result (€ m) – undiluted/diluted	70	-535
Number of shares (millions)		
Average number of ordinary shares outstanding undiluted/diluted	302	302
Earnings per share (€)		
Undiluted	0.23	-1.77
Diluted	0.23	-1.77

Notes on the Group statement of financial position

24. Cash reserve

Cash reserve

(€ m)	2018	2017
Cash on hand	1	4
Balances at central banks	5,299	6,515
of which at the Deutsche Bundesbank	5,289	6,499
Treasury bills, discounted treasury notes and similar debt instruments issued by public-sector institutions	62	106
Total	**5,362**	**6,625**

25. Loans and advances to banks

Loans and advances to banks

(€ m)	2018			2017		
	Domestic	Foreign	Total	Domestic	Foreign	Total
Payable on demand	568	1,216	1,784	582	1,333	1,915
Other loans and advances	1,303	80	1,383	1,773	150	1,923
Total before loan loss provisions	**1,871**	**1,296**	**3,167**	**2,355**	**1,483**	**3,838**
Loan loss provisions	–	–	–	–	1	1
Total after loan loss provisions	**1,871**	**1,296**	**3,167**	**2,355**	**1,482**	**3,837**

Of loans and advances to banks, holdings in the amount of € 91 million (previous year: € 222 million) have a residual maturity of more than one year.

Loans and advances to banks include money market transactions in the amount of € 2,356 million (previous year: € 2,317 million).

The development of the carrying amounts of loans and advances to banks is shown in Note 50.

Information on collateral transferred which also contains information regarding securities lending and repurchase agreements can be found in Note 61.

26. Loans and advances to customers

Loans and advances to customers

(€ m)	2018			2017		
	Domestic	Foreign	Total	Domestic	Foreign	Total
Retail customers	441	11	452	651	36	687
Corporate clients	16,262	12,173	28,435	18,424	16,152	34,576
Public authorities	3,732	172	3,904	3,752	159	3,911
Total before loan loss provisions	**20,435**	**12,356**	**32,791**	**22,827**	**16,347**	**39,174**
Loan loss provisions	497	334	831	1,952	2,541	4,493
Total after loan loss provisions	**19,938**	**12,022**	**31,960**	**20,875**	**13,806**	**34,681**

Of loans and advances to customers, holdings in the amount of € 24,502 million (previous year: € 25,420 million) have a residual maturity of more than one year.

Loans and advances to customers include money market transactions in the amount of € 1,114 million (previous year: € 982 million).

Loans and advances to customers include receivables under finance lease transactions in the amount of € 73 million (previous year: € 76 million). The gross investment value of the leasing transactions is € 78 million (previous year: € 82 million). Further details on leasing transactions can be found in Note 60.

The development of the carrying amounts of loans and advances to customers is shown in Note 50.

Information on collateral transferred which also contains information regarding securities lending and repurchase agreements can be found in Note 61.

27. Loan loss provisions

Loan loss provisions

(€ m)	2018	2017
Loan loss provisions for loans and advances to banks categorised as AC	-	
Loan loss provisions for loans and advances to customers - categorised as AC, incl. leasing	831	
Loan loss provisions for loans and advances to banks	-	1
Loan loss provisions for loans and advances to customer and non-current assets held for sale and disposal groups	-	4,493
Loan loss provisions in the lending business	**831**	**4,494**
Compensation under the second loss guarantee	-	-5,181
Loan loss provisions for items in the statement of financial position	**831**	**-687**
Provisions in the lending business	60	67
Loan loss provisions for items in the statement of financial position and off-balance sheet risks in the lending business	**891**	**-620**

In accordance with IFRS 9, loan loss provisions are only set up for transactions categorised as AC. As at 31 December 2018, there was no longer any hedging effect of the second loss guarantee (see Note 3).

The 2017 compensation item also includes compensatory claims against the guarantor HSH Finanzfonds AöR resulting from settled losses for transactions for which loan loss provisions had already been derecognised. For information on the development of the IFRS 9 portfolio of loan loss provisions for banks and loans and advances to customers, please refer to Note 50.

The development of loan loss provisions for banks under IAS 39 in the previous year was as follows:

Development of loan loss provisions for loans and advances to banks before compensation

(€ m)	Specific loan loss provisions	General loan loss provisions	Total
As at 1 January 2017	**–**	**1**	**1**
As at 31 December 2017	**–**	**1**	**1**

Loan loss provisions for customers under IAS 39 developed as follows in the previous year:

Development of loan loss provisions for loans and advances to customer and non-current assets held for sale and disposal groups before compensation

(€ m)	Specific loan loss provisions	General loan loss provisions	Total
As at 1 January 2017	**6,336**	**375**	**6,711**
Additions	2,307	–	2,307
Reversals	536	228	764
Utilisation	3,093	–	3,093
Unwinding	-94	–	-94
Changes in the scope of consolidation	-13	–	-13
Exchange rate changes	-552	-9	-561
As at 31 December 2017	**4,355**	**138**	**4,493**

The loan loss provisions under IAS 39 relate exclusively to items categorised as loans and receivables (LaR).

28. Hedge Accounting

Hamburg Commercial Bank continues to apply the portfolio fair value hedge approach in accordance with IAS 39, making use of the option under IFRS 9.6.1.3. Furthermore, Hamburg Commercial Bank now uses the micro fair value hedge approach in accordance with IFRS 9 for financial instruments measured at fair value directly in equity under IFRS 9. The following section provides a description of the hedging and underlying transactions used for hedging purposes, including the risk management strategy, the impact on cash flows and the effects on the net assets, statement of comprehensive income and statement of changes in equity.

I. Risk management strategy

In order to avoid distortions in the statement of income resulting from interest-bearing financial instruments, micro and portfolio fair value hedge accounting is used to hedge the market price risk interest.

For micro fair value hedges, structured euro swaps are designated as hedging instruments for structured euro underlying transactions. These designated hedges correspond to economic back-to-back hedges which neutralise the market price risks associated with the underlying transactions. The effectiveness of these hedges is ensured by a critical term match and ineffectiveness is expected from model adjustments, measurement mismatches and the inclusion of tenor basis spreads. In portfolio fair value hedges on interest rate risks, the underlying transactions as a whole are hedged by means of interest rate swaps. Effectiveness is measured in accordance with the rules set out in IAS 39 and the hedge ratio is calculated using the dollar offset method. Ineffectiveness can result from maturities of assets and liabilities that do not match, and from the reference interest rate of the hedging transactions.

Hedge accounting is used solely for interest rate risks.

II. Effects on cash flows

In order to assess the cash flows to be expected, the nominal and average prices of the hedging instruments in micro fair value hedges are presented below.

Micro fair value hedges

(€ m)	Maturity date		
	2027	2037	2038
Nominal value of hedging instruments	100	450	200
Average swap rate	3.869	3.694	3.633

III. Effects on net assets and statement of comprehensive income

The effects on the net assets and statement of comprehensive income are presented separately for hedging transactions and underlying transactions.

HEDGING INSTRUMENTS

This section presents the nominal, hedge adjustment and the positive and negative fair values of derivatives used in hedge accounting. Only interest rate swaps are currently taken into account as hedging instruments. If a derivative is only designated pro rata in hedge accounting, the item Positive/negative fair value of hedging derivatives contains the corresponding share of the derivative's fair value, nominal value and hedge adjustment. The residual amount is reported under Trading assets/Net trading income.

Hedging instruments[1]

(€ m)		2018			2017		
Hedge type/type of risk	Balance sheet item	Nominal value	Carrying amount	Hedge adjustment (ytd)	Nominal value	Carrying amount	Hedge adjustment (ytd)
Fair value hedge/interest rate risk							
Interest rate derivatives (assets side)	Positive fair values of hedging derivatives	9,577	175	-62	–	264	–
Interest rate derivatives (liabilities side)[2]	Negative fair value of hedging derivatives	7,610	501	-41	–	163	–

[1] The portfolios are newly designated/redesignated on a monthly basis at the time of the integration of the new business. This leads to a change in the composition of the hedging relationship between the underlying and hedging transactions.

[2] The carrying amount of € 501 million as at the reporting date includes a micro fair value hedge, the carrying amount of € 163 million for the previous year does not include a micro fair value hedge.

Asset-side transactions are reported in the balance sheet item Positive fair values of hedging derivatives and derivatives on the liabilities side are shown in the balance sheet item Negative fair values of hedging derivatives. The overall changes in these items are mainly due to changes in the portfolio compositions and movements in interest rates in the euro and US dollar capital markets.

UNDERLYING TRANSACTIONS

This section presents financial instruments on the assets and liabilities side used in hedge accounting. The following table shows the carrying amounts, accumulated changes in value (ltd) and since the beginning of the financial year (ytd) for these financial instruments. The underlying transactions currently include assets (receivables and securities) and liabilities. Hedge accounting is used solely for interest rate risks.

Underlying transactions[1]

(€ m)		2018			2017		
Hedge type/type of risk	Balance sheet item	Carrying amount	Cum. hedge adjustment (ltd)	Hedge adjustment (ytd)	Carrying amount	Cum. hedge adjustment (ltd)	Hedge adjustment (ytd)
Fair value hedge/ interest rate risk							
Portfolio fair value hedge: Fixed-interest rate loans, debentures, securities	Positive adjustment item from portfolio fair value hedges	9,347	195	-54	–	249	–
Micro fair value hedge	Loans and advances to customers	1,035	13	13	–	–	–
Portfolio fair value hedge: Fixed-interest issues	Negative adjustment item from portfolio fair value hedges	13,315	399	-57	–	456	–
Portfolio fair value hedge (inactive)	Positive adjustment item from portfolio fair value hedges	802	5	-1	–	6	–
Portfolio fair value hedge (inactive)	Negative adjustment item from portfolio fair value hedges	302	61	-36	–	97	–
Micro fair value hedge (inactive)	Loans and advances to customers	262	74	-14	–	88	–
Micro fair value hedge (inactive)	Liabilities to customers, securitised liabilities, subordinated capital	293	16	-10	–	26	–

[1] The portfolios are newly designated/redesignated on a monthly basis at the time of the integration of the new business. This leads to a change in the composition of the hedging relationship between the underlying and hedging transactions.

29. Trading assets

Only financial assets in the FVPL Trading category are reported under Trading assets. Mainly included in this category are original financial instruments held for trading purposes, including accrued interest, and derivatives with a positive fair value which are either not designated as a hedge derivative or are used as hedging instruments but do not meet the requirements of IAS 39/IFRS 9 for hedge accounting.

Trading assets of € 2,843 million (previous year: € 3,313 million) have a residual maturity of more than one year.

Information on collateral transferred which also contains information regarding securities lending and repurchase agreements can be found in Note 61 .

Trading assets

(€ m)	2018	2017
Bonds and debentures		
from public-sector issuers	81	42
negotiable and listed	81	42
from other issuers	115	159
negotiable and listed	113	156
negotiable and not listed	2	3
Debentures and other fixed-interest securities	**196**	**201**
Positive fair value of financial derivatives		
Interest rate-related transactions	2,499	2,990
currency-related business	72	72
other business	275	358
Positive fair value of financial derivatives	**2,846**	**3,420**
Other, including promissory notes held for trading	–	13
Receivables from syndication transactions	52	7
Total	**3,094**	**3,641**

30. Financial investments

In particular, financial instruments not held for trading purposes are reported as financial investments. This item includes bonds and other fixed-interest securities, equities and other non-fixed-interest securities, holdings in unconsolidated affiliated companies, holdings in joint ventures and associates not carried at equity in the Group financial statements. Under IAS 39, these financial instruments were classified as AfS and LaR and, to a lesser extent, as DFV. Under IFRS 9, these financial instruments belong to the categories FVPL Designated and FVPL Other, FVOCI Mandatory and AC.

Financial investments

(€ m)	2018	2017
Debentures and other fixed-interest securities	10,046	13,545
Shares and other non-fixed-interest securities	9	51
Equity holdings	44	50
Interests in affiliated companies	1	1
Total	**10,100**	**13,647**

The development in the carrying amounts of financial investments for the current year is shown in Note 50.

31. Intangible assets

INTANGIBLE ASSETS

(€ m)	2018	2017
Software	8	9
developed in-house	1	3
acquired	7	6
Software in development	–	1
acquired	–	1
Total	**8**	**10**

Changes in the carrying amounts of intangible assets are shown below:

Development in intangible assets

(€ m)		Software		Software in development		
2018	Goodwill	Software developed in-house	Acquired software	Software developed in-house	Acquired software	Total
Acquisition costs as at 1 January 2018	**190**	**98**	**173**	**–**	**1**	**462**
Additions	–	–	3	–	–	3
Disposals	–	16	16	–	–	32
Reclassifications	–	–	1	–	-1	–
Changes in the scope of consolidation	-19	–	–	–	–	-19
As at 31 December 2018	**171**	**82**	**161**	**–**	**–**	**414**
Amortisation as at 1 January 2018	**190**	**95**	**167**	**–**	**–**	**452**
Additions	–	2	3	–	–	5
Disposals	–	16	16	–	–	32
Changes in the scope of consolidation	-19	–	–	–	–	-19
As at 31 December 2018	**171**	**81**	**154**	**–**	**–**	**406**
Carrying amount as at 31 December 2018	**–**	**1**	**7**	**–**	**–**	**8**
Carrying amount as at 1 January 2018	**–**	**3**	**6**	**–**	**1**	**10**

Development in intangible assets

(€ m)		Software		Software in development		
2017	Goodwill	Software developed in-house	Acquired software	Software developed in-house	Acquired software	Total
Acquisition costs as at 1 January 2017	**190**	**98**	**172**	**–**	**2**	**462**
Additions	–	–	1	–	–	1
Disposals	–	–	1	–	–	1
Reclassifications	–	–	1	–	-1	–
Changes in the scope of consolidation	–	–	–	–	–	–
As at 31 December 2017	**190**	**98**	**173**	**–**	**1**	**462**
Amortisation as at 1 January 2017	**190**	**93**	**165**	**–**	**–**	**448**
Additions	–	2	3	–	–	5
Disposals	–	–	1	–	–	1
Changes in the scope of consolidation	–	–	–	–	–	–
As at 31 December 2017	**190**	**95**	**167**	**–**	**–**	**452**
Carrying amount as at 31 December 2017	**–**	**3**	**6**	**–**	**1**	**10**
Carrying amount as at 1 January 2017	**–**	**5**	**7**	**–**	**2**	**14**

As in the previous year, no research costs were incurred in the year under review in connection with the implementation of software developed in-house.

32. Property, plant and equipment and investment property

Property, plant and equipment

(€ m)	2018	2017
Land and buildings	130	219
Plant and equipment	7	12
Assets under construction	2	1
Total	**139**	**232**

Under the item Investment property, all property (land or buildings) is recorded that is held to earn rent or for capital appreciation but is not used in the production or supply of goods or services of the Bank. Properties leased, in the capacity of lessor, under operating leases are also included in this item.

Investment property

(€ m)	2018	2017
Investment property	40	13
Total	**40**	**13**

The fair value of investment property amounts to € 43 million (previous year: € 13 million). The fair values of investment property are allocated without exception to level 3 of the fair value hierarchy. Market-based and income-based valuation techniques are used to determine fair value.

The development in Property, plant and equipment and Investment property in the financial year was as follows:

DEVELOPMENT IN PROPERTY, PLANT AND EQUIPMENT AND INVESTMENT PROPERTIES

(€ m) 2018	Land and buildings	Plant and equipment	Assets under construction	Investment properties	Leasing assets	Technical equipment and machinery
Acquisition costs as at 1 January 2018	**232**	**64**	**1**	**15**	**–**	**–**
Additions	–	1	1	–	–	–
Disposals	–	5	–	1	–	–
Reclassifications	-90	–	–	31	–	–
As at 31 December 2018	**142**	**60**	**2**	**45**	**–**	**–**
Amortisation as at 1 January 2018	**13**	**52**	**–**	**2**	**–**	**–**
Additions	2	3	–	1	–	–
Disposals	–	2	–	–	–	–
Reclassifications	-3	–	–	2	–	–
As at 31 December 2018	**12**	**53**	**–**	**5**	**–**	**–**
Carrying amount as at 31 December 2018	**130**	**7**	**2**	**40**	**–**	**–**
Carrying amount as at 1 January 2018	**219**	**12**	**1**	**13**	**–**	**–**

In the reporting year, land and buildings in the amount of € 34 million were reclassified as investment properties, while € 53 million was reclassified as assets held for sale.

€ 5 million was reclassified from investment properties to assets held for sale.

Further details on depreciation are presented in Note 16.

Development in property, plant and equipment and investment property

(€ m) 2017	Land and buildings	Plant and equipment	Assets under construction	Investment properties	Leasing assets	Technical equipment and machinery
Acquisition costs as at 1 January 2017	**233**	**64**	**1**	**14**	**–**	**–**
Additions	2	1	–	–	–	–
Disposals	–	1	–	–	–	–
Reclassifications	-3	–	–	1	–	–
As at 31 December 2017	**232**	**64**	**1**	**15**	**–**	**–**
Amortisation as at 1 January 2017	**11**	**51**	**–**	**2**	**–**	**–**
Additions	2	3	–	–	–	–
Disposals	–	2	–	–	–	–
As at 31 December 2017	**13**	**52**	**–**	**2**	**–**	**–**
Carrying amount as at 31 December 2017	**219**	**12**	**1**	**13**	**–**	**–**
Carrying amount as at 1 January 2017	**222**	**13**	**1**	**12**	**–**	**–**

In the previous year, land and buildings in the amount of € 3 million were reclassified as investment properties.

€ 2 million was reclassified from investment properties to assets held for sale. These assets were sold in the year under review.

33. Non-current assets held for sale and disposal groups

Non-current assets held for sale and disposal groups

(€ m)	2018	2017
Loans and advances to banks	–	1
Loans and advances to customers	8	12
Property, plant and equipment	53	113
Investment property	4	–
Other assets	–	13
Total	**65**	**139**

As was the case as at 31 December 2017, the loans and advances to customers in the amount of € 8 million (previous year: € 12 million) relate to the few loans that have not yet been definitively sold from a larger non-strategic loan portfolio belonging to the Aviation asset class for which the purchase agreement was already signed in August 2017 as part of the implementation of the market portfolio transaction. Due to the staggered closing mechanism provided for in the purchase agreement, the sale of this loan portfolio involves different closing dates. Loans and advances to customers attributable to the Non-Core Bank segment are included in IFRS 9 category FVPL.

The sale of the FSL Group (formerly Non-Core Bank segment) was completed in February 2018. More detailed information on this disposal process can be found in Note 5 . This sale involved the derecognition of the loans and advances to banks and other assets in the amount of € 12 million reported under IFRS 5 as at 31 December 2017 from the balance sheet.

As at 31 December 2017, six aircraft held for sale by former subsidiaries of Hamburg Commercial Bank were reported under Property, plant and equipment. The sales plan to be included in the market portfolio transaction stipulated that these aircraft, together with the cash accounts and maintenance reserves recognised at the special purpose companies, would be sold to various buyers in order to reduce Hamburg Commercial Bank AG's loan receivables to the greatest extent possible. As at 31 December 2017, this sales plan comprised a total of six disposal groups (Aviation II/I to Aviation II/VI), each consisting of property, plant and equipment, other assets (cash accounts), other liabilities and provisions. Within the first three quarters of the reporting period, the sales of the disposal groups Aviation II/I to Aviation II/VI were completed. The disposal resulted in other Operating income of € 18 million (see note 17). The subsequent measurement in accordance with IFRS 5 resulted in a total loss of € 7 million in the reporting period, which is reported under Administrative expenses. This leaves a disposal gain of € 10 million. Furthermore, both the decrease in property, plant and equipment and the decrease in other liabilities and provisions (see Note 43) are due to the disposal of these disposal groups.

As part of the Bank's restructuring plan, the intention is to concentrate the Bank's operations in one building at both the Hamburg and Kiel locations. The land and buildings no longer to be used for the Bank's own purposes as a result of these plans and two further investment properties are to be sold by the end of the 2019 financial year and are therefore reported under this item under Property, plant and equipment/Investment property.

34. Current tax assets

Current tax assets

(€ m)	2018	2017
Domestic	43	41
Foreign	6	5
Total	**49**	**46**

35. Deferred tax assets

Deferred tax assets arose due to temporary differences in the tax base of the following items in the statement of financial position and tax losses carried forward:

Deferred tax assets

(€ m)	2018	2017
Assets		
Loans and advances to banks	–	12
Loan loss provisions	180	715
Trading assets	–	61
Financial investments	17	17
Other assets	41	55
Liabilities		
Liabilities to banks	53	–
Liabilities to customers	48	–
Securitised liabilities	43	45
Negative fair value of hedging derivatives	160	44
Negative adjustment item from portfolio fair value hedges	147	148
Trading liabilities	289	241
Provisions	203	197
Other liabilities	42	218
Tax losses carried forward	185	17
Subtotal for deferred tax assets	**1,408**	**1,770**
of which long-term	–	121
Netting of deferred tax liabilities	-695	-1,047
Total	**713**	**723**

Out of the deferred tax assets after offsetting, € 703 million is attributable to Germany and € 10 million to abroad.

Deferred taxes on loss carryforwards were recognised in the amount of € 185 million (previous year: € 17 million). As at 31 December 2018, € 159 million of this amount was attributable to the head office (previous year: € 0 million), € 16 million to the Luxembourg branch (previous year: € 0 million) and € 10 million to the Singapore branch (previous year: € 17 million). For the head office and the Singapore branch, the recoverability of the deferred taxes on loss carryforwards results from planned future income. With regard to the Luxembourg branch, the recoverability results from offsetting deferred tax liabilities in the same amount.

There were tax loss carryforwards of € 5,190 million as at the reporting date (previous year: € 7,343 million) for which no deferred tax assets were recognised. The decline compared with the previous year is due in particular to the elimination of tax loss carryforwards in 2018 in connection with the privatisation of the Bank, which was assumed with a high degree of probability at the balance sheet date.

The decrease in deferred tax assets of € 362 million before netting mainly results from changes in valuation differences with regard to loan loss provisions, trading assets and liabilities, the negative fair values of hedging derivatives, other assets and other liabilities, as well as the measurement of loss carryforwards.

The recoverability of deferred tax assets results from positive future results. As part of the assessment of the recoverability of deferred tax assets, there were no impairments recognised on temporary valuation differences at the end of the financial year (previous year: € 330 million).

€ 19 million of the reduction in deferred tax assets relates to deferred taxes for pension obligations recognised directly in equity.

The difference between the valuation for tax purposes and measurement under IFRS 9 B5.4.6 (previous year: IAS 39.AG8) results in deferred tax expenses of € 113 million (previous year: € 7 million in deferred tax income).

36. Other assets

Other assets

(€ m)	2018	2017
Other prepaid expenses	15	16
Receivables from fund transactions	10	9
Receivables from other taxes	3	5
Receivables from insurance contracts	–	16
Other assets	21	28
Total	**49**	**74**

Other assets in the amount of € 0 million (previous year: € 12 million) have a residual maturity of more than one year.

€ 34 million of the assets reported here relate to financial instruments (previous year: € 35 million).

37. Liabilities to banks

Liabilities to banks

(€ m)	2018			2017		
	Domestic	Foreign	Total	Domestic	Foreign	Total
Payable on demand	259	217	476	433	184	617
Term liabilities	4,660	334	4,994	6,580	1,074	7,654
Total	**4,919**	**551**	**5,470**	**7,013**	**1,258**	**8,271**

Of liabilities to banks, holdings in the amount of € 4,047 million (previous year: € 3,871 million) have a residual maturity of more than one year.

The difference between the carrying amount of the liabilities designated as FVPL and their par value, which corresponds to the contractually agreed repayment amount at the due date, amounted as at 31 December 2018 to € -4 million (previous year: € -3 million). Changes in value caused by credit risk account for € 2 million of this amount (previous year: € 1 million).

Information on collateral transferred which also contains information regarding securities lending and repurchase agreements can be found in Note 61.

38. Liabilities to customers

Liabilities to customers by customer group

(€ m)	2018	2017
Corporate clients	15,743	20,907
Public authorities	8,365	14,024
Retail customers	3,985	1,274
Total	**28,093**	**36,205**

Liabilities to customers

(€ m)	2018			2017		
	Domestic	Foreign	Total	Domestic	Foreign	Total
Savings deposits with agreed notice periods of						
3 months	11	–	11	14	–	14
Other liabilities						
Payable on demand	6,599	1,504	8,103	9,146	1,743	10,889
Term liabilities	18,553	1,426	19,979	23,015	2,287	25,302
Total	**25,163**	**2,930**	**28,093**	**32,175**	**4,030**	**36,205**

Of liabilities to customers, holdings in the amount of € 7,258 million (previous year: € 9,791 million) have a residual maturity of more than one year.

The difference between the carrying amount of the liabilities designated as FVPL and their par value, which corresponds to the contractually agreed repayment amount at the due date, amounted as at 31 December 2018 to € -69 million (previous year: € -73 million). Changes in value caused by credit risk account for € 4 million of this amount (previous year: € 7 million).

Information on collateral transferred which also contains information regarding securities lending and repurchase agreements can be found in Note 61.

39. Securitised liabilities

Securitised liabilities

(€ m)	2018	2017
Debentures issued	9,458	12,441
Money market securities issued	–	3
Total	**9,458**	**12,444**

Of securitised liabilities, holdings of € 6,818 million (previous year: € 8,798 million) have a residual maturity of more than one year.

Debentures issued include € 180 million of hybrid financial instruments (31 December 2017: € 508 million). As part of a restructuring of the regulatory capital structure, all of the Bank's silent participations were terminated in the year under review with a notice period of 2 years, i.e. with effect from 31 December 2020. The carrying amounts of the corresponding hybrid financial instruments decreased due to the reassessment of contractual cash flows and on the basis of assumptions and results of Hamburg Commercial Bank's business plan (IFRS 9.B5.4.6, previous year: IAS 39.AG8).

In the item Securitised liabilities repurchased own debentures in the amount of € 1,341 million (31 December 2017: € 2,666 million) were deducted.

The difference between the carrying amount of the securitised liabilities designated as FVPL and their par value, which corresponds to the contractually agreed repayment amount at the due date, amounted as at 31 December 2018 to € -116 million (previous year: € -136 million). Changes in value caused by credit risk account for € 4 million of this amount (previous year: € 3 million).

40. Trading liabilities

Only financial obligations in the FVPL Trading category (previous year: HfT) are reported under Trading liabilities. Mainly included in this category are derivatives with a negative fair value which are either not designated as a hedging derivative or are used as hedging instruments but do not meet the requirements of IFRS 9 for hedge accounting (previous year: IAS 39).

Trading liabilities

(€ m)	2018	2017
Negative fair value from derivative financial instruments		
Interest rate-related business	2,417	3,374
Currency-related business	33	59
Other business	362	442
Total	**2,812**	**3,875**

Of the trading liabilities, holdings of € 2,617 million (previous year: € 3,614 million) have a residual maturity of more than one year.

Information on collateral transferred is presented in Note 61.

41. Provisions

Provisions

(€ m)	2018	2017
Provisions for pension obligations and similar obligations	995	1,103
Other provisions		
Provisions for personnel expenses	28	24
Provisions in the lending business	63	67
Provisions for restructuring	308	45
Provisions for litigation risks and costs	250	98
Other provisions	102	101
Total	**1,746**	**1,438**

The provisions in the lending business shown in the table above include € 3 million in provisions attributable to guarantees and credits by way of bank guarantees. These are measured in accordance with IAS 37, meaning that they are not treated as financial instruments in accordance with IFRS 9.

Of the provisions, holdings of € 1,398 million (previous year: € 1,167 million) have a residual maturity of more than one year.

Further details on provisions in the lending business can be found in Note 27.

€ 271 million of the provisions for restructuring (previous year: € 25 million) relate to personnel expenses and € 37 million (previous year: € 20 million) to operating expenses. The provisions were mainly set up in connection with the current restructuring programme resulting from the privatisation of Hamburg Commercial Bank. The amount of the provisions was estimated based on the expected utilisation of the restructuring programs. Depending on the actual utilisation of the restructuring programs, the amount set up as provisions may differ from the amount utilised.

Other provisions mainly comprise interest on tax liabilities, provisions from onerous contracts and provisions for regulatory expenses.

Changes in pension provisions are presented in Note 42.

Hamburg Commercial Bank had set up provisions for litigation risks and costs as at the balance sheet date. To determine for which claim the possibility of a loss is likely, and in order to estimate the amount of the potential payment obligations, Hamburg Commercial Bank takes a variety of factors into account. These include, among other things, the type of claim and the underlying facts of the case, the status of the individual proceedings, (provisional) decisions made by courts and arbitration bodies, the experience of Hamburg Commercial and third parties in comparable cases (insofar as they are known to the Bank), prior settlement negotiations, as well as the expert opinions and assessments of the Bank's internal and external legal advisors and other professionals.

A major portion of the provisions for litigation risks relates to the legal proceedings mentioned below. The current status of the proceedings and the expected outcome of the proceedings are taken into account for accounting purposes. It is not currently possible to predict how long the individual legal disputes will last or, as a result, the time at which the provisions will be used. Depending on the actual outcome of the proceedings, the actual amounts used may vary from the amounts set up as a provision.

Since 2005, Hamburg Commercial Bank AG has been involved in legal proceedings with a Turkish shipping group and up to now had to pay a total amount of 54 million US dollars in 2013 due to decisions of Turkish courts. Later on, the plaintiffs filed suits with Turkish courts asserting further claims for damages due to a loss of profit and due to third-party liabilities in connection with realisation measures relating to loan collateral furnished in favour of the Bank in respect of a loan.

In addition, Hamburg Commercial Bank AG is being sued for payment by a former borrower. In the fourth quarter of 2018, the plaintiff increased and adjusted the claims. The plaintiff is asserting various claims, in particular for the payment of damages and resulting from unjust enrichment in connection with measures taken by the Bank in respect of a problem loan. Various legal disputes have already been conducted in the past regarding material aspects of the facts on which the lawsuit is based.

In addition individual or groups of investors in hybrid financial instruments have filed lawsuits against the Bank in court and, in addition to seeking a decision rendering the termination invalid, are demanding, among other things, that the instruments be written up to the nominal value or that compensation be paid for lost interest payments.

Other provisions changed as follows:

Changes in other provisions

(€ m) 2018	For personnel expenses	In the lending business (non-financial instruments)	For restructuring	For litigation risks and costs	Other	Total
As at 1 January 2018	**24**	**14**[1]	**45**	**98**	**101**	**282**
Additions	21	2	282	164	165	634
Reversals	4	13	3	7	8	35
Other changes	–	–	–	–	–	–
Reclassifications	–	–	-9	–	1	-8
Changes in exchange rates	–	–	–	–	-1	-1
Utilisation in the financial year	13	–	7	5	156	181
As at 31 December 2018	**28**	**3**	**308**	**250**	**102**	**691**

[1] Due to the first-time application of IFRS 9, the opening balance of provisions in the lending business differs from the closing balance for the previous year. Further information on this can be found in the balance sheet item reconciliation from IAS 39 to IFRS 9 in the section entitled Reconciliation of impairments in accordance with IFRS 7.42P –
Off-balance-sheet transactions.

For information on the development of loan loss provisions for financial instruments reported under contingent liabilities in the current year, please refer to Note 50 (Schedule of loan loss provisions).

Changes in other provisions

(€ m) 2017	For personnel expenses	In the lending business	For restructuring	For litigation risks and costs	Other	Total
As at 1 January 2017	39	110	85	34	101	369
Additions	15	46	2	70	58	191
Reversals	6	83	9	4	25	127
Compounding	–	–	–	–	–	–
Reclassifications	-19	–	-19	–	–	-38
Changes in exchange rates	–	-4	-1	–	-1	-6
Utilisation in the financial year	5	2	13	2	32	54
As at 31 December 2017	24	67	45	98	101	335

42. Pension obligations and similar obligations

In recognising and measuring direct benefit pension plans, the net present value of the obligations is reduced by the fair value of the plan assets.

Provisions for pension obligations and similar obligations

(€ m)	2018	2017
Net present value of obligations, wholly or partly financed through funds	13	15
Net present value of obligations not financed through funds	990	1,097
Net present value of pension obligations and similar obligations	**1,003**	**1,112**
Fair value of plan assets	8	9
Pension plan net liability (provisions for pension obligations and similar obligations)	**995**	**1,103**

The net present value of defined benefit pension obligations has changed as follows:

Changes in net present value

(€ m)	2018	2017
Net present value as at 1 January	**1,112**	**1,161**
Actuarial losses/gains (–)		
due to changed financial assumptions	-56	-38
due to experience-based adjustments	-18	-8
due to demographic adjustments	11	–
Interest expenses	19	18
Past service cost	-1	–
Plan settlements	-27	–
Current service cost	8	12
Benefits paid	-50	-46
Reclassifications	5	13
Net present value as at 31 December	**1,003**	**1,112**

Early retirement arrangements were negotiated as part of the restructuring and associated reduction in staff and the corresponding provisions were transferred from restructuring to pension provisions.

The loss due to the change in demographic assumptions is attributable to the first-time application of the 2018 G Heubeck mortality tables.

In the past financial year, some Group companies transferred their pension obligations to an insurance company, which is shown under Net present value of plan settlements.

The fair value of plan assets has changed as follows:

Changes in fair value of plan assets

(€ m)	2018	2017
Fair value of plan assets as at 1 January	**9**	**9**
Actuarial gains	-1	–
Fair value of plan assets as at 31 December	**8**	**9**

The change in actuarial gains and losses was mainly attributable to an increase of the discount rate.

The total actuarial gains for the financial year before deferred taxes amounted to € 63 million (previous year: € 46 million). Allowing for deferred taxes, this results in a profit of € 44 million (previous year: € 28 million), which is recognised in Other comprehensive income and disclosed in retained earnings on an accumulated basis. As at 31 December 2018, the balance of actuarial gains/losses in retained earnings before tax amounted to € -122 million (previous year: € -196 million) and to € -83 million after tax (previous year: € -138 million).

Breakdown of plan assets

(€ m)	2018	2017
Qualified insurance policies	7	8
Debentures and other fixed-interest securities	1	1
Total	**8**	**9**

The debentures and other fixed-interest securities included in the plan assets are traded on an active market.

Expenses of € 26 million were incurred for defined benefit pension plans in the 2018 reporting year (previous year: € 30 million).

Pension obligations represent future amounts to be paid and are uncertain both as to the amount and the date they fall due. Future fluctuations in the present value of the pension obligations can result particularly from a change in the actuarial assumptions such as the discount rate and life expectancy. An increase or decrease in the actuarial assumptions (see Note 6) would have had the following impact on the present value of pension obligations as at 31 December 2018:

Sensitivity of pension obligations

(€ m)	Increase	Decrease
2018		
Discount rate (+/–0.25 %)	-40	43
Inflation trend[1] (+/–0.25 %)	35	-33
Life expectancy (+1 year)	42	

Sensitivity of pension obligations

(€ m)	Increase	Decrease
2017		
Discount rate (+/–0.25 %)	-40	49
Inflation trend[1] (+/–0.25 %)	39	-36
Life expectancy (+1 year)	47	

[1] A variation in the inflation trend affects the salary trend. An assumption regarding future salary levels has a direct influence on future pension levels because of the fully dynamic pension commitments. The salary and pension trends were therefore not separately varied.

The average duration of the pension obligations determined as at 31 December 2018 was used as the basis for the sensitivity calculations. The impact of the major assumptions on the present value of the pension obligations is presented. As the sensitivity analyses are based on the average duration of the expected pension obligations and expected payment dates are therefore not taken into account, the figures represent only approximate values. Furthermore, where a change in an actuarial assumption is analysed, the other assumptions are kept constant.

Hamburg Commercial Bank expects to make payments of € 51 million to beneficiaries under defined benefit pension plan commitments for the 2019 financial year (previous year: € 52 million).

The weighted average duration of the defined benefit obligation is 17.4 years as at 31 December 2018 (previous year: 18.0 years).

Expenses for defined contribution plans came to € 15 million in the 2018 reporting period (previous year: € 16 million). Payments to statutory pension schemes in the amount of € 13 million (previous year: € 14 million) are included in this figure.

43. Liabilities relating to disposal groups

Liabilities relating to disposal groups

(€ m)	2018	2017
Provisions	–	44
Other liabilities	–	2
Deferred tax liabilities	–	1
Total	**–**	**47**

All liabilities included in this item as at 31 December 2017 were attributable to the disposal groups from Aviation II and the disposal group consisting of the assets and liabilities of the FSL Group (see Note 33).

44. Current tax liabilities

Current tax liabilities

(€ m)	2018	2017
Provisions for income taxes	12	103
Total	**12**	**103**

Provisions for income taxes include tax liabilities for which no legally binding tax assessment notice has been received as at the balance sheet date. The year-on-year decline is due, in particular, to the assessment of prior-year taxes at the head office.

45. Deferred tax liabilities

For temporary differences in the tax bases of the following items in the statement of financial position deferred tax liabilities were created.

Deferred tax liabilities

(€ m)	2018	2017
Assets		
Loans and advances to banks	169	–
Loans and advances to customers	17	90
Credit derivative under the second loss guarantee	–	296
Financial investments	253	338
Trading assets	92	–
Positive fair values of hedging derivatives	56	84
Positive adjustment item from portfolio fair value hedges	64	82
Intangible assets	–	1
Other assets	–	1
Liabilities		
Liabilities to banks	10	28
Liabilities to customers	13	55
Securitised liabilities	–	4
Provisions	1	–
Other liabilities	20	68
Total	**695**	**1,047**
Netting off deferred tax assets	-695	-1,047
Total	**–**	**–**

The drop in deferred tax liabilities before netting mainly results from the change in existing temporary differences on the credit derivative from the second loss guarantee, financial investments, positive fair values of hedging derivatives, the positive adjustment item from portfolio fair value hedges and liabilities to customers.

€ 73 million of the total change is attributable to reductions recognised directly in equity relating to the measurement of receivables and financial investments.

Deferred tax liabilities of € 2 million (previous year: € 2 million) associated with investments in subsidiaries (so-called outside basis differences) were not recognised in accordance with IAS 12.39, as realisation is not probable.

46. Other liabilities

Other liabilities

(€ m)	2018	2017
Collateral provided for liabilities assumed	423	519
Liabilities for invoices outstanding	49	45
Deferred income	11	13
Personnel liabilities	8	8
Liabilities for restructuring	5	12
Other tax liabilities	5	7
Outstanding payments for the second loss guarantee	–	33
Other	17	21
Total	**518**	**658**

Other liabilities in the amount of € 431 million (previous year: € 658 million) have a residual maturity of more than one year.

The collateral provided for liabilities assumed serves to hedge leasing transactions of our customers with third parties.

€ 498 million of the liabilities reported here relate to financial instruments (previous year: € 638 million).

47. Subordinated capital

Subordinated capital

(€ m)	2018	2017
Subordinated liabilities	1,067	1,060
Maturing in less than two years	104	4
Silent participations	547	1,192
Total	**1,614**	**2,252**

Hamburg Commercial Bank reports subordinated liabilities and silent participations under subordinated capital.

Subordinated capital of € 1,540 million (previous year: € 2,248 million) have a residual maturity of more than one year.

The difference between the carrying amount of the liabilities designated as FVPL and their nominal value, which corresponds to the contractually agreed repayment amount at the due date, amounted to € 0 million as at 31 December 2018, as in the previous year.

As part of a capital restructuring measure, all of the Bank's silent participations were terminated in the year under review with a notice period of 2 years, i.e. with effect from 31 December 2020. The carrying amounts of silent participations decreased due to the reassessment of contractual cash flows and on the basis of assumptions and results of Hamburg Commercial Bank's business plan (IFRS 9.B5.4.6, previous year: IAS 39.AG8). In addition to hybrid instruments disclosed here, hybrid instruments are also disclosed in the line item Securitised liabilities (cf. Note 39).

48. Equity

Equity

(€ m)	2018	2017
Share capital	3,018	3,018
Capital reserve	75	75
Retained earnings	1,012	1,701
thereof: cumulative gains and losses arising from the revaluation of net defined benefit liabilities recognised in OCI	-122	-196
of which: Deferred taxes on cumulative gains and losses arising from the revaluation of net defined benefit liabilities recognised in OCI	39	58
Revaluation reserve	238	117
thereof: credit risk-induced changes in the value of liabilities designated at fair value (after taxes)	1	8
of which: Valuation results relating to financial assets classified as FVOCI as a mandatory requirement (after taxes)	237	n.r.
Thereof: from fair value measurement AfS	n.r.	109
Currency conversion reserve	22	2
Group net result	70	-535
Total before non-controlling interests	**4,435**	**4,378**
Non-controlling interests	2	-5
Total	**4,437**	**4,373**

Share capital

The share capital of Hamburg Commercial Bank is divided into 301,822,453 registered shares each representing a notional of € 10.00 of share capital. All the issued shares have been fully paid up.

As at 31 December 2018, several funds launched by Cerberus Capital Management L.P., New York, indirectly held a total of 42.50 % of the voting rights via three acquisition companies (Promontoria Holding 221 B.V. 9.89 %, Promontoria Holding 231 B.V. 13.88 % and Promontoria Holding 233 B.V. 18.73 %). Funds advised by J.C. Flowers & Co LLC, New York, indirectly hold a 35.00 % stake through JCF IV Neptun Holdings S.à r.l. as an acquisition company. In addition, a fund launched by Golden Tree Asset Management LP, New York, indirectly holds a share of 12.50 % in Hamburg Commercial Bank AG via GoldenTree Asset Management Lux S.à r.l. as an acquisition company, while Centaurus Capital LP, Houston, indirectly holds a share of 7.50 % via Chi Centauri LLC as an acquisition company. The remaining 2.5 % stake is held by BAWAG P.S.K. Bank für Arbeit und Wirtschaft und Österreichische Postsparkasse Aktiengesellschaft, Vienna.

In the previous year, HSH Beteiligungs Management GmbH, Hamburg, was the largest shareholder with 94.90 % of the voting rights. HSH Finanzfonds AöR – Gemeinsame Anstalt der Freien und Hansestadt Hamburg und des Landes Schleswig-Holstein – held an interest of 68.03 %, the Free and Hanseatic City of Hamburg, incl. the interest held indirectly via HGV Hamburger Gesellschaft für Vermögens- und Beteiligungsmanagement mbH held an interest of 11.30 %, the Federal State of Schleswig-Holstein held an interest of 10.02 % and Sparkassen- und Giroverband für Schleswig-Holstein held an interest of 5.55 % in Hamburg Commercial Bank AG, with all of these interests being held indirectly via HSH Beteiligungs Management GmbH. As at 31 December 2017, the nine groups of investors advised by J.C. Flowers & Co LLC held 5.10 % of the voting rights.

JCF IV Neptun Holdings S.à r.l., Luxembourg, informed us in November 2018 that it directly owned more than one quarter of the shares of Hamburg Commercial Bank AG pursuant to Section 20 (1) of the German Stock Corporation Act (AktG). In addition, the following companies and natural persons notified us in November 2018 that they indirectly owned more than one quarter of the shares of Hamburg Commercial Bank AG pursuant to Section 20 (1) sentence 1, sentence 2 in conjunction with Section 16 (4) AktG.

- JCF IV Europe S.à r.l.
- J.C. Flowers IV L.P.
- JCF Associates IV L.P.
- JCF Associates IV Ltd.
- Mr. James Christopher Flowers
- Mr. Stephen A. Feinberg

Neither Hamburg Commercial Bank AG nor any company dependent on it or majority-owned companies hold treasury stock. There are no cross-shareholdings as defined by Section 19 AktG.

Changes in ordinary shares

(Number of shares)	2018	2017
Number at the beginning of the year	301,822,453	301,822,453
Number at the end of the year	**301,822,453**	**301,822,453**

Retained earnings and dividends
The item Retained earnings mainly shows amounts allocated from previous year profits and the profits of the current year. There are no statutory reserves or legal reserves within the meaning of Section 150 (2) of the German Stock Corporation Act (AktG).

As was the case for the previous financial year 2017, no dividend payments were made for previous years during the current financial year 2018.

Capital reserve
There were no withdrawals from the capital reserve either in the year under review or in the previous year.

Revaluation reserve
The revaluation reserve includes the effects of credit risk-induced changes in the value of liabilities designated at fair value and the effects of the measurement of assets classified at fair value through other comprehensive income as a mandatory requirement.

In the previous year, the revaluation reserve included the effects of the measurement of AfS financial instruments disclosed at fair value directly in equity.

The changes in value associated with deferred taxes shown in the revaluation reserve are also presented in the revaluation reserve pursuant to IAS 12.61A.

Currency conversion reserve
Assets and liabilities in financial statements of subsidiaries in foreign currencies are translated at the reporting date exchange rate in preparing the Group financial statements, while average rates for the reporting period are used to translate expenses and income. Equity is translated at historical rates, with the exception of revaluation reserves in Group financial statements reported in foreign currencies, which are translated at the reporting date exchange rate.

Any differences arising from this method of translation compared to complete translation at the reporting date exchange rate are reported in this Equity item.

Capital management
The capital management of Hamburg Commercial Bank aims to comply with regulatory capital ratios. In addition to these requirements, capital management is used as the basis for complying with the capital ratios planned and is designed to ensure that the Bank's capital base also meets the requirements imposed by the Bank's stakeholders. The common equity Tier 1 capital ratio is the main parameter for capital management.

The regulatory capitalisation is in accordance with the provisions of the European Capital Requirements Regulation (CRR) in conjunction with the Supervisory Review and Evaluation Process (SREP). Hamburg Commercial Bank determines the capital requirements for counterparty risk in accordance with the approach permitted by the Federal Financial Supervisory Authority based on internal ratings (Advanced IRBA) and based on the CSA (standard approach). The capital base is reported to the regulatory authorities quarterly. The capital ratios required under supervisory law were complied with on each reporting date in the course of the year under review.

Regulatory figures[1)]

(%)	2018	2017
Overall capital ratio	23.3	31.4
Tier 1 capital ratio	18.4	23.2
CET1 capital ratio	18.4	18.7

[1)] Values before adoption of the Group financial statements of Hamburg Commercial Bank.

The regulatory capital commitment was monitored closely both at Bank and division level in the course of the financial year.

As part of the regulatory restructuring of the capital structure, all silent participations of the Bank and, as a result, all silent participations subject to the regulatory phase-out provisions for additional Tier 1 capital pursuant to Art. 486 CRR were terminated in the year under review with a notice period of two years, i.e. with effect from 31 December 2020. As a result, the remaining regulatory recognition of hybrid instruments as AT1/T2 capital for the regulatory capital ratios under the CRR and SREP requirements no longer applies at the end of the 2018 financial year. The positive valuation effect resulting from the necessary reassessment of the cash flows of hybrid financial instruments leads to a significant strengthening of the Common Equity Tier 1 capital in the 2018 financial year.

Segment reporting

49. Segment report

(€ m / %)	Corporate Clients		Real Estate		Shipping		Treasury & Markets		Core Bank (total)	
	2018	2017	2018	2017	2018	2017	2018	2017	2018	2017
Net interest income	168	162	168	178	95	85	86	139	517	564
Net commission income	44	49	14	13	13	14	-4	1	67	77
Result from hedging	–	–	–	–	–	8	–	–	–	–
Result from financial instruments categorised as FVPL	7	39	4	24	–	8	70	83	81	154
Net income from financial investments including other income items	3	–	3	–	–	–	66	350	72	350
Total income	**222**	**250**	**189**	**215**	**108**	**107**	**218**	**573**	**737**	**1,145**
Loan loss provisions incl. credit derivative under the second loss guarantee1[1]	-54	-53	-55	2	-205	63	16	1	-298	13
Administrative expenses	-122	-118	-57	-51	-35	-39	-74	-84	-288	-292
Other operating result	7	4	3	1	–	1	1	2	11	8
Expenses for regulatory affairs, deposit guarantee fund and banking associations	-7	-7	-8	-9	-4	-4	-8	-10	-27	-30
Net income before restructuring and privatisation	46	76	72	158	-136	128	153	482	135	844
Net income from restructuring and privatisation	**–**	**–**	**–**	**–**	**–**	**–**	**–**	**–**	**–**	**–**
Expenses for government guarantees	-12	-3	-5	-1	-20	-18	-4	–	-41	-22
Net income before taxes	34	73	67	157	-156	110	149	482	94	822
Cost/income ratio (CIR)	**53%**	**46%**	**30%**	**24%**	**32%**	**36%**	**34%**	**15%**	**39%**	**25%**
Return on equity before taxes	2%	5%	8%	16%	-25%	29%	24%	69%	3%	23%
Average equity	1,437	1,460	884	972	625	378	614	701	3,560	3,511

(€ bn)	2018	2017	2018	2017	2018	2017	2018	2017	2018	2017
Segment assets	**11.5**	**11.6**	**12.4**	**10.3**	**4.5**	**5.1**	**19.3**	**21.4**	**47.7**	**48.4**

[1] Summary of "Loan loss provisions" and "Hedging effect of credit derivative under the second loss guarantee

(€ m/%)	Core Bank		Non-Core Bank		Other and Consolidation[2]		Group	
	2018	2017	2018	2017	2018	2017	2018	2017
Net interest income	517	564	172	23	903	293	1,592	880
Net commission income	67	77	1	20	-33	-32	35	65
Result from hedging	–	–	–	–	-9	-18	-9	-18
Result from financial instruments categorised as FVPL	81	154	-184	84	-33	16	-136	254
Net income from financial investments including other income items	72	350	–	-48	32	64	104	366
Total income	**737**	**1,145**	**-11**	**79**	**860**	**323**	**1,586**	**1,547**
Loan loss provisions incl. credit derivative under the second loss guarantee[1]	-298	13	7	-1,295	-76	6	-367	-1,276
Administrative expenses	-288	-292	-117	-190	3	1	-402	-481
Other operating result	11	8	-12	-10	-106	23	-107	21
Expenses for regulatory affairs, deposit guarantee fund and banking associations	-27	-30	-2	-7	-60	-12	-89	-49
Net income before restructuring and privatisation	**135**	**844**	**-135**	**-1,423**	**621**	**341**	**621**	**-238**
Net income from restructuring and privatisation	–	–	–	–	-366	-66	-366	-66
Expenses for government guarantees	-41	-22	-118	-127	1	–	-158	-149
Net income before taxes	**94**	**822**	**-253**	**-1,550**	**256**	**275**	**97**	**-453**
Cost/income ratio (CIR)	39%	25%	–	–	–	–	27%	31%
Return on equity before tax	3%	23%	–	–	–	–	2%	-10%
Average equity	3,560	3,511	441	866	329	284	4,330	4,662

(€ bn)	2018	2017	2018	2017	2018	2017	2018	2017
Segment assets[3]	**47.7**	**48.4**	**0.2**	**11.7**	**7.2**	**10.3**	**55.1**	**70.4**

[1] Summary of "Loan loss provisions" and "Hedging effect of credit derivative under the second loss guarantee.

[2] Consolidation includes, among other things, reconciliation effects resulting from differences in recognition between the internal management system and IFRS accounting.

[3] Segment assets of the Non-Core Bank following transfer to the sphere of the buyers in the context of privatisation

(€ m/%)	2018			2017		
	Other	Consolidation[2]	Total Other and Consolidation	Other	Consolidation[2]	Total Other and Consolidation
Net interest income	908	-5	903	267	26	293
Net commission income	-29	-4	-33	-27	-5	-32
Result from hedging	–	-9	-9	-	-18	-18
Result from financial instruments categorised as FVPL	14	-47	-33	5	11	16
Net income from financial investments including other income items	33	-1	32	66	-2	64
Total income	**926**	**-66**	**860**	**311**	**12**	**323**
Loan loss provisions incl. credit derivative under the second loss guarantee[1]	2	-78	-76	1	5	6
Administrative expenses	3	–	3	1	–	1
Other operating income	-107	1	-106	24	-1	23
Expenses for regulatory affairs, deposit guarantee fund and banking associations	-62	2	-60	-14	2	-12
Net income before restructuring and privatisation	**762**	**-141**	**621**	**323**	**18**	**341**
Net income from restructuring and privatisation	–	-366	-366	-	-66	-66
Expenses for government guarantees	–	1	1	–	–	–
Net income before taxes	**762**	**-506**	**256**	**323**	**-48**	**275**
Cost/income ratio (CIR)	–	–	–	–	–	–
Return on equity before tax	–	–	–	–	–	–
Average equity	329	–	329	284	–	284

(€ bn)	2018			2017		
Segment assets	**7.2**	**–**	**7.2**	**10.3**	**–**	**10.3**

[1] Summary of "Loan loss provisions" and "Hedging effect of credit derivative under the second loss guarantee.
[2] Consolidation includes, among other things, reconciliation effects resulting from differences in recognition between the internal management system and IFRS accounting.

Segment reporting is in accordance with the provisions of IFRS 8. The Group has five segments subject to a reporting requirement: four in the Core Bank, and the Non-Core Bank. The Core Bank segments result from the Bank's internal organisational structure which is based on product and customer groups and which corresponds to the delimitation for internal Group management purposes. The formation of the segments is intended to achieve the greatest possible homogeneity of customer groups with regard to a focused loan financing product range as well as other products and services.

Hamburg Commercial Bank's Core Bank consists of the segments Real Estate, Shipping, Corporate Clients and Treasury & Markets. The business activities of the Real Estate, Shipping and Corporate Clients customer departments focus on offering financing solutions in the lending business.

The Real Estate segment includes business with real estate clients, while the Shipping segment includes the business with shipping clients. In the Corporate Clients segment, the strategic focus is on the Energy & Infrastructure, Trade & Food, Healthcare, Industry & Services and Wealth Management business areas. In addition, the business unit offers the consultancy areas of structured financing, leveraged buy-out and mergers & acquisitions from a single source for all clients of the Bank.

The Treasury & Markets segment supports the customer departments in their business by providing a tailored range of capital market-oriented product solutions and within the framework of syndications.

At the same time, support is provided to the savings banks and institutional clients in the areas of issuance and deposits. This segment is also responsible for the central management of the liquidity and market price risks relating to the Bank's positions and the Bank's function as an issuer.

The results of the Non-Core Bank are related to the lending and capital market transactions which were transferred to the sphere of the buyers when the privatisation process was closed.

In preparation for the closing, a total of € 2.5 billion (thereof € 0.4 billion in NPE volume) of transactions not included in the portfolio transaction was transferred from the Non-Core Bank to the Core Bank in the first half of 2018. Most of these loans are healthy portfolios that were previously allocated to the non-strategic business and will remain within the Bank in the future. The prior-year figures were not adjusted, as the effects on the Core Bank segments are not material and the costs associated with adjusting the Non-Core Bank are disproportionately high.

The expenses for regulatory affairs, the deposit guarantee fund and banking associations are allocated to the segments based on the adjusted balance sheet volume. The provisions set up in 2018 for expected one-off payments to the Association of German Banks (*Bundesverband deutscher Banken*) were reported under Other in deviation from the above.

Loan loss provisions are shown in the segments in which they originated. Since the introduction of IFRS 9 in 2018, the hedging effect of the second loss guarantee on the balance sheet has resulted in compensation effects relating to the items Result from financial instruments categorised as FVPL and Loan loss provisions, have virtually no effect on income overall and are presented under Consolidation. These delayed compensation effects are related to the privatisation process and result from the ongoing guarantee settlement/the guarantee settlement report dated 15 June 2018.

By way of derogation from this principle, the guarantee fees are allocated to the segments based on the regulatory equity capital requirements for the guaranteed portfolio.

Overall bank items, as well as administration and service divisions, are disclosed as segments not subject to reporting requirements in the "Other" column. Overall bank items include, among other things, the liquidity buffer to be maintained in accordance with the Minimum Requirements for Risk Management (MaRisk) and the effects from equity. In the 2018 financial year, the measurement of hybrid instruments had a significant positive impact on total income (see Note 8). The administration and service divisions also include the Transaction Banking product division, which offers tailor-made services in the fields of payment transactions, account management and foreign trade for the customer departments, insofar as these activities were not allocated to the reportable segments as part of the business management of the Bank.

The "Consolidation column contains effects from different accounting methods between the parameters reported internally and the presentation in the Group financial statements. The reconciliation effects included are shown separately in the table above pursuant to IFRS 8.28 and are explained in further detail below.

Net interest income for the purpose of internal reporting to management is calculated in accordance with the Fund Transfer Pricing (FTP). The planned investment and financing profit is distributed among the business segments on the basis of economic capital committed. The transformation contribution mainly includes the results from the liquidity management of the banking book and, as a result, the temporary burdens resulting from the increase in liquidity and funding structure during the privatisation phase, in particular. As of 2018, the transformation contribution is reported centrally under Other in line with the internal management and is no longer allocated to the segments. The figures for the previous year have been adjusted accordingly.

Reconciliation effects relating to net interest income in the amount of € -5 million are due largely to valuation differences. These are largely the result of the use of internal transactions within the framework of internal interest rate and liquidity management/the consideration of imputed interest rate margins (fund transfer pricing, FTP)) instead of gross interest in the lending business. Further reconciliation effects result, in particular, from the use of what are, in some cases, different calculation and amortisation methods within the context of internal reporting. In addition, in the internal management system, the measurement results of the hedging derivatives in hedge accounting are only recognised upon the disposal of AC or FVOCI positions, whereas under the IFRS hedge accounting regulations, the hedge adjustments are continuously amortised within Net interest income.

The reconciliation effects of the Result from financial instruments categorised as FVPL (€ -47 million) include not only subsequent compensation effects but also the differences resulting from the presentation of capital market transactions between the internal management system and IFRS accounting, as well as from the hedging of certain financial instruments that are included in the portfolio fair value hedge in full in the internal recognition of the interest rate hedge transaction, whereas under the IFRS, they are not, or are only partly, included in the portfolio fair value hedge.

In addition, Net income from restructuring and privatisation is also shown in full under Consolidation as an item for reconciliation with the internally managed values.

Total income recognised in the segments is exclusively generated from business conducted with external customers.

Geographical information as well as information on income from external clients for each product and service is not collected for management reporting due to a lack of management relevance and disproportionately high costs, whereby disclosures in accordance with IFRS 8.32 and 8.33 are not made.

The cost/income ratio (CIR) and return on equity (RoE) are not shown in the segment report for the Non-Core Bank segment. In the case of the Non-Core Bank, the segment involves business areas which are not strategic and are currently being wound down. This segment is not managed on the basis of these ratios.

The allocation key for the allocation of the average reported equity capital to the segments is the regulatory capital commitment, taking into account the termination of the guarantee, due to its management relevance.

The CIR is calculation as the ratio of Administrative expenses, taking into account the prior-year adjustment (see Note 3), to Total income plus Other operating income. Return on equity is the ratio of net income before taxes to average equity capital.

Information on the companies consolidated under the equity method which are shown under Net income from financial investments including other income items in the segment report can be found in Note 14.

Disclosures on financial instruments

50. Information on the development of loan loss provisions and the carrying amounts of financial instruments not measured at fair value through profit or loss

The following table shows the development of the gross carrying amounts of financial instruments not measured at fair value through profit or loss in the balance sheet items "Loans and advances to banks", "Loans and advances to customers", "Financial investments", "Assets held for sale" and for the off-balance sheet business.

The development of loan loss provisions for financial instruments not measured at fair value through profit or loss is also shown separately by balance sheet item. Only the loan loss provisions for the financial instruments categorised as AC are shown under loan loss provisions in the balance sheet item Loan loss provisions. Loan loss provisions for financial instruments categorised as FVOCI are shown in net terms directly in the carrying amount of the financial instruments under the items "Loans and advances to banks", "Loans and advances to customers" and "Financial investments" (see Note 7).

Development in gross carrying amounts for loans and advances to banks

(€ m)	2018				
	Insignificant increase in the loan default risk (12-month ECL)	Significant increase in the loan default risk (LECL level 2)	Credit-impaired (LECL level 3)	Loans purchased or originated credit-impaired (POCI)	Total
Carrying amounts as at 1 January 2018	**3,761**	**5**	**–**	**–**	**3,766**
thereof AC	3,556	5	–	–	3,561
thereof FVOCI	205	–	–	–	205
New additions and increases	861	12	–	–	873
thereof AC	861	12	–	–	873
Repayments, disposals and sales	1,451	17	–	–	1,468
thereof AC	1,416	17	–	–	1,433
thereof FVOCI	35	–	–	–	35
Exchange rate changes	1	–	–	–	1
thereof AC	2	–	–	–	2
thereof FVOCI	-1	–	–	–	-1
FV changes	-3	–	–	–	-3
thereof FVOCI	-3	–	–	–	-3
Changes in the scope of consolidation	-3	–	–	–	-3
thereof AC	-3	–	–	–	-3
Carrying amounts as at 31 December 2018	**3,166**	**–**	**–**	**–**	**3,166**
thereof AC	3,000	–	–	–	3,000
thereof FVOCI	166	–	–	–	166

Development in loan loss provisions for loans and advances to banks

(€ m)	2018				
	Insignificant increase in the loan default risk (12-month ECL)	Significant increase in the loan default risk (LECL level 2)	Credit-impaired (LECL level 3)	Loans purchased or originated credit-impaired (POCI)	Total
Loan loss provisions on 1 January 2018	**1**	**–**	**–**	**–**	**1**
Reversals due to disposals, repayments and other reductions	1	–	–	–	1
Loan loss provisions on 31 December 2018	**–**	**–**	**–**	**–**	**–**

Development in gross carrying amounts for loans and advances to customers

(€ m)	2018				
	Insignificant increase in the loan default risk (12-month ECL)	Significant increase in the loan default risk (LECL level 2)	Credit-impaired (LECL level 3)	Loans purchased or originated credit-impaired (POCI)	Total
Carrying amounts as at 1 January 2018	**28,441**	**2,743**	**1,700**	**–**	**32,884**
thereof AC	26,095	2,724	1,700	–	30,519
thereof FVOCI	2,270	19	–	–	2,289
thereof receivables under finance leases	76	–	–	–	76
Transfer to LECL level 2	-1,067	1,293	-226		–
thereof AC	-1,067	1,293	-226		–
Transfer to LECL level 3	-36	-423	459		–
thereof AC	-36	-423	459		–
Transfer to 12-month ECL	482	-149	-333		–
thereof AC	482	-149	-333		–
New additions and increases	10,274	520	262	–	11,056
thereof AC	10,274	520	262	–	11,056
Utilisation and impairment	–	–	492	–	492
thereof AC	–	–	492	–	492
Repayments, disposals and sales	10,089	1,016	445	–	11,550
thereof AC	9,853	1,005	445	–	11,303
thereof FVOCI	229	11	–	–	240
thereof receivables under finance leases	7	–	–	–	7
Exchange rate changes	207	48	30	–	285
thereof AC	199	48	30	–	277
thereof FVOCI	4	–	–	–	4
thereof receivables under finance leases	4	–	–	–	4
FV changes	-60	1	–	–	-59
thereof FVOCI	-60	1	–	–	-59
Carrying amounts as at 31 December 2018	**28,152**	**3,017**	**955**	**–**	**32,124**
thereof AC	26,094	3,008	955	–	30,057
thereof FVOCI	1,985	9	–	–	1,994
thereof Receivables under finance lease transactions	73	–	–	–	73

Development in loan loss provisions for loans and advances to customers

(€ m)	2018				
	Insignificant increase in the loan default risk (12-month ECL)	Significant increase in the loan default risk (LECL level 2)	Credit-impaired (LECL level 3)	Loans purchased or originated credit-impaired (POCI)	Total
Loan loss provisions on 1 January 2018	**61**	**216**	**700**	**–**	**977**
Transfer to LECL level 2	-12	12	–		–
Transfer to LECL level 3	–	-21	21		–
Transfer to 12-month ECL	12	-12	–		–
Reversals due to disposals, repayments and other reductions	49	134	149	–	332
Additions due to new additions and other increases	81	180	373	–	634
Utilisation	–	–	474	–	474
Change in line with effective interest rate	–	–	13	–	13
Exchange rate changes	1	–	12	–	13
Loan loss provisions on 31 December 2018	**94**	**241**	**496**	**–**	**831**

In the reporting period, changes in loans and advances to customers relate only to transactions categorised as AC.

Development in gross carrying amounts for financial investments

(€ m)	2018				
	Insignificant increase in the loan default risk (12-month ECL)	Significant increase in the loan default risk (LECL level 2)	Credit-impaired (LECL level 3)	Loans purchased or originated credit-impaired (POCI)	Total
Carrying amounts as at 1 January 2018	**12,664**	**250**	**–**	**–**	**12,914**
thereof AC	103	–	–	–	103
thereof FVOCI	12,561	250	–	–	12,811
Transfer to 12-month ECL	53	-53	–		–
thereof FVOCI	53	-53	–		–
New additions and increases	519	4	–	–	523
thereof AC	31	3	–	–	34
thereof FVOCI	488	1	–	–	489
Repayments, disposals and sales	3,771	152	–	–	3,923
thereof AC	20	3	–	–	23
thereof FVOCI	3,751	149	–	–	3,900
Exchange rate changes	-1	–	–	–	-1
thereof FVOCI	-1	–	–	–	-1
FV changes	-51	6	–	–	-45
thereof FVOCI	-51	6	–	–	-45
Carrying amounts as at 31 December 2018	**9,413**	**55**	**–**	**–**	**9,468**
thereof AC	114	–	–	–	114
thereof FVOCI	9,299	55	–	–	9,354

Development in loan loss provisions for financial investments

(€ m)	2018				
	Insignificant increase in the loan default risk (12-month ECL)	Significant increase in the loan default risk (LECL level 2)	Credit-impaired (LECL level 3)	Loans purchased or originated credit-impaired (POCI)	Total
Loan loss provisions on 1 January 2018	**–**	**7**	**–**	**–**	**7**
Reversals due to disposals and other reductions	–	5	–	–	5
Additions due to new additions and other increases	–	3	–	–	3
Loan loss provisions on 31 December 2018	**–**	**5**	**–**	**–**	**5**

In the reporting period, changes in financial investments relate only to transactions categorised as FVOCI.

Development in gross carrying amounts of non-current assets held for sale and disposal groups

(€ m)	31/12/2018				
Carrying amounts IFRS	Insignificant increase in the loan default risk (12-month ECL)	Significant increase in the loan default risk (LECL level 2)	Credit-impaired (LECL level 3)	Loans purchased or originated credit-impaired (POCI)	Total
Carrying amounts on 1 January 2018	**2**	**–**	**–**	**–**	**2**
thereof AC	2	–	–	–	2
Changes in the scope of consolidation	-2	–	–	–	-2
thereof AC	-2	–	–	–	-2
Carrying amounts on 31 December 2018	**–**	**–**	**–**	**–**	**–**
thereof AC	–	–	–	–	–

Carrying amounts of off-balance sheet business

(€ m)	2018			
	Insignificant increase in the loan default risk (12-month ECL)	Significant increase in the loan default risk (LECL level 2)	Credit-impaired (LECL level 3)	Total
Carrying amounts as at 1 January 2018	**7,152**	**252**	**199**	**7,603**
Transfer to LECL level 2	-92	95	-3	–
Transfer to LECL level 3	-6	-1	7	–
Transfer to 12-month ECL	23	-23	–	–
New joiners	7,972	280	40	8,292
Disposals	6,971	219	167	7,357
Exchange rate changes	32	2	1	35
Carrying amounts as at 31 December 2018	**8,110**	**386**	**77**	**8,573**

Development in loan loss provisions for off-balance-sheet business

(€ m)	2018			
	Insignificant increase in the loan default risk (12-month ECL)	Significant increase in the loan default risk (LECL level 2)	Credit-impaired (LECL level 3)	Total
Loan loss provisions on 1 January 2018	**8**	**2**	**46**	**56**
Reversals due to disposals and other reductions	9	2	18	29
Additions due to new additions and other increases	7	6	27	40
Utilisation	–	–	8	8
Exchange rate changes	–	–	1	1
Loan loss provisions on 31 December 2018	**6**	**6**	**48**	**60**
Thereof provisions for contingent liabilities	1	–	9	10
Thereof provisions for irrevocable loan commitments	5	6	19	30
Thereof other loan provisions	–	–	20	20

51. Residual maturity breakdown of financial instruments

When determining the residual maturities of financial liabilities for purposes of presenting liquidity risk, the contractually agreed maturity dates of non-discounted cash flows are used as the basis.

(€ m) 2018	Payable on demand	Up to 3 months	3 months to 1 year	1 year to 5 years	More than 5 years	Total
Liabilities						
Liabilities to banks	442	615	370	2,330	1,843	5,600
Liabilities to customers	8,095	6,653	6,202	4,783	3,840	29,573
Securitised liabilities	1	418	2,265	6,278	726	9,688
Negative fair value of hedging derivatives	–	32	80	259	228	599
Trading liabilities	9	275	486	1,505	1,229	3,504
of which: derivatives	9	275	486	1,505	1,229	3,504
Other liabilities	3	58	27	425	6	519
Subordinated capital	–	2	56	943	1,168	2,169
Contingent liabilities	1,748	–	–	–	–	1,748
Irrevocable loan commitments	7,627	–	–	–	–	7,627
Total	**17,925**	**8,053**	**9,486**	**16,523**	**9,040**	**61,027**

(€ m) 2017	Payable on demand	Up to 3 months	3 months to 1 year	1 year to 5 years	More than 5 years	Total
Liabilities						
Liabilities to banks	639	2,802	1,058	2,225	1,832	8,556
Liabilities to customers	10,986	10,739	4,717	6,956	4,768	38,166
Securitised liabilities	1	1,252	2,642	6,764	3,213	13,872
Negative fair value of hedging derivatives	–	23	41	134	16	214
Trading liabilities	8	343	500	1,698	1,654	4,203
of which: derivatives	8	343	500	1,698	1,654	4,203
Liabilities relating to disposal groups	–	–	3	–	–	3
Other liabilities	9	59	56	523	6	653
Subordinated capital	–	1	13	229	2,800	3,043
Contingent liabilities	1,862	–	–	–	–	1,862
Irrevocable loan commitments	6,367	–	–	–	–	6,367
Total	**19,872**	**15,219**	**9,030**	**18,529**	**14,289**	**76,939**

Interest rate swaps, cross currency interest rate swaps and equity swaps are presented on the basis of their future net payment obligations. Other derivatives are assigned to maturity bands by overall maturity at their carrying amount.

Liquidity management is described in detail in the Risk report section of the Group management report.

52. Disclosure of fair value in accordance with IFRS 7 and IFRS 13

I. Fair values of financial instruments

The section below shows the fair values of the financial assets and liabilities presented by category of financial instrument, compared with the carrying amounts and divided into the three levels of the measurement hierarchy in accordance with IFRS 13.

Fair values of financial Instruments

Assets

(€ m) 2018	Carrying amount	Fair value	Level 1	Level 2	Level 3
FVOCI Mandatory	**11,510**	**11,705**	**8,169**	**3,326**	**15**
Loans and advances to banks	167	167	–	167	–
Loans and advances to customers	1,994	1,994	–	1,994	–
Financial investments[1]	9,349	9,544	8,169	1,165	15
FVPL Designated	**216**	**216**	**–**	**216**	**–**
Loans and advances to customers	120	120	–	120	–
Financial investments	96	96	–	96	–
FVPL Held For Trading	**3,094**	**3,094**	**147**	**2,656**	**291**
Trading assets	3,094	3,094	147	2,656	291
FVPL Other	**1,096**	**1,096**	**8**	**579**	**509**
Loans and advances to customers	547	547	–	136	411
Financial investments	541	541	8	443	90
Non-current assets held for sale and disposal groups	8	8	–	–	8
AC assets	**37,735**	**38,359**	**–**	**11,462**	**26,897**
Cash reserve	5,362	5,362	–	5,362	–
Loans and advances to banks	3,000	3,007	–	2,956	51
Loans and advances to customers	29,226	29,843	–	3,020	26,823
Financial investments	114	114	–	91	23
Other assets	33	33	–	33	–
No IFRS 9 category	**448**	**248**	**–**	**175**	**–**
Positive fair values of hedging derivatives	175	175	–	175	–
Receivables under finance leases	73	73	n.r.	n.r.	n.r.
Value adjustments from the portfolio fair value hedge	200	–	n.r.	n.r.	n.r.
Total assets	**54,099**	**54,718**	**8,324**	**18,414**	**27,712**

[1] The difference between the carrying amount and fair value of the financial investments classified as FVOCI as a mandatory requirement amounts to € 195 million. This amount is offset by the separately reported reconciling item from the portfolio fair value hedge in the amount of € 200 million, € 195 million of which is attributable to FVOCI financial investments. It corresponds to the effective portion of the hedging relationship recognised through profit or loss and is therefore not included in the carrying amount.

The carrying amounts of loans and advances to banks and loans and advances to customers classified as AC HTC are shown less the loan loss provisions disclosed on the balance sheet, since fair value also reflects possible impairments.

The effective portions of the hedging relationship recognised through profit or loss are disclosed in the Value adjustments from the portfolio fair value hedge item, of which € 195 million is accounted for by financial investments classified as FVOCI as a mandatory requirement (previous year: € 243 million) and € 5 million (previous year: € 12 million) by loans and advances to banks and customers classified as AC HTC.

Fair values of financial Instruments

Assets

(€ m) 2017	Carrying amount	Fair value	Level 1	Level 2	Level 3
Held for Trading (HfT)	**4,655**	**4,655**	**81**	**3,229[2)]**	**1,345[2)]**
Trading assets	3,641	3,641	81	3,229[2)]	331[2)]
Credit derivative under the second loss guarantee	1,014	1,014	–	–	1,014
Designated at Fair Value (DFV)	**1,867**	**1,867**	**–**	**1,734[2)]**	**133[2)]**
Loans and advances to customers	1,255	1,255	–	1,170[2)]	85[2)]
Financial investments	612	612	–	564[2)]	48[2)]
Available for Sale (AfS)	**12,705**	**12,948**	**11,322**	**1,210**	**173**
Cash reserve	106	106	–	106	–
Loans and advances to banks	79	79	–	36	43
Loans and advances to customers	45	45	–	–	45
Financial investments[1)]	12,475	12,718	11,322	1,068	85
LaR assets	**44,203**	**44,503**	**21[2)]**	**13,801**	**30,681**
Cash reserve	6,519	6,519	–	6,519	–
Loans and advances to banks	3,758	3,764	–	3,676	88
Loans and advances to customers	33,305	33,519	–	2,955	30,564
Financial investments	560	640	21[2)]	602	17
Other assets	35	35	–	35	–
Non-current assets held for sale and disposal groups	26	26	–	14	12
No IAS 39 category	**595**	**340**	**–**	**264**	**–**
Positive fair values of hedging derivatives	264	264	–	264	–
Receivables under finance leases	76	76	n.r.	n.r.	n.r.
Value adjustments from the portfolio fair value hedge	255	–	n.r.	n.r.	n.r.
Total assets	**64,025**	**64,313**	**11,424**	**20,238**	**32,332**

1) The difference between the carrying amount and fair value of financial investments classified as AfS amounts to € 243 million. This amount is offset by the separately reported reconciling item from the portfolio fair value hedge in the amount of € 255 million, € 243 million of which is attributable to AfS financial investments. It corresponds to the effective portion of the hedging relationship recognised through profit or loss and is therefore not included in the carrying amount.

2) The value as at 31 December 2017 was adjusted. Please refer to Note 3 for more details.

The carrying amounts of loans and advances to banks and loans and advances to customers classified as LaR are shown less the loan loss provisions disclosed on the balance sheet, since fair value also reflects possible impairments.

Fair values of financial Instruments

Liabilities

(€ m) 2018	Carrying amount	Fair value	Level 1	Level 2	Level 3
FVPL Designated	**2,181**	**2,181**	**–**	**1,323**	**858**
Liabilities to banks	124	124	–	16	108
Liabilities to customers	746	746	–	362	384
Securitised liabilities	1,311	1,311	–	945	366
FVPL Held For Trading	**2,812**	**2,812**	**–**	**2,719**	**93**
Trading liabilities	2,812	2,812	–	2,719	93
AC liabilities	**42,953**	**44,079**	**–**	**43,158**	**921**
Liabilities to banks	5,346	5,258	–	5,203	55
Liabilities to customers	27,347	28,104	–	27,859	245
Securitised liabilities	8,147	8,351	–	8,248	103
Other liabilities	499	499	–	499	–
Subordinated capital	1,614	1,867	–	1,349	518
No IFRS 9 category	**961**	**501**	**–**	**501**	**–**
Negative fair value of hedging derivatives	501	501	–	501	–
Value adjustments from the portfolio fair value hedge	460	–	n.r.	n.r.	n.r.
Total liabilities	**48,907**	**49,573**	**–**	**47,701**	**1,872**

Fair values of financial Instruments

Liabilities

€ m 2017	Carrying amount	Fair value	Level 1	Level 2	Level 3
Held for Trading (HfT)	**3,875**	**3,875**	**–**	**3,708[1)]**	**167[1)]**
Trading liabilities	3,875	3,875	–	3,708	167[1)]
Designated at Fair Value (DFV)	**2,564**	**2,564**	**–**	**1,676[1)]**	**888[1)]**
Liabilities to banks	118	118	–	11	107
Liabilities to customers	819	819	–	398[1)]	421[1)]
Securitised liabilities	1,627	1,627	–	1,267[1)]	360[1)]
Other liabilities (LIA)	**57,248**	**57,877**	**–**	**56,127**	**1,750**
Liabilities to banks	8,153	8,054	–	7,570	484
Liabilities to customers	35,386	36,194	–	35,734	460
Securitised liabilities	10,817	10,786	–	10,786	–
Liabilities relating to disposal groups	2	2	–	–	2
Other liabilities	638	638	–	638	–
Subordinated capital	2,252	2,203	–	1,399	804
No IAS 39 category	**716**	**163**	**–**	**163**	**–**
Negative fair value of hedging derivatives	163	163	–	163	–
Value adjustments from the portfolio fair value hedge	553	–		n.r.	
Total liabilities	**64,403**	**64,479**	**–**	**61,674**	**2,805**

[1)] The value as at 31 December 2017 was adjusted. Please refer to Note 3 for more details.

In the period under review financial instruments measured at fair value were transferred from one hierarchy level to another. These transfers are shown below together with the carrying amounts at the time of transfer for each class of financial instruments.

Transfer, assets

(€ m) 2018	Transfer to level 1	Transfer from level 1	Transfer to level 2	Transfer from level 2	Transfer to level 3	Transfer from level 3
Loans and advances to customers						
thereof FVPL Other	–	–	–	-19	19	–
Credit derivative under the second loss guarantee	–	–	969	–	–	-969
Trading assets (FVPL Trading)	25	-64	67	-27	2	-3
Financial investments						
thereof FVOCI Mandatory	536	-1,079	1,079	-536	–	–
thereof FVPL Other	–	–	23	–	–	-23
Total	**561**	**-1,143**	**2,138**	**-582**	**21**	**-995**

Transfer, assets

(€ m) 2017	Transfer to level 1	Transfer from level 1	Transfer to level 2	Transfer from level 2	Transfer to level 3	Transfer from level 3
Trading assets (HfT)	39	-27	27	-79	40	–
Financial investments (excl. equity instruments measured at cost)						
AfS	5,744	-4,218	4,218	-5,744	–	–
Total	**5,783**	**-4,245**	**4,245**	**-5,823**	**40**	**–**

Transfer, liabilities

(€ m) 2018	Transfer to level 1	Transfer from level 1	Transfer to level 2	Transfer from level 2	Transfer to level 3	Transfer from level 3
Trading liabilities (FVPL Trading)	–	–	–	1	–	-1
Total	**–**	**–**	**–**	**1**	**–**	**-1**

Transfer, liabilities

(€ m) 2017	Transfer to level 1	Transfer from level 1	Transfer to level 2	Transfer from level 2	Transfer to level 3	Transfer from level 3
Liabilities to customers						
DFV	–	–	–	-6	6	–
Trading liabilities (HfT)	–	–	–	-31	31	–
Total	**–**	**–**	**–**	**-37**	**37**	**–**

Reconciliation, Assets

(€ m)		Change in balance affecting income		Quantitative change in balance	
2018	01.01.2018	Realised net income(income statement)	OCI reserve	Purchases	Sales
Balance sheet item/ category/ instrument type					
Loans and advances to banks					
thereof FVPL Other	43	–	–	–	–
Loans and advances to customers					
thereof FVOCI Mandatory	135[2)]	-2	-33	–	–
thereof FVPL Other	491[2)]	36	–	71	-103
Credit derivative under the second loss guarantee	1,014	-45	–	–	–
Trading assets (FVPL Trading)	331[2)]	-28	–	53	-63
Financial investments					
thereof FVOCI Mandatory	–	–	–	15	–
thereof FVPL Other	150[2)]	-10	–	–	-24
Non-current assets held for sale and disposal groups					
thereof FVPL Other	12	–	–	–	–
Total	**2,176[2)]**	**-49[1)]**	**-33**	**139**	**-190**

[1)] Of the net income in the income statement recognised in profit or loss, € -65 million relates to the result from financial instruments categorised as FVPL and € 16 million to net interest income.

[2)] The value as at 31 December 2017 was adjusted. Please refer to Note 3 for more details.

Quantitative change in balance		Transfers					
Issues	Settlements	From level 3	To level 3	Transfer/ recategorisation	Exchange rate changes	31 December 2018	Net income from assets held as at 31 December 2018
							–
–	-43	–	–	–	–	–	–
–	-100	–	–	–	–	–	–
–	-103	–	19	–	–	411	-11
–	–	-969	–	–	–	–	–
–	–	-3	2	–	-1	291	-37
–	–	–	–	–	–	15	–
–	–	-23	–	–	-3	90	-1
–	-4	–	–	–	–	8	–
–	**-250**	**-995**	**21**	**–**	**-4**	**815**	**-49**

Reconciliation, Assets

(€ m)		Change in balance affecting income		Quantitative change in balance	
2017	1 January 2017	Realisednet income(income statement)	Net income not recognised in profit or loss	Purchases	Sales
Balance sheet item/ category/ instrument type					
Loans and advances to banks					
AfS	44	-2	1	–	–
Loans and advances to customers					
AfS	61	-9	–	–	–
DFV	100[2)]	-1	–	–	-11
Credit derivative second loss guarantee (HfT)	199	815	–	–	–
Trading assets (HfT)	401[2)]	-98	–	8	-20
Financial investments (excluding equity instruments measured at cost)					
AfS	29	-54	8	–	-26
DFV	75[2)]	-3	–	–	–
Total	**909[2)]**	**648[1)]**	**9**	**8**	**-57**

[1)] Of the net income in the income statement recognised in profit or loss, € -100 million relates to net trading income, € -4 million to net interest income, € -63 million to net income from financial investments and € 815 million to the hedging effect of the credit derivative under the second loss guarantee.

[2)] The value as at 31 December 2017 and, as a result, also the starting value as at 1 January 2017 have been adjusted. Please refer to Note 3 for more details.

Quantitative change in balance	Transfers					
Settlements	From level 3	To level 3	Reclassification	Exchange rate changes	31 December 2017	Net income from assets held as at 31 December 2017
–	–	–	–	–	43	-2
–	–	–	–	-7	45	-9
–	–	–	–	-3	85[2)]	-2
–	–	–	–	–	1,014	815
–	–	40	–	–	331[2)]	-12
–	–	–	132	-4	85	-54
-22	–	–	–	-2	48[2)]	-1
-22	**–**	**40**	**132**	**-16**	**1,651[2)]**	**735**

Reconciliation, Liabilities

(€ m)		Change in balance affecting income		Quantitative change in balance	
2018	1 January 2018	Realised net income (income statement)	Net income not recognised in profit or loss	Purchases	Sales
Balance sheet item/ category/ instrument type					
Liabilities to banks					
FVPL Designated	107	2	-1	–	–
Liabilities to customers					
FVPL Designated	421[2)]	-10	3	14	-13
Securitised liabilities					
FVPL Designated	360[2)]	-16	2	–	–
Trading liabilities (FVPL Trading)	167[2)]	-17	–	–	-56
Total	**1,055[2)]**	**-41[1)]**	**4**	**14**	**-69**

[1)] Of the net income in the income statement recognised in profit or loss, € -27 million relates to the result from financial instruments categorised as FVPL and € -14 million to net interest income.

[2)] The value as at 31 December 2017 (1 January 2018) was adjusted. Please refer to Note 3 for more details.

Reconciliation, Liabilities

(€ m)		Change in balance affecting income		Quantitative change in balance	
2017	1 January 2017	Realised net income (income statement)	Net income not recognised in profit or loss	Purchases	Sales
Balance sheet item/ category/ instrument type					
Liabilities to banks					
DFV	109	-2	–	–	–
Liabilities to customers					
DFV	443[2)]	-13	2	–	-10
Securitised liabilities					
DFV	439[2)]	-18	6	-14	-1
Trading liabilities (HfT)	269[2)]	-104	–	–	-29
Total	**1,260[2)]**	**-137[1)]**	**8**	**-14**	**-40**

[1)] Of the net income in the income statement recognised in profit or loss, €-118 million relates to net trading income and € -19 million to net interest income.

[2)] The value as at 31 December 2017 and, as a result, also the starting value as at 1 January 2017 have been adjusted. Please refer to Note 3 for more details.

Quantitative change in balance		Transfers					
Newbusiness	Settlements	From level 3	To level 3	Reclassi-fication/ transfer	Exchange rate changes	31 December 2018	Net income from assets held as at 31 December 2018
–	–	–	–	–	–	108	1
–	-31	–	–	–	–	384	-6
–	-2	–	–	–	22	366	-14
–	–	-1	–	–	–	93	-23
–	**-33**	**-1**	**–**	**–**	**22**	**951**	**-42**

Quantitative change in balance		Transfers					
Newbusiness	Settlements	From level 3	To level 3	Reclassi-fication/ transfer	Exchange rate changes	31. December 2017	Net income from assets held as at 31 December 2017
–	–	–	–	–	–	107	-2
–	-5	–	6	–	-2	421[2)]	-13[2)]
–	-30	–	–	–	-22	360[2)]	-17[2)]
–	–	–	31	–	–	167[2)]	18[2)]
–	**-35**	**–**	**37**	**–**	**-24**	**1,055[2)]**	**-14[2)]**

The first-time application of IFRS 9 results in changes between the column value for 1 January 2018 in the above reconciliations in accordance with IFRS 9 and the column value for 31 December 2017 in the reconciliations in accordance with IAS 39 included in the previous financial statements. The changes are based on the new IFRS 9 classification and measurement provisions.

The following reconciliation has been prepared to show these changes. This reconciliation was made for each balance sheet item if the financial instruments contained therein were measured at fair value in accordance with either IAS 39 or IFRS 9 or both accounting standards, and were assigned to Level 3.

The IAS 39 carrying amounts as at 31 December 2017 are shown in the following reconciliations for each IAS 39 holding category and type of instrument in the column IAS 39 carrying amount ("from" line). In the Reclassification column, these IAS 39 carrying amounts are allocated to the IFRS 9 carrying amount categories ("to" line). The IFRS 9 carrying amounts as at 1 January 2018 are shown for each IFRS 9 measurement category and type of instrument in the column "IFRS 9 carrying amount" (also "to" line). The difference between the columns "Reclassifications" and "IFRS 9 carrying amount" column is displayed in the "Remeasurement/retained earnings" column and represents the measurement difference between IAS 39 and IFRS 9 that is recognised exclusively in retained earnings.

Some financial instruments that are not measured at fair value in accordance with IAS 39 but are assigned to Level 3 are measured at fair value for the first time in accordance with IFRS 9. The IAS 39 carrying amounts of these transactions are presented in net terms in the following reconciliations, i.e. the loan loss provisions associated with the transactions have already been offset against their amortised cost. This is designed to facilitate the appropriate presentation of the measurement difference between IAS 39 and IFRS 9, since the derecognised loan loss provision amount has already been taken into account implicitly as a component of the fair value measurement.

Reconciliation – first-time application, assets

	31.12.2017	01.01.2018		
	IAS 39 carrying amount	Reclassification	Remeasurement/ retained earnings	IFRS 9 carrying amount
Loans and advances to banks				
From AfS	43			
To FVPL		43	–	43
Loans and advances to customers				
From AfS	45			
To FVPL				
of which FVPL Designated	–	–[1]	–	–[1]
thereof FVPL Other	–	45[1]	–	45[1]
from DFV	85[1]	–	–	–
To FVPL				
of which FVPL Designated	–	–[1]	–	–[1]
thereof FVPL Other	–	85[1]	–	85[1]
thereof FVOCI Mandatory	–	–[1]	–	–[1]
From LaR	459[1]	–	–	–
To FVPL				
thereof FVPL Other	–	357	4	361
To FVOCI				
thereof FVOCI Mandatory		102[1]	34[1]	136[1]
Credit derivative under the second loss guarantee (HfT)				
From HfT	1,014	–	–	–
To FVPL				
of which FVPL Trading	–	1,014	–	1,014
Trading assets				
From HfT	331[1]	–	–	–
To FVPL				
of which FVPL Trading	–	331[1]	–	331[1]
Financial investments				
From AfS	85	–	–	–
To FVPL				
thereof FVPL Other	–	85	–	85
from DFV	48[1]	–	–	–
To FVPL				
of which FVPL Designated		–[1]	–	–[1]
thereof FVPL Other	–	48[1]	–	48[1]
From LaR	13	–	–	–
To FVPL				
thereof FVPL Other	–	13	4	17
Non-current assets held for sale and disposal groups				
From LaR	12	–	–	–
To FVPL				
thereof FVPL Other	–	12	–	12
Total	**2,135**	**2,135**	**42**	**2,177**

[1] The value as at 31 December 2017 was adjusted. Please refer to Note 3 for more details.

Reconciliation – first-time application, liabilities

	31.12.2017	01.01.2018		
	IAS 39 carrying amount	Reclassification	Remeasurement/ retained earnings	IFRS 9 carrying amount
Liabilities to banks				
from DFV	107			
To FVPL				
of which FVPL Designated		107	–	107
Liabilities to customers				
from DFV	421[1]			
To FVPL				
of which FVPL Designated		421[1]	–	421[1]
Securitised liabilities				
from DFV	360[1]			
To FVPL				
of which FVPL Designated		360[1]	–	360[1]
Trading liabilities				
From HfT	167[1]			
To FVPL				
of which FVPL Trading		167[1]	–	167[1]
Total	**1,055**[1]	**1,055**[1]	**–**	**1,055**[1]

[1] The value as at 31 December 2017 was adjusted. Please refer to Note 3 for more details.

II. Information on significant unobservable inputs

QUANTITATIVE INFORMATION ON SIGNIFICANT UNOBSERVABLE INPUTS

The following overview contains quantitative information on significant unobservable inputs.

Fair value

(€ m) 2018		Assets	Liabilities	Measurement procedures	Significant unobservable inputs (level 3)	Margin
Loans and advances to customers	FVPL Other	411		DCF method	Spread (bps)	71 -1447
				Option pricing model	Interest rate FX correlation	-33 % -26 %
				Price	Price	
Trading assets /trading liabilities	FVPL Held For Trading	291	93	DCF method	Spread	71 -1447
				Option pricing model	Interest rate volatility	4% -24%
					Interest rate FX correlation	-33 % -26 %
					FX correlation	31% -56%
Financial investments	FVPL Other	90		Option pricing model		
					Interest rate volatility	4% -24%
				Price	Price	1 -12,000
				DCF method	Capital costs	7% -9%
	Mandatory FVOCI	15		DCF method	Spread (bps)	71 -1447
Non-current assets held for sale and disposal groups	FVPL Other	8		DCF method	Spread	71 -1447
Liabilities to banks	FVPL Designated		108	Option pricing model	Interest rate volatility	4% -24%
					Interest rate FX correlation	-33 % -26 %
Liabilities to customers	FVPL Designated		384	Option pricing model		
					Interest rate volatility	4% -24%
					Interest rate FX correlation	-33 % -26 %
				Price	Price	30 -95
Securitised liabilities	FVPL Designated		366	Option pricing model		
					Interest rate volatility	4% -24%
					FX correlation	31% -56%
Subordinated capital	FVPL DFP		–	Option pricing model	Interest rate volatility	17 % -87 %
Total		**815**	**951**			

Fair value

(€ m) 2017		Assets	Liabilities	Measurement procedures	Significant unobservable inputs (level 3)	Margin
Loans and advances to banks	AfS	43	–	DCF method	Spread (bps)	54
Loans and advances to customers	AfS	45	–	DCF method Price	Spread (bps) Price	700
	DFV	85[1]	–	Option pricing model	Interest rate FX correlation	-29% -33%
				Price	Price	25 -83
Credit derivative under the second loss guarantee	HfT	1,014	–	DCF method	Expected cash flow	–
Trading assets/trading liabilities	HfT	331[1]	167[1]	DCF method	Spread (bps)	175 -200
		–	–	Option pricing model	Interest rate volatility	5% -23%
					Interest rate FX correlation	-29% -33%
		–	–		FX correlation	44% -64%
		–	–		Shares FX correlation	-45% -25%
					Interest rate correlation	-73% -21%
Financial investments	AfS	85	–	Price	Price	1 -12,000
				DCF method	Spread (bps)	20
					Capital costs	6% -10%
	DFV	48[1]	–	Option pricing model	Interest rate volatility	5% -23%
		–	–	Price	Price	5
Liabilities to banks	DFV	–	107[1]	Option pricing model	Interest rate volatility	5% -23%
					Interest rate FX correlation	-29% -33%
Liabilities to customers	DFV	–	421[1]	Option pricing model	Interest rate volatility	5% -23%
					Interest rate correlation	-73% -21%
					Interest rate FX correlation	-29% -33%
Securitised liabilities	DFV	–	360[1]	Option pricing model	Interest rate volatility	5% -23%
					FX correlation	44% -64%
					Shares FX correlation	-45% -25%
				Price	Price	52 -83
Total		**1,651[1]**	**1,055[1]**			

[1] The value as at 31 December 2017 was adjusted. Please refer to Note 3 for more details.

The correlation and volatility ranges shown for derivatives cover derivatives with different types of underlying, tenors and exercise prices.

The overview also includes financial instruments, whose change in value resulting from inputs unobservable in the market does not give rise to any P&L effect due to economic hedging relationships (at the micro level). Changes in value attributable to the respective relevant inputs are offset for these financial instruments by the changes in value of the hedging derivatives.

Sensitivities of fair values in relation to unobservable inputs

The following describes how the fair values of financial instruments can change as a result of fluctuations in significant unobservable inputs.

CORRELATION

Correlation can represent an important unobservable input for the measurement of derivatives. It is a measure of the degree to which two reference values move in relation to each other. Correlation is an important input for the model-based determination of the fair value of derivatives with more than one underlying. Financial instruments of this type include, for example, derivatives with several currencies ("FX basket") or several shares as the underlyings ("equity basket" derivatives). Currency correlations describe the relationship between changes in value of several currencies. Share correlations express the relationship between yields on different shares. A high degree of correlation means that there is a close relationship between the changes in value of the respective underlyings.

Depending on the type of derivative changes in correlation can have a positive or negative effect on the fair value. For example, in the case of a "best of two" derivative, an increase in the correlation between two underlyings results in a decrease of the fair value of the derivative from the perspective of the purchaser.

VOLATILITY

Volatility can also represent an important unobservable input for the measurement of options. It expresses how strongly the value of the underlying fluctuates over time. The amount of volatility depends on the type of the underlying, its tenor and the exercise price agreed for the option.

The fair value of options typically increases if volatility increases. The sensitivity of the fair value of options to changes in volatility can vary considerably. For example, the sensitivity of the fair value to changes in volatility is comparatively high, if the price of the underlying is close to the agreed exercise price ("at-the-money"). By contrast, sensitivity to changes in volatility is lower, if the price of the underlying is far from the exercise price ("far out-of-the-money" or "far in-the-money").

PRICE

Prices can represent an important unobservable input for the measurement of financial instruments. These prices represent pricing information of third parties within the meaning of IFRS 13.93(d) sentence 4, whereby the Bank does not produce any quantitative, unobservable input factors for measuring the fair value of the respective financial instrument. More detailed quantitative information on these input factors is not required therefore. The fair value increases, if the price increases, and it falls, if the price declines.

Reciprocal effects between unobservable inputs

Reciprocal effects between unobservable inputs can exist in principle. If several unobservable inputs are used in determining fair value, the range of the possible characteristics for another unobservable input can be restricted or increased by the characteristic used for one of the relevant unobservable inputs.

Effects of unobservable inputs

If the measurement of a financial instrument is based partly on unobservable inputs, the fair value determined is the best estimated value in accordance with a discretionary decision made by the Bank. However, it remains subjective in that there may be alternative input selection options that cannot be refuted by observable market data. For many of the financial instruments included (such as derivatives) the unobservable inputs only represent a subset of the total inputs required for the measurement. The remaining inputs are observable inputs.

An alternative choice of inputs for the unobservable inputs depending on the limits of a possible range would have had certain effects on the fair values of the financial instruments in question. Advantageous and disadvantageous changes to fair value have been determined by recalcuating the fair values based on possible alternative values to the relevant unobservable inputs. The interest volatilities were changed by +/-5 %, all correlations by +/-20 % (capped at +/-100 %), price parameters by +/-2 % and spreads by +/-69 bp. Overall, this would then have had a positive/negative effect on the fair values of the financial instruments in question in the amount of € 22 million (previous year: € 26 million). This would have been attributable to the income statement in full as income/expense (previous year: € 21 million income statement, € 5 million revaluation reserve).

III. Day One Profit and Loss

The day one profit and loss reserve developed as follows:

(€ m)	2018	2017
Holdings as at 1 January	**2**	**13**
Additions not recognised in profit or loss	1	1
Reversals recognised in profit or loss	1	12
Holdings as at 31 December	**2**	**2**

The day one profit and loss reserve is solely attributable to financial instruments classified as FVPL Trading.

53. Offsetting of financial instruments

Financial assets and financial liabilities are netted and disclosed as a net amount on the balance sheet, if there is a legal entitlement to do so at the current point in time and there is the intention to settle the claims on a net basis or to settle the associated liability at the time the asset concerned is realised.

Set out below are the financial instruments on the balance sheet that were netted as at the reporting date as well as financial instruments, which are subject to a legally enforceable global netting agreement, irrespective of whether the financial instruments concerned are actually netted on the face of the balance sheet. ISDA master agreements and the Master Agreement for Financial Derivative Transactions (DRV) are the master agreements customarily used by Hamburg Commercial Bank for OTC transactions. These only provide for the netting of reciprocal claims and obligations in the event of the termination of all individual transactions under a master agreement that is based on specific events and therefore do not permit netting of the assets and liabilities on the balance sheet. Hamburg Commercial Bank has entered into clearing agreements with brokers for certain OTC derivatives enabling the Bank to access central counterparties (clearing houses). The contractual arrangements for these transactions include a legal right to set off financial assets and financial liabilities that can be enforced legally at any time and thereby result in the offsetting of positive and negative fair values of derivative financial instruments and of collateral provided and received in accordance with IAS 32.42.

The fair value of the collateral received or provided in this connection is also given in this table. This includes cash collateral as well as financial instruments received or provided as collateral.

Financial assets

(€ m) 2018	Gross carrying amount	Gross carrying amount from netting	Net amount	Gross amount, netting criteria not met	Collateral received	Net amount after collateral
Loans and advances to banks	1,409	68	1,341	–	1,205	136
Loans and advances to customers	407	–	407	–	372	35
Derivatives	3,699	978	2,721	1,568	400	753

In the reporting year, the netted amounts disclosed under Loans and advances to banks and Loans and advances to customers relate to genuine repo transactions.

Of the net amount of derivatives disclosed on the balance sheet positive market values of hedging derivatives account for € 175 million and trading assets for € 2,546 million.

Financial liabilities

(€ m) 2018	Gross carrying amount	Gross carrying amount from netting	Net amount	Gross amount, netting criteria not met	Collateral provided	Net amount after collateral
Liabilities to banks	272	12	260	–	257	3
Liabilities to customers	409	207	202	–	191	11
Derivatives	4,088	827	3,261	1,568	1,577	116

In the reporting year, the netted amounts disclosed under Liabilities to banks and Liabilities to customers relate to genuine repo transactions.

Of the net amount of derivatives disclosed on the balance sheet negative market values of hedging derivatives account for € 501 million and trading liabilities for € 2,760 million.

Financial assets

(€ m) 2017	Gross carrying amount	Gross carrying amount from netting	Net amount	Gross amount, netting criteria not met	Collateral received	Net amount after collateral
Loans and advances to banks	1,492	–	1,492	–	1,432	60
Loans and advances to customers	505	–	505	–	424	81
Derivatives	4,206	945	3,261	2,068	326	867

In the previous year, the netted amounts disclosed under Loans and advances to banks and Loans and advances to customers exclusively concern current accounts.

Of the net amount of derivatives disclosed on the balance sheet positive market values of hedging derivatives account for € 264 million and trading assets for € 2,997 million.

Financial liabilities

(€ m) 2017	Gross carrying amount	Gross carrying amount from netting	Net amount	Gross amount, netting criteria not met	Collateral provided	Net amount after collateral
Liabilities to banks	572	20	552	–	543	9
Liabilities to customers	460	250	210	–	199	11
Derivatives	4,697	675	4,022	2,068	1,856	98

In the previous year, the netted amounts disclosed under Liabilities to banks and Liabilities to customers exclusively resulted from current account transactions.

Of the net amount of derivatives disclosed on the balance sheet negative market values of hedging derivatives account for € 163 million and trading liabilities for € 3,859 million.

54. Credit risk analysis of financial assets

I. Credit quality

The following table contains information on the credit quality of all financial instruments held by the Bank. The following table shows the credit risk exposures by classifying the gross carrying amounts of financial assets and the nominal amounts of off-balance sheet transactions by credit risk level and assigning them to rating categories.

Credit quality

(€ m) 2018		1(AAA) to 1(AA+)	1(AA) to 1(A–)	2 to 5	6 to 9
Financial instruments without any significant deterioration in credit quality (12-month ECL)	Cash reserve				
	thereof AC assets	5,362	–	–	–
	Loans and advances to customers				
	thereof AC assets	1,927	5,051	10,221	8,100
	thereof FVOCI Mandatory	1,874	111	–	–
	Loans and advances to banks				
	thereof AC assets	1,306	1,296	270	101
	thereof FVOCI Mandatory	166	–	–	–
	Financial investments				
	thereof AC assets	–	64	50	–
	thereof FVOCI Mandatory	6,574	2,363	362	–
	Other assets				
	thereof AC assets	–	33	–	–
	No holding category				
	Receivables under finance lease transactions	–	73	–	–
	Contingent liabilities	102	173	326	237
	Irrevocable loan commitments	446	709	3,512	2,493
Financial instruments with a significant deterioration in credit quality (LECL level 2)	Loans and advances to customers				
	thereof AC assets	–	10	757	621
	thereof FVOCI Mandatory	–	–	9	–
	Financial investments				
	thereof FVOCI Mandatory	–	–	47	–
	No holding category				
	Contingent liabilities	–	–	1	22
	Irrevocable loan commitments	–	–	128	127
Credit-impaired (LECL level 3)	Loans and advances to customers				
	thereof AC assets	–	–	–	82
	thereof FVOCI Mandatory	–	–	–	–
	No holding category				
	Contingent liabilities	–	–	–	–
	Irrevocable loan commitments	–	–	–	–
Total		**17,757**	**9,883**	**15,683**	**11,783**

Credit quality

(€ m) 2018		10 to 12	13 to 15	16 to 18
Financial instruments without any significant deterioration in credit quality (12-month ECL)	Cash reserve			
	thereof AC assets			
	Loans and advances to customers			
	thereof AC assets	547	248	–
	thereof FVOCI Mandatory	–	–	–
	Loans and advances to banks			
	thereof AC assets	27	–	–
	thereof FVOCI Mandatory	–	–	–
	Financial investments			
	thereof AC assets	–	–	–
	thereof FVOCI Mandatory	–	–	–
	Other assets	–	–	–
	thereof AC assets	–	–	–
	No holding category			
	Receivables under finance lease transactions	–	–	–
	Contingent liabilities	6	–	–
	Irrevocable loan commitments	39	66	–
Financial instruments with a significant deterioration in credit quality (LECL level 2)	Loans and advances to customers			
	thereof AC assets	855	760	5
	thereof FVOCI Mandatory	–	–	–
	Financial investments			
	thereof FVOCI Mandatory	8	–	–
	No holding category			
	Contingent liabilities	12	1	–
	Irrevocable loan commitments	38	58	–
Credit-impaired (LECL level 3)	Loans and advances to customers			
	thereof AC assets	184	115	575
	thereof FVOCI Mandatory	–	–	–
	No holding category			
	Contingent liabilities	–	–	65
	Irrevocable loan commitments	–	–	11
Total		**1,716**	**1,248**	**656**

The Bank does not apply the simplified approach under IFRS 9.5.5.15, meaning that the disclosure under IFRS 7.35 M(b)(iii) is not relevant.

In the previous year, only those financial instruments that were neither impaired nor overdue were shown separately, broken down by category, in the table on credit quality. Impaired and overdue financial instruments are shown in separate tables, which are shown under II. and III. for the comparative period. These disclosures in accordance with IAS 39 will no longer be made in the next reporting period.

Credit quality

(€ m)				
2017	1(AAA) to 1(AA+)	1(AA) to 1(A–)	2 to 5	6 to 9
Held for Trading (HfT)				
Trading assets	1,165	801	1,202	328
Credit derivative under the second loss guarantee	1,014	–	–	–
Designated at Fair Value (DFV)				
Loans and advances to customers	1,180	–	–	–
Financial investments	98	416	98	–
Available for Sale (AfS)				
Cash reserve	106	–	–	–
Loans and advances to banks	–	–	79	–
Loans and advances to customers	–	–	–	–
Financial investments	9,181	2,730	496	–
Non-current assets held for sale and disposal groups	–	–	–	–
Loans and receivables (LaR)				
Cash reserve	6,519	–	–	–
Loans and advances to banks	1,242	1,127	1,315	–
Loans and advances to customers	2,778	4,614	10,648	9,301
Financial investments	106	129	56	269
Assets held for sale and disposal groups	–	–	–	26
Other assets	–	–	–	–
No IAS 39 category				
Positive fair values of hedging derivatives	61	74	129	–
Receivables under finance lease transactions	7	12	27	24
Value adjustments from the portfolio fair value hedge	59	71	125	–
Total	**23,516**	**9,974**	**14,175**	**9,948**

Credit quality

(€ m)			
2017	10 to 12	13 to 15	16 to 18
Held for Trading (HfT)			
Trading assets	–	109	36
Credit derivative under the second loss guarantee	–	–	–
Designated at Fair Value (DFV)			
Loans and advances to customers	–	75	–
Financial investments	–	–	–
Non-current assets held for sale and disposal groups	–	–	–
Available for Sale (AfS)			
Cash reserve	–	–	–
Loans and advances to banks	–	–	–
Loans and advances to customers	–	–	–
Financial investments	–	–	–
Non-current assets held for sale and disposal groups	–	–	–
Loans and receivables (LaR)			
Cash reserve	–	–	–
Loans and advances to banks	75	–	–
Loans and advances to customers	1,450	1,236	148
Financial investments	–	–	–
Non-current assets held for sale and disposal groups	–	–	–
Other assets	35	–	–
No IAS 39 category			
Positive fair values of hedging derivatives	–	–	–
Receivables under finance lease transactions	4	2	–
Value adjustments from the portfolio fair value hedge	–	–	–
Total	**1,564**	**1,422**	**184**

II. Carrying amounts of overdue but unimpaired financial assets

The table below shows the financial assets which were overdue but unimpaired as at 31 December 2017 as the comparative period. The assets are broken down by category. Categories not shown have no overdue assets. These disclosures in accordance with IAS 39 will no longer be made in the next reporting period.

Carrying amounts of overdue but unimpaired financial assets

(€ m)					
2017	Overdue < 3 months	Overdue 3 to 6 months	Overdue 6 to 12 months		Overdue > 12 months
Loans and receivables (LaR)					
Loans and advances to customers	231	51	214	314	
of which hedged by the second loss guarantee	28	29	192	288	
Total	**231**	**51**	**214**	**314**	

III. Impaired financial assets

The table below shows all impaired financial assets as at 31 December 2017 as the comparative period. The financial assets are broken down by category. These disclosures in accordance with IAS 39 will no longer be made in the next reporting period.

Impaired financial assets as at 31 December 2018

(€ m)			
Loans and receivables (LaR)			
Loans and advances to customers	6,813	4,354	2,459
Available for Sale (AfS)			
Loans and advances to customers	82	38	44
Financial investments[1]	208	140	68
Total	**7,103**	**4,532**	**2,571**

[1] Financial investments classified as LaR and AfS are shown net in the statement of financial position, i,e, at their carrying amounts less impairment.

IV. Credit risk exposure

With the exception of Loans and advances to banks and customers, the credit risk exposure as at the reporting date corresponds to the carrying amount of financial assets, as presented in Note 50, as well as the nominal value of off-balance sheet liabilities as presented in Note 58.

In the case of Loans and advances to banks and customers, the credit risk exposure corresponds to the carrying amount after loan loss provisions as presented in Note 27. The maximum default risk of the loans and advances recognised at fair value through profit or loss (FVPL) (in the previous year: designated at fair value (DFV)) is not reduced by associated credit derivatives.

Collateral and other risk-reducing agreements are not reflected in these amounts.

V. Collateral received

A) COLLATERAL VALUES OF FINANCIAL ASSETS THAT MINIMISE THE DEFAULT RISK AND ARE NOT SUBJECT TO THE IMPAIRMENT PROCEDURE

The following information quantifies the extent to which the collateral retained and other loan collateralisation reduce the maximum default risk for financial instruments that are not subject to the impairment procedure pursuant to IFRS 9. The amount of risk reduction from the value of each form of collateral is indicated for each class of financial instruments.

The value of collateral received is determined directly on the basis of the objective market value, provided that such a value can be determined. The reliability of the collateral value is ensured by the fact that it is recognised as risk-reducing only up to the level of the applicable collateral-specific recovery ratio.

The following table shows the respective carrying amount for each class of financial instrument as well as the collateral value that reduces default risk.

Financial assets an associated collateral

(€ m)		Value of collateral received		
2018	Carrying amount	Real estate and registered liens	Sureties and guarantees	Other collateral
FVPL Designated				
Loans and advances to customers	120	–	–	–
Financial investments	96	–	–	–
FVPL Other				
Loans and advances to customers	547	370	–	–
Financial investments	541	–	–	–
Non-current assets held for sale and disposal groups	8	8	–	–
FVPL Held For Trading				
Trading assets	3,094	367	16	302
No holding category				
Positive fair values of hedging derivatives	175	–	–	–
Value adjustments from the portfolio fair value hedge	200	–	–	–
Total assets	**4,781**	**745**	**16**	**302**

Financial assets an associated collateral

(€ m)		Value of collateral received		
2017	Carrying amount	Real estate and registered liens	Sureties and guarantees	Other collateral
HfT				
Trading assets	3,641	329	26	422
Credit derivative under the second loss guarantee	1,014	–	–	–
DFV				
Loans and advances to customers	1,255	–	–	–
Financial investments	612	–	–	–
AfS				
Cash reserve	106	–	–	–
Loans and advances to banks	79	–	–	–
Loans and advances to customers	45	–	–	–
Financial investments	12,475	–	–	–
LaR				
Cash reserve	6,519	–	–	–
Loans and advances to banks	3,759	9	22	68
Loans and advances to customers	37,798	13,778	584	1,428
Financial investments	560	–	–	–
Non-current assets held for sale and disposal groups	26	12	–	–
Other assets	35	–	–	–
No IAS 39 category				
Positive fair values of hedging derivatives	264	–	–	–
Value adjustments from the portfolio fair value hedge	255	–	–	–
Receivables under finance leases	76	–	–	–
Contingent liabilities	1,862	101	7	142
Irrevocable loan commitments	6,367	840	64	152
Total assets	**76,748**	**15,069**	**703**	**2,212**

B) IMPAIRED FINANCIAL ASSETS AND ASSOCIATED COLLATERAL

The following overview shows the volume and concentration of collateral held by Hamburg Commercial Bank to reduce the default risk and other loan collateralisation for impaired financial assets.

(€ m)	Value of collateral received			
2018	Carrying amount	Real estate and registered liens	Sureties and guarantees	Other collateral
AC assets				
Loans and advances to customers	955	282	4	12
No holding category				
Contingent liabilities	65	1	2	8
Irrevocable loan commitments	11	2	–	–
Total assets	**1,031**	**285**	**6**	**20**

For loans and advances to customers in the amount of € 199 million, no impairment losses were recognised despite default due to the collateral available.

Collateral is a key instrument for managing default risks. They are included in the main procedures for managing and monitoring default risks to reduce risk. The methods and processes for the valuation and management of collateral are set out in Hamburg Commercial Bank's Collateral Guideline.

The value of collateral received is determined directly on the basis of the objective market value, provided that such a value can be determined. The reliability of the collateral value is ensured by the fact that it is recognised as risk-reducing only up to the level of the applicable collateral-specific recovery ratio. Only collateral listed in the collateral catalogue is included as valuable collateral. Upon initial recognition, the value of movable property and real estate recognised as collateral is determined by an appraiser who is independent of the market. Depending on the type of collateral, the recoverability and realisation options are reviewed regularly at set intervals, and more frequently in the event of considerable market fluctuations.

Significant collateral values are provided by domestic collateral providers. The creditworthiness of the collateral providers is mainly in the 1(AAA) to 1(A-) rating categories.

Information on the risk concentrations for the collateral provided can be found in the Risk Report in the Default risk section.

C) THEREOF COLLATERAL RECEIVED FOR WHICH THERE ARE NO RESTRICTIONS ON DISPOSAL OR REALISATION EVEN IF THERE IS NO DEFAULT IN PAYMENT

Hamburg Commercial Bank received collateral from counterparties with a total fair value of € 271 million (31 December 2017: € 405 million). The collateral received is split up as follows: € 271 million (31 December 2017: € 405 million) relates to OTC derivatives and structured transactions. The Group did not receive any collateral under genuine repo transactions where it acted as the lender either on the balance sheet date or on the previous year's balance sheet date. Collateral received includes cash collateral in the amount of € 271 million (31 December 2017: € 405 million). Collateral received was not resold or pledged. There are no restrictions on disposal or realisation. Hamburg Commercial Bank is obliged to return all collateral resold or pledged to the guarantor without exception.

Hamburg Commercial Bank carries out securities repurchase and lending transactions as well as tri-party repo transactions under standard master agreements with selected counterparties. The same conditions and collateralisation methods apply as for collateral transferred and received.

D) OTHER COLLATERAL RECEIVED

As in the previous year, no assets from the realisation of collateral were capitalised in the reporting period.

VI. Assets that have been written off and are still subject to an enforcement measure

In the current reporting period, financial assets that are still subject to an Authorisations measure were written off in the amount outstanding under contract law of € 99 million.

55. Restructured or modified loans

The following table shows the carrying amounts of loans and loan commitments that have been restructured or whose contractual terms and conditions have been modified in order to place the debtor in a position to continue to service or resume servicing its capital debt despite financial difficulties.

Forbearance exposure

(€ m) 2018	Rating class 1–15	Rating class 16–18	Total
Loans and advances to customers	1,520	736	2,256
Irrevocable and revocable loan commitments	40	2	42
Total	**1,560**	**738**	**2,298**

Forbearance exposure

(€ m)	Core Bank		Non-Core Bank		
2017	Rating class 1–15	Rating class 16–18	Rating class 1–15	Rating class 16–18	Total
Loans and advances to customers	1,180	894	521	5,434	8,029
Irrevocable and revocable loan commitments	76	48	13	32	169
Total	**1,256**	**942**	**534**	**5,466**	**8,198**

For the volume of receivables shown here, which is subject to forbearance measures, loan loss provisions of € 618 million have already been set up for the portfolios measured at amortised cost (previous year for all portfolios: € 3,934 million).

56. Information on unconsolidated structured entities

I. Interests in unconsolidated subsidiaries

Hamburg Commercial Bank maintains business relationships with unconsolidated structured entities, within the meaning of an interest pursuant to IFRS 12, if Hamburg Commercial Bank is exposed to variable returns based on equity, debt instruments, derivatives, guarantees, etc.

These unconsolidated structured entities relate to ABS investments, securitisation and refinancing vehicles, investment funds and other structured entities.

Hamburg Commercial Bank has a business relationship within the meaning of an interest with a total of 28 unconsolidated structured entities (previous year: 34). The following table shows the accumulated total assets of the unconsolidated structured entities with which Hamburg Commercial Bank maintains a business relationship within the meaning of an interest:

Information on the size of unconsolidated entities

(€ m)	Number		Total assets	
	2018	2017	2018	2017
ABS investments	1	5	9	211
Investment funds	11	12	2,463	2,411
Securitisation and refinancing vehicles	12	13	396	672
Other	4	4	355	281
Total	**28**	**34**	**3,223**	**3,575**

The purpose of refinancing and securitisation vehicles is to issue securities. These companies are involved in the (revolving) purchase and securitisation of loan, trading and lease receivables, including refinancing with investors. They are mainly financed through issuing debentures (and promissory notes). There is also an ABS investment. ABS structures are financed by the issuance of debentures. Furthermore investments in the ABS structures are backed by collateral. These companies are involved in the (revolving) purchase and securitisation of loan receivables, including refinancing via investors.

The main corporate purposes of investment funds are to finance assets, participate in non-listed companies and hold shares in real estate funds. The main activities of such investment funds are to carry out research for analysing markets, make decisions on investment and disinvestment in order to adjust portfolios and to attract investors. Investment funds raise their funds by the issuing of equity and debt instruments. The investment funds are funds launched by third parties, to which Hamburg Commercial Bank has mainly granted loans.

II. Risks from interests in unconsolidated structured entities

The following information concerning risk refers not just to the current reporting period but also to risks which result from business relationships with unconsolidated structured entities in earlier reporting periods.

The risks from unconsolidated structured entities are presented in the form of the maximum potential loss which may arise from these business relationships based on an interest within the meaning of IFRS 12. Hamburg Commercial Bank discloses the carrying amounts of these transactions as a maximum potential loss. In the case of irrevocable loan commitments and contingent liabilities, the carrying amount matches the par value.

There are no credit derivatives relating to unconsolidated structured entities as of the balance sheet date.

The following table shows the IFRS carrying amounts of exposures involving unconsolidated structured entities as of 31 December 2018 broken down into the items of financial position.

Type of business relationship

(€ m) 2018	Investment funds	ABS	Securitisation and refinancing vehicles	Other structured entities	Total
Loans and advances to customers	120	–	124	69	313
Positive fair value of hedging derivatives	–	–	–	–	–
Trading assets	1	–	–	–	1
Financial investments	–	–	64	91	155
Total assets	**121**	**–**	**188**	**160**	**469**
Liabilities to customers	2	–	1	5	8
Total liabilities	**2**	**–**	**1**	**5**	**8**

(€ m) 2017	Investment funds	ABS	Securitisation and refinancing vehicles	Other structured entities	Total
Loans and advances to customers	143	–	171	80	394
Positive fair value of hedging derivatives	–	–	–	–	–
Trading assets	1	–	42	91	134
Financial investments	1	–	160	–	161
Total assets	**145**	**–**	**373**	**171**	**689**
Liabilities to customers	3	–	271	7	281
Total liabilities	**3**	**–**	**271**	**7**	**281**

The above table contains the loans, debentures, deposits and derivatives in respect of unconsolidated structured entities.

In addition, there are maximum potential losses from irrevocable loan commitments amounting to € 47 million (previous year: € 3 million), of which € 1 million results from investment funds (previous year € 1 million) and € 46 million from securitisation and refinancing vehicles (previous year € 0 million).

There are no business relationship risks based on an interest in unconsolidated structured entities as defined in IFRS 12.B26 that exceed the maximum potential loss, such as contractual terms under which Hamburg Commercial Bank would have to grant financial support, liquidity arrangements, guarantees extended or support provided by Hamburg Commercial Bank in the event of difficulties in refinancing unconsolidated structured entities.

Furthermore, Hamburg Commercial Bank has not entered into any loss-transfer agreements with unconsolidated structured entities. Mainly net interest income for granting loans and commission income were generated from business relationships with unconsolidated structured entities based on an interest within the meaning of IFRS 12.

III. Sponsoring

Hamburg Commercial Bank has sponsor relationships within the meaning of IFRS 12 if Hamburg Commercial Bank is exposed to variable return flows, although there is no business relationship in the form of an interest within the meaning of IFRS 12. Hamburg Commercial Bank is a sponsor if it was involved in establishing an unconsolidated structured entity, if it stands to gain the main profit from the entity or is the main collateral taker, if Hamburg Commercial Bank provides implicit guarantees or if the name of Hamburg Commercial Bank is part of the name of the structured entity or of the products issued by such entity.

Details of sponsored entities are only shown, if they are not already included in the disclosures under II, (Risks from interests in unconsolidated structured entities). This requirement is satisfied in the case of one structured entity. This company was sponsored by Hamburg Commercial Bank, but there is no interest within the meaning of IFRS 12.

In the case in question, Hamburg Commercial Bank had sponsored a securitisation vehicle since December 2016. The transaction was based on the transfer of default risks. Hamburg Commercial Bank was involved in the establishment process and had transferred default risks relating to a mezzanine tranche to the structured entity in the amount of € 235 million by way of a financial guarantee. The transaction was ended in December 2018.

IV. Provision of support

During the current reporting period, Hamburg Commercial Bank has not supported any unconsolidated structured entity financially or in any other way without a contractual commitment to do so. Hamburg Commercial Bank also has no intention of granting financial support to any unconsolidated structured entity or helping to procure financial support from third parties.

57. Non-substantially modified financial instruments

As far as modifications are concerned, a distinction is made between substantial and non-substantial modifications.

The following overview shows the amortised cost, taking into account the loan loss provisions before adjustments, and the net results of all financial instruments at levels 2 and 3 that were not substantially modified during the reporting period. The gains or losses resulting from the modification are based on the change in the gross carrying amount of the financial instrument as a result of the modification.

Assets

(€ m)	Amortised cost for level 2, level 3 and POCI financial instruments modified in the reporting period before modification		Gains or losses from the modification at level 2, 3 or POCI in the reporting period	
	2018	2017	2018	2017
AC				
Loans and advances to customers	24	n.r.	–	n.r.
Total	**24**	**n.r.**	**–**	**n.r.**

The net gains from the transactions that were not substantially modified in the reporting period were insignificant.

58. Contingent liabilities and irrevocable loan commitments

Contingent liabilities

(€ m)	2018	2017
Contingent liabilities from guarantees and warranty agreements		
Loan guarantees	200	189
Letters of credit	210	314
Other guarantees	1,338	1,359
Total	**1,748**	**1,862**

Loan commitments

(€ m)	2018	2017
Loan commitments for		
Open account loans to banks	232	–
Open account loans to customers	7,308	6,198
Guarantees	47	94
Other	40	75
Total	**7,627**	**6,367**

Information on collateral transferred is presented in Note 61 .

In addition to the values shown in the table, there are other contingent liabilities arising from litigation. These relate to a litigation risk explained under Provisions. The legal dispute covered by this litigation risk includes several matters in dispute. Provisions have been set up for litigation risks for some of these matters, while contingent liabilities are in place for others. The Bank does not present the disclosures required by IAS 37, including the disclosure required by IAS 37.86 (a) regarding the estimated financial impact of contingent liabilities, due to the fact that this could adversely affect the Bank's position in the underlying litigation.

To determine for which claim the possibility of a loss is likely, and in order to estimate the amount of the potential payment obligations, Hamburg Commercial Bank takes a variety of factors into account. These include, among other things, the type of claim and the underlying facts of the case, the status of the individual proceedings, (provisional) decisions made by courts and arbitration bodies, the experience of Hamburg Commercial and third parties in comparable cases (insofar as they are known to the Bank), prior settlement negotiations, as well as the expert opinions and assessments of the Bank's internal and external legal advisors and other professionals.

Please also refer to the note on Provisions and the explanations set out in the Risk Report, which forms part of the Management Report, with respect to existing uncertainties regarding risks arising from legal disputes.

Other disclosures

59. Report on business in derivatives

Derivative financial instruments are used to a considerable degree in order to hedge risk efficiently, to take advantage of market opportunities and to cover special customer financing needs. The derivatives business of Hamburg Commercial Bank is predominantly transacted with banks based in OECD countries.

Positive and negative fair values are presented on the basis of gross values before offsetting in accordance with IAS 32.42.

I. Volumes

Derivative transactions with interest rate risks

(€ m)	Nominal values		Positive market values		Negative market values	
	2018	2017	2018	2017	2018	2017
Interest rate swaps	114,456	123,800	3,160	3,490	2,861	3,663
FRAs	937	–	–	–	–	–
Swaptions						
Purchases	3,258	2,053	62	72	16	15
Sales	4,109	2,660	9	7	118	114
Caps, floors	13,152	10,948	24	28	45	43
Exchange-traded contracts	764	219	–	–	–	–
Other forward interest rate transactions	159	591	14	15	19	35
Total	**136,835**	**140,271**	**3,269**	**3,612**	**3,059**	**3,870**

Derivatives transactions with interest rate and foreign exchange risks

(€ m)	Nominal values		Positive market values		Negative market values	
	2018	2017	2018	2017	2018	2017
Cross-currency interest rate swaps	6,588	10,529	58	156	72	110
Total	**6,588**	**10,529**	**58**	**156**	**72**	**110**

Derivatives transactions with foreign exchange risks

(€ m)	Nominal values		Positive market values		Negative market values	
	2018	2017	2018	2017	2018	2017
Forward exchange transactions	3,448	7,232	65	58	31	53
Currency options						
Purchases	178	235	7	14	–	–
Sales	128	213	–	–	2	6
Total	**3,754**	**7,680**	**72**	**72**	**33**	**59**

Derivatives transactions with equity and other price risks

(€ m)	Nominal values		Positive market values		Negative market values	
	2018	2017	2018	2017	2018	2017
Equity options						
Purchases	7	113	–	43	–	–
Sales	–	96	–	–	–	43
Exchange-traded contracts	10	78	–	–	–	–
Equity/index-based swaps	54	80	10	14	–	–
Commodity-based transactions	–	–	–	–	–	–
Total	**71**	**367**	**10**	**57**	**–**	**43**

Credit derivatives

(€ m)	Nominal values		Positive market values		Negative market values	
	2018	2017	2018	2017	2018	2017
Guarantor position	48	96	1	1	–	–
Collateral taker position	55	170	13	26	–	–
Total	**103**	**266**	**14**	**27**	**–**	**–**

Credit derivative under the second loss guarantee

(€ m)	Nominal values		Positive market values		Negative market values	
	2018	2017	2018	2017	2018	2017
Collateral-taker position	–	1,107	–	199	–	–
Total	**–**	**1,107**	**–**	**199**	**–**	**–**

Derivatives transactions with structured products

(€ m)	Nominal values		Positive market values		Negative market values	
	2018	2017	2018	2017	2018	2017
Structured products	3,813	3,912	251	289	362	395
Total	**3,813**	**3,912**	**251**	**289**	**362**	**395**

Derivatives transactions in fair value hedge accounting

(€ m)	Nominal values		Positive market values		Negative market values	
	2018	2017	2018	2017	2018	2017
Fair value hedges						
Interest rate swaps	17,188	22,942	326	431	614	236
Total	**17,188**	**22,942**	**326**	**431**	**614**	**236**

II. Counterparty classification

Counterparty classification

(€ m)	Nominal values		Positive market values		Negative market values	
	2018	2017	2018	2017	2018	2017
OECD banks	68,350	81,234	1,561	1,918	2,616	3,163
Non-OECD banks	56	96	1	2	–	1
Non-banks[1]	95,514	99,587	2,205	2,473	1,175	1,167
Public authorities	4,432	5,917	233	1,250	349	382
Total	**168,352**	**186,834**	**4,000**	**5,643**	**4,140**	**4,713**

[1] Including exchange-traded contracts

III. Maturities

Maturities

(€ m)	Positive market value of derivatives		Positive market value of derivatives from fair value hedging		Negative market value of derivatives		Negative market value of derivatives from fair value hedging	
	2018	2017	2018	2017	2018	2017	2018	2017
Residual maturity								
Up to 3 months	107	174	–	–	100	154	–	–
3 months to 1 year	107	153	17	19	122	152	4	8
1 year to 5 years	775	922	214	182	877	1,057	148	147
Over 5 years	2,685	3,964	95	230	2,427	3,114	462	81
Total	**3,674**	**5,213**	**326**	**431**	**3,526**	**4,477**	**614**	**236**

60. Lease receivables and liabilities

Operating leases where Hamburg Commercial Bank acts as a lessee serve the purpose of leasing technical facilities and equipment required to operate IT networks, among other purposes. In addition, Hamburg Commercial Bank is a lessee of real estate and motor vehicles.

In operating leases, Hamburg Commercial Bank acts as lessor for real estate.

In the case of finance leases on the US market, Hamburg Commercial Bank acts as lessor under sale-and-lease-back leasing arrangements to finance photovoltaic installations.

I. Lessee under operating leases

Minimum lease payments under operating leases

(€ m)	2018	2017
Minimum lease payments due		
Up to 1 year	30	30
1 year to 5 years	51	80
More than 5 years	–	–
Total	**81**	**110**

Out of the minimum lease payments to be paid, multi-component agreements that include both leasing and service payments account for: € 28 million for up to one year (previous year: € 28 million) and € 49 million for one year to five years (previous year: € 78 million).

Expenses for lease payments

(€ m)	2018	2017
Expenses for		
Minimum lease payments	30	30
Total	**30**	**30**

The expenses for minimum lease payments in the reporting year include € 28 million that is attributable to multi-component agreements that include both leasing and service payments (previous year: € 27 million).

Expenses on assets used under operating leases are disclosed in Administrative expenses (cf. Note 16).

II. Lessor under operatingleases

Minimum lease payments to be expected under operating leases

(€ m)	2018	2017
Minimum lease payments to be received		
Up to 1 year	5	8
1 year to 5 years	14	27
More than 5 years	8	11
Total	**27**	**46**

Income from conditional leasing payments was neither recorded in the reporting period nor in the previous year.

III. Lessor under financeleases

Finance leases

(€ m)	2018	2017
Outstanding lease payments	46	51
+ Guaranteed residual values	14	14
= Minimum lease payments	60	65
+ Non-guaranteed residual values	18	17
= Gross investment	78	82
– Unearned finance income	4	6
= Net investment	74	76
– Net present value of non-guaranteed residual values	13	12
= Net present value of minimum lease payments	**61**	**64**

The gross investments amount and the net present value of the minimum lease payments break down by maturity as follows:

BREAKDOWN OF RESIDUAL MATURITIES

(€ m)	Gross investments in the lease		Present value of minimum lease payments	
	2018	2017	2018	2017
Minimum lease payments to be received				
Up to 1 year	19	8	17	6
1 year to 5 years	16	30	14	27
More than 5 years	43	44	30	31
Total	**78**	**82**	**61**	**64**

Income from conditional lease payments was neither recorded during the year nor in the previous year.

61. Disclosures on collateral transferred and financial assets transferred with retention of rights and/or obligations

I. Collateral transferred

As at 31 December 2018, Hamburg Commercial Bank had transferred assets as collateral which do not meet the requirements for derecognition under IFRS 9 (previous year: IAS 39). The assets transferred as collateral continue to be recognised in the Group statement of financial position as the interest rate risk, credit risk and other material risks as well as the prospects of appreciation and interest income largely reside with Hamburg Commercial Bank.

The following table mainly shows the collateral used to collateralise OTC derivative transactions and funds raised at central banks and other credit institutions. Notes on repurchase agreements are separately disclosed below. A small amount of collateral has been transferred in the course of securities lending business.

CARRYING AMOUNTS OF TRANSFERRED COLLATERAL

(€ m)	2018	2017
Receivables	8,304	7,690
Loans and advances to banks	2,356	2,254
Loans and advances to customers	5,948	5,436
Trading assets/Financial investments	92	341
Total	**8,396**	**8,031**

Money market borrowing generally involves pledging and transferring securities lodged with the European Central Bank. Promissory notes and other receivables from lending are not pledged to the European Central Bank or other banks, but are assigned without this being disclosed. It is not possible to resell or pledge in the interim.

In addition, Hamburg Commercial Bank concludes repurchase agreements under repo master agreements both on a national and international scale. The associated liabilities are recognised under Liabilities to banks or Liabilities to customers. At the end of the reporting period, the carrying amount of the securities transferred as collateral in the framework of repo transactions was € 104 million (previous year: € 1,284 million). The fair value amounts to € 104 million (previous year: € 1,284 million). The corresponding liabilities are recognised in the amount of € 101 million (previous year: € 1,692 million) with the fair value corresponding to the carrying amount. Taking into account the netting of receivables and liabilities with our business partners, a net position of € 3 million arose from the fair values of the assets transferred and the associated liabilities (previous year: € -408 million). Collateral transferred under repo transactions can be resold or repledged.

Repo and securities lending transactions are monitored by measuring transactions on a daily basis. If there is a shortfall in collateral the counterparty may require Hamburg Commercial Bank to provide additional securities to increase collateral. Where Hamburg Commercial Bank has provided collateral and the market situation changes such that the cover provided is excessive, it is entitled to require the counterparty to release collateral. The collateral provided is subject to a full transfer of rights, i.e. the party receiving collateral may act like an owner and in particular may transfer or pledge such collateral. In the case of securities collateral, securities of the same type and quality ('the same sort') must be delivered or returned unencumbered. Where collateral has been provided in the form of securities, it may not be returned in cash.

The above conditions and collateral modalities apply to tri-party repo transactions between Hamburg Commercial Bank and its counterparties accordingly. The transactions are executed via a tri-party agent.

II. Financial assets transferred with retention of rights and/or obligations

Hamburg Commercial Bank has transferred assets to third parties outside the Group that meet the conditions for full derecognition. The rights and obligations retained under these transfers were of an overall immaterial nature. The risks become transparent by recognition of provisions and/or recording of contingent liabilities. There is a hypothetical repurchase option relating to the sale of an equity holding, which the Bank, however, can only exercise based on the occurrence of certain biometric events. The option has a time value of € 0; it entails no risk.

62. Trust transactions

The table below shows the volume of trust transactions not recognised in the statement of financial position.

Trust transactions

(€ m)	2018	2017
Loans and advances to customers	3	4
Trust assets	**3**	**4**
Liabilities to customers	3	4
Trust liabilities	**3**	**4**

63. Related parties

Hamburg Commercial Bank does business with related parties and companies.

These include the funds and accounts managed by Cerberus Capital Management, L.P. and J.C. Flowers IV L.P., which exert a significant influence over the Bank.

Furthermore, business relations exist with subsidiaries which are controlled but not included in the Group financial statements for reasons of materiality, associates, joint ventures, individuals in key positions and their relatives and companies controlled by these individuals. Individuals in key positions comprise exclusively the members of the Management and Supervisory Boards of Hamburg Commercial Bank AG.

In the course of the normal business operations transactions are entered into at arm’s length with companies and parties that are related parties. These transactions include loans, call and fixed-term deposits, derivatives and securities transactions.

I. Entities with a significant influence over the Bank

As at the balance sheet date, there were no transactions with entities that have a significant influence over the Bank.

II. Subsidiaries

The transactions with unconsolidated subsidiaries are shown below:

Subsidiaries - assets

(€ m)	2018	2017
Loans and advances to banks	-	-
Loans and advances to customers	1	10
Loan loss provisions	-1	–
Total	**–**	**10**

Subsidiaries – liabilities

(€ m)	2018	2017
Other liabilities	9	1
Total	**9**	**1**

Subsidiaries – income statement

(€ m)	2018	2017
Net interest income	–	1
Result from financial instruments categorised as FVPL	2	–
Other operating income	4	4
Total	**6**	**5**

Other financial liabilities to subsidiaries as at the balance sheet date amount to € 3 million (previous year: € 0 million).

III. Associates

As in the same period of the previous year, there were no transactions with associates on the balance sheet date.

IV. Joint ventures

The following tables show the transactions with joint ventures:

Joint ventures – assets

(€ m)	2018	2017
Loans and advances to customers	15	16
Total	**15**	**16**

Joint ventures – liabilities

(€ m)	2018	2017
Liabilities to customers	2	15
Total	**2**	**15**

Joint ventures – income statement

(€ m)	2018	2017
Result from financial instruments categorised as FVPL	1	1
Total	**1**	**1**

V. Other related parties and companies

The following transactions had been entered into with individuals in key positions at Hamburg Commercial Bank AG and their close relatives or companies controlled by these individuals as at the balance sheet date:

Other related parties and companies – liabilities

(€ m)	2018	2017
Liabilities to customers	1	1
Total	**1**	**1**

VI. Remuneration of persons in key management positions

Up until the successful closing of the privatisation on 28 November 2018, the remuneration of each member of the Management Board of Hamburg Commercial Bank AG (formerly HSH Nordbank AG) was limited to € 500,000 per year (total fixed salary) in accordance with the guarantee agreement for as long as Hamburg Commercial Bank AG was not capable of making dividend distributions. Remuneration payable for secondary employment undertaken by the Management Board at the request of the Supervisory Board was set off against the remuneration entitlement set out in the employment contract.

Any additional variable remuneration was excluded under the terms of the guarantee agreement. The Management Board has opted not to collect a premium for a successful privatisation that would have been possible in line with the EU decision of 2 May 2016.

The Bank did not offer additional long-term incentives such as equity option schemes.

Following its privatisation on 28 November 2018, Hamburg Commercial Bank AG concluded new employment contracts with the current members of the Management Board. The remuneration system was also adjusted.

In addition to their fixed salary, each member of the Management Board receives a pension contribution corresponding to 20 % of their fixed annual salary and appropriate remuneration in kind.

LONG-TERM VARIABLE COMPENSATION PROGRAMME, INCLUDING SHARE-BASED PAYMENT

The new employment contracts of the Management Board include performance-related variable remuneration. Within this context, Management Board members receive 50 % of their annual bonus for the performance years leading up to 31 December 2021 in cash (cash bonus) and 50 % in the form of shares (share bonus) in Hamburg Commercial Bank AG.

40 % of the payment of the cash bonus and the transfer of the shares will be made in the year following the performance period in question, with 60 % subject to a deferral period of up to seven years.

The Bank’s Supervisory Board uses an independent valuation for each performance year to determine the price at which the share bonus earned in euros is converted into shares in the Bank.

The variable remuneration was recognised in administrative expenses (personnel expenses) as at 31 December 2018.

The following table shows the remuneration of persons in key management positions. Remuneration of the Supervisory Board consists of additions to provisions for the activities of the Supervisory Board carried out during the financial year excluding value-added tax. See Section VIII for further details.

Remuneration of persons in key management positions

(€ k)	Management Board		Supervisory Board		Total	
	2018	2017	2018	2017	2018	2017
Short-term benefits	2,560	2,148	840	468	3,400	2,616
Termination benefits	167	–	–	–	167	–
Other long-term benefits	133	–	–	–	133	–
Post-employment benefits	473	400	–	–	473	400
Share-based payment	133	–	–	–	133	–
Total remuneration	**3,466**	**2,548**	**840**	**468**	**4,306**	**3,016**

VII.Additional disclosures under Section 315e HGB

Hamburg Commercial Bank is obliged to provide additional disclosures in its Group financial statements under Section 315e HGB. Several differences compared to the IFRS disclosures should be borne in mind in this regard: termination benefits payable are not included in the total remuneration of the active members of the Management Board. This remuneration is disclosed instead under total remuneration payable to former members of the Management Board. Furthermore, in contrast to the presentation under IFRS, the total remuneration of active members of the Management Board only includes the variable remuneration resulting from share-based payments.

Remuneration of executive bodies

(€ k)	2018	2017
Total remuneration of all active members of executive bodies		
Management Board	3,166	2,548
Supervisory Board	840	468
Total	**4,006**	**3,016**
Total remuneration of former members of executive bodies and their surviving dependants		
Management Board	2,989	2,787

As at 31 December 2018, a total of €k 53,506 (previous year: €k 56,115) was added to provisions for pension obligations relating to former members of the Management Board and their surviving dependants.

As was the case in the previous year, there were no advances, loans and other liabilities to members of the Management Board as at 31 December 2018. For members of the Supervisory Board they amounted to € 0 (previous year: €k 54). . In the 2018 reporting year no new loans were granted to members of the Supervisory Board.

Repayments of loans by members of the Supervisory Board totalled €k 54 in 2018 (previous year: €k 96) .

VIII. Disclosure of Supervisory Board remuneration

The members of the Supervisory Board receive remuneration for their service during a financial year in an amount determined by the Annual General Meeting of the following year. The remuneration for the Supervisory Board for the 2017 financial year was therefore paid in the 2018 reporting period. Appropriate provisions have been recognised in the 2018 Annual Accounts for the 2018 reporting year.

The remuneration system that applied up until 28 November 2018 was based on the requirements of the German Corporate Governance Code and was organised as follows after the resolution of the Annual General Meeting of HSH Nordbank AG on 23 May 2014 and applied to the term of office of the Supervisory Board that has started on 23 May 2014:

Remuneration system

(€) Executive body	Function	Fixed component	Attendance fee
Supervisory Board	Chair	25,000	250
	Deputy Chair	18,000	250
	Member	11,000	250
Risk Committee	Chair	15,000	250
	Member	7,000	250
Executive Committee	Chair	15,000	250
	Member	7,000	250
Audit Committee	Chair	15,000	250
	Member	7,000	250
Remuneration Monitoring Committee	Chair	12,000	250
	Member	5,000	250

The Mediation Committee to be formed under the German Codetermination Act of 1976 (Mitbestimmungsgesetz) did not receive any separate remuneration. Members of the Supervisory Board were also reimbursed for any value-added tax payable and for their expenses.

A new Supervisory Board has been in office since 28 November 2018, for which a new remuneration system is expected to be defined with retroactive effect from 28 November 2018. The new remuneration system will be approved at an extraordinary general meeting in mid-March 2019. The amount set up as provisions for the reporting period already includes the expected change.

€k 554 of the amount provided for in the 2017 financial year (€k 557, thereof VAT: €k 89) was paid to the members of the Supervisory Board in the reporting period. This includes €k 86 of value-added tax.

€ 1 million has been set up in provisions for activities of the Supervisory Board in the reporting year (thereof VAT: €k 160) and will be disbursed after the Annual General Meeting provided a corresponding resolution is passed by the 2019 Annual General Meeting. The expected remuneration (excluding value-added tax) is distributed as follows among the Supervisory Board members who were in office up until 28 November 2018/31 December 2018 (employee representatives):

Members of the Supervisory Board

(€)	Fixed remuneration		Attendance fee		Total	
Members of the Supervisory Board	2018	2017	2018	2017	2018	2017
Dr Thomas Mirow, Chair	53,666	59,000	5,250	6,000	58,916	65,000
Olaf Behm, Deputy Chair	43,548	44,000	7,000	6,500	50,548	50,500
Stefanie Arp[1]	–	15,682	–	3,000	–	18,682
Peter Axmann	18,000	18,000	2,750	3,250	20,750	21,250
Simone Graf	29,367	30,000	5,750	5,250	35,117	35,250
Silke Grimm	15,005	16,000	1,250	2,250	16,255	18,250
Cornelia Hintz	11,000	11,000	2,250	2,500	13,250	13,500
Stefan Jütte	23,649	26,000	3,000	3,500	26,649	29,500
Dr Rainer Klemmt-Nissen	27,288	30,000	5,250	5,750	32,538	35,750
Rieka Meetz-Schawaller	17,367	18,000	3,500	3,500	20,867	21,500
Bert Michels[2]	18,000	2,049	3,250	250	21,250	2,299
Dr David Morgan[3]	16,373	18,000	2,500	1,750	18,873	19,750
Dr Philipp Nimmermann	33,655	37,000	5,000	5,500	38,655	42,500
Stefan Schlatermund	18,000	18,000	3,000	3,750	21,000	21,750
Klaus-Dieter Schwettscher	11,000	11,000	2,250	2,500	13,250	13,500
Elke Weber-Braun	23,649	26,000	2,250	3,500	25,899	29,500
Jörg Wohlers	22,740	25,000	4,250	4,500	26,990	29,500
Total	**382,307**	**404,731**	**58,500**	**63,250**	**440,807**	**467,981**

[1] until 14 November 2017
[2] from 15 November 2017
[3] Amounts before deduction of Supervisory Council tax and solidarity surcharge

The members of the Supervisory Board have again not provided any advisory or brokerage services or any other personal services to the Bank in the year 2018. Accordingly no additional remunerations were granted.

64. Other financial obligations

The transactions listed below include payment obligations under pending contracts or continuing obligations that cannot be recognised in the balance sheet as well as other financial obligations that could have a material effect on the future financial position of Hamburg Commercial Bank.

With regard to equity investments, there is a payment obligation vis-à-vis a fund in the amount of € 36 million.

Under the German Deposit Protection Act (EinSiG), the guarantee scheme of the German Savings Banks Finance Group is required to meet a statutory target volume by 3 July 2024. For this purpose, the guarantee scheme of the German Savings Banks Finance Group calculates the proportionate target volume allocated to the individual member institution every year, by 31 May of the current year, on the basis of data as at 31 December of the previous year, and arrives at the annual premium per member institution based on this data. The premium is collected before 30 September of each year. In previous years, Hamburg Commercial Bank AG had contributed a portion of its premium obligations as irrevocable payment obligations (total € 6 million, previous year: € 2 million). Special or additional contributions over and above the annual membership fees referred to above may be levied, for instance, as part of a compensation case where support is provided. This means that, until it leaves the guarantee scheme of the German Savings Banks Finance Group at the end of 2021 and until the planned subsequent seamless transition of Hamburg Commercial Bank AG to the deposit guarantee fund for private banks, the Bank is obliged to pay any special or additional contributions potentially levied by the guarantee scheme of the German Savings Banks Finance Group, and these represent a risk with regard to the financial position of Hamburg Commercial Bank AG.

With the transposition of the Bank Recovery and Resolution Directive (BRRD) into German law a new legal basis for determining the bank levy came into force as at 1 January 2015. The target amount of the EU-wide Single Resolution Fund (SRF) is to be achieved by 1 January 2024 through contributions paid by European banks. The current levy is determined by the supervisory authorities as at 31 May of each year and is payable by 30 June. Subsequent assessments are not provided for.

Obligations amounting to € 77 million (previous year: € 105 million) result from leasing agreements for IT services.

Long-term rental agreements for office space result in annual obligations of approximately € 1 million (previous year: € 1 million).

Under a sale of an equity holding the Bank has undertaken to purchase fund units at the market price up to a nominal amount of € 8 million (previous year: € 8 million).

The estimated payments made to BVV Versorgungskasse des Bankgewerbes e.V. amount to € 1 million (previous year: € 2 million). These include the additional contributions to compensate for the reduction in pension payments to employees applied by BVV Versicherungsverein des Bankgewerbes a.G. and BVV Versorgungskasse des Bankgewerbes e.V. in order to maintain the original benefit amount based on the individual pension commitments for these employees and prevent any pension gaps.

As part of its former guarantor function the Bank also has a general liability towards Deka Bank Deutsche Girozentrale together with other former shareholders. It applies to liabilities entered into until 18 July 2001 regardless of their term.

There exist no material other financial obligations apart from those listed above.

65. List of shareholders

The following information is based on German commercial law.

Consolidated subsidiaries with a share of voting rights of the Bank of more than 50 %

Serial no.	Name/place	Share	Voting rights	Currency code	Equity capital in respective currency	Income/loss in respective currency
1	Avia Management S.à.r.l., Luxembourg, Luxembourg	100.00	100.00	EUR	-5,646.42	10,944.73
2	BINNENALSTER-Beteiligungsgesellschaft mbH, Hamburg	100.00	100.00	EUR	253,496.50	-8,313.52
3	Bu Wi Beteiligungsholding GmbH, Hamburg	100.00	100.00	EUR	21,202.86	2,222.82
4	CAPCELLENCE Dritte Fondsbeteiligung GmbH, Hamburg[1]	100.00	100.00	EUR	2,204,177.23	3,880,617.08
5	CAPCELLENCE Erste Fondsbeteiligung GmbH, Hamburg[1]	100.00	100.00	EUR	1,067,999.66	306,958.62
6	CAPCELLENCE Holding GmbH & Co. KG, Hamburg[1]	100.00	100.00	EUR	113,201,642.08	4,542,670.57
7	Capcellence Vintage Year 06/07 Beteiligungen GmbH & Co. KG, Hamburg[1]	83.33	99.91	EUR	161,281.85	121,488.33
8	Capcellence Vintage Year 07/08 Beteiligungen GmbH & Co. KG, Hamburg[1]	90.91	99.99	EUR	799,359.07	-23,083.57
9	CAPCELLENCE Vintage Year 11 Beteiligungen GmbH & Co. KG, Hamburg[1]	83.33	99.99	EUR	4,389,660.12	2,673,987.59
10	CAPCELLENCE Vintage Year 13 Beteiligungen GmbH & Co. KG, Hamburg[1]	90.91	99.47	EUR	-30,681.12	1,250,457.70
11	CAPCELLENCE Vintage Year 16 Beteiligungen GmbH & Co. KG, Hamburg[1]	83.33	99.99	EUR	14,548,105.44	-126,600.24
12	CAPCELLENCE Zweite Fondsbeteiligung GmbH, Hamburg[1]	100.00	100.00	EUR	5,015,613.44	2,620,376.55
13	HSH Auffang- und Holdinggesellschaft mbH & Co. KG, Hamburg	100.00	100.00	EUR	2,321,685.25	359,521.34
14	HSH Care+Clean GmbH, Hamburg[1] [3]	51.00	51.00	EUR	25,000.00	41,793.68
15	HSH Facility Management GmbH, Hamburg[2]	100.00	100.00	EUR	205,600.00	-31,809.41
16	HSH Gastro+Event GmbH, Hamburg[1] [3]	100.00	100.00	EUR	25,000.00	51,876.22
17	HSH Move+More GmbH, Kiel[1] [3]	51.00	51.00	EUR	25,000.00	303,163.90
18	HSH N Finance (Guernsey) Limited, St. Peter Port, Guernsey	100.00	100.00	EUR	346,164.00	-140,303.00
19	HSH N Funding II, George Town, Cayman Islands[12]	56.33	100.00	USD	654,305,988.00	36,276,800.00
20	HSH Nordbank Securities S.A., Luxembourg, Luxembourg	100.00	100.00	EUR	207,855,834.61	9,355,834.61
21	HSH N Residual Value Ltd., Hamilton, Bermuda	100.00	100.00	USD	3,928,126.00	16,324.00
22	HSH Private Equity GmbH, Hamburg[2]	100.00	100.00	EUR	550,000.00	-2,404,337.61
23	Neptune Finance Partner S.à.r.l., Luxembourg, Luxembourg	100.00	100.00	USD	73,894.70	0.00
24	Neptune Finance Partner II S.à.r.l., Luxembourg, Luxembourg[10]	100.00	100.00	USD	62,763.63	0.00
25	RESPARCS Funding Limited Partnership I, Hong Kong, Hong Kong[1] [12]	0.01	100.00	USD	-1,442,877.00	7,092,061.00
26	RESPARCS Funding II Limited Partnership, St. Helier, Jersey[1] [12]	0.01	100.00	EUR	-125,899,585.00	405,671.00

Consolidated subsidiaries with a share of voting rights of the Bank of 50 % or less

- of which subsidiaries due to a principal-agent relationship

Serial. no.	Name/place	Share	Voting rights	Currency code	Equity capital in respective currency	Income/loss in respective currency
27	Next Generation Aircraft Finance 2 S.à.r.l.,Findel, Luxembourg[1) 12)]	49.00	49.00	EUR	-5,648,667.00	3,785,444.00
28	Next Generation Aircraft Finance 3 S.à.r.l., Findel, Luxembourg[1) 12)]	49.00	49.00	EUR	-6,742,994.00	3,929,202.00

- of which subsidiaries due to contractual rights

Serial. no.	Name/place	Share	Voting rights	Currency code	Equity capital in respective currency	Income/loss in respective currency
29	Adessa Grundstücksverwaltungsgesellschaft mbH & Co. Vermietungs KG, Mainz[12)]	0.00	0.00	EUR	-389,309.99	49,214.46
30	GmbH Altstadt Grundstücksgesellschaft, Mainz[1) 12)]	50.00	50.00	EUR	-239,917.11	279,088.35
31	OCEAN Funding 2013 GmbH, Frankfurt am Main[12)]	0.00	0.00	EUR	29,978.98	1,167.05
32	Senior Assured Investment S.A., Luxembourg, Luxembourg[12)]	0.00	0.00	EUR	31,000.00	0.00

Unconsolidated subsidiaries with a share of voting rights of the bank of more than 50 %

Serial. no.	Name/place	Share	Voting rights	Currency code	Equity capital in respective currency	Income/loss in respective currency
33	Asian Capital Investment Opportunities Limited, Hong Kong, Hong Kong[1)]	51.00	51.00	USD	114.00	0.00
34	Aviation Leasing OpCo France III, Paris, France[1)]	100.00	100.00	EUR	-387,581.00	-48,816.00
35	Aviation Leasing OpCo France IV, Paris, France[1)]	100.00	100.00	EUR	-92,893.00	-31,076.00
36	CAPCELLENCE Vintage Year 16 Beteiligungen GmbH, Hamburg[1)]	100.00	100.00	EUR	4,166.35	-253,492.58
37	European Capital Investment Opportunities Limited, St. Helier, Jersey[1)]	51.00	51.00	EUR	225.00	-103.00
38	HSH N Structured Situations Limited, St. Helier, Jersey[8)]	100.00	100.00	USD	346,449.00	-68.00
39	NORDIC BLUE CONTAINER V LIMITED, Majuro, Marshall Islands	100.00	100.00		[4)]	[4)]
40	PERIMEDES GmbH, Hamburg	100.00	100.00	EUR	31,190.81	2,707.20

Unconsolidated subsidiaries with a share of voting rights of the Bank of 50 % or less

- of which subsidiaries due to a principal-agent relationship

Serial. no.	Name/place	Share	Voting rights	Currency code	Equity capital in respective currency	Income/loss in respective currency
41	AGV Irish Equipment Leasing No. 7 Limited, Dublin, Ireland[1)]	49.00	49.00	USD	20,674.00	-21,122.00
42	Amentum Aircraft Leasing No. Ten Limited, Dublin, Ireland[1) 7)]	49.00	49.00	USD	2,377.00	10,253,806.00

- of which subsidiaries due to contractual rights

Serial. no.	Name/place	Share	Voting rights	Currency code	Equity capital in respective currency	Income/loss in respective currency
43	Lyceum Capital Fund 2000 (Number Five) GmbH & Co. KG, Stuttgart[1) 6)]	80.00	0.00	EUR	-240,902.29	0.00

Unconsolidated joint ventures

Serial. no.	Name/place	Share	Voting rights	Currency code	Equity capital in respective currency	Income/loss in respective currency
44	Infrastructure Holding S.à.r.l., Luxembourg, Luxembourg [5)]	0.00	0.00	EUR	12,500.00	0.00

Unconsolidated associates

Serial no.	Name/place	Share	Voting rights	Currency code	Equity capital in respective currency	Income/loss in respective currency
45	FSP CAPCELLENCE Beteiligungs GmbH, Hamburg[1)]	100.00	40.00	EUR	14,987,330.84	-47,178.34
46	Global Format GmbH & Co. KG, Munich	28.57	28.57	EUR	1,948,092.72	41,614.87
47	HGA New Office Campus-Kronberg GmbH & Co. KG, Hamburg	56.44	56.44	EUR	10,674,163.21	-448,692.74
48	KAIACA LLC, New York, USA[11)]	55.30	55.30	USD	20,206.69	0.00
49	MORATIM Produktions GmbH & Co. KG	20.66	20.66	EUR	-1,069,912.46	835,297.47
50	4Wheels Management GmbH, Düsseldorf[1) 9)]	68.75	40.00	EUR	5,222,630.31	-981,266.48

Equity holdings

Serial. no.	Name/place	Share	Voting rights	Currency code	Equity capital in respective currency	Income/loss in respective currency
51	AKA Ausfuhrkredit-Gesellschaft mbH, Frankfurt am Main	1.33	1.33	EUR	238,732,103.15	11,080,000.00
52	CapVis Equity III L.P., St. Helier, Jersey[1]	2.50	0.00	EUR	266,051,522.00	59,349,078.00
53	CVC European Equity Partners V (A) L.P., St. Helier, Jersey[1]	0.45	0.00	EUR	1,546,534,316.00	301,837,946.00
54	Deutsche WertpapierService Bank AG, Frankfurt am Main	2.51	2.51	EUR	193,702,296.19	22,114,512.74
55	EDD AG, Düsseldorf	0.89	0.89	EUR	27,792,319.98	-3,009,362.33
56	EURO Kartensysteme GmbH, Frankfurt am Main	2.82	2.82	EUR	11,834,836.14	199,431.92
57	GB Deutschland Fund GmbH & Co. KG, Hamburg[1]	4.69	0.00	EUR	24,277,672.21	10,691,119.74
58	GLB GmbH & Co. OHG, Frankfurt am Main	15.77	15.77	EUR	5,658,173.91	453,351.20
59	GLB-Verwaltungs-GmbH, Frankfurt am Main	15.80	15.80	EUR	53,707.83	1,964.86
60	Hamburgische Grundbesitz und Anlage GmbH & Co. Objekte Hamburg und Potsdam KG, Hamburg	5.15	5.16	EUR	10,946,020.84	1,103,626.68
61	HGA Objekt München GmbH & Co. KG, Hamburg	5.23	5.23	EUR	18,064,553.83	1,567,288.53
62	HGA Objekt Stuttgart GmbH & Co. KG, Hamburg	7.25	7.26	EUR	9,578,657.45	203,510.18
63	HGA Objekte Hamburg und Hannover GmbH & Co. KG, Hamburg	5.10	5.09	EUR	7,825,607.71	303,498.39
64	Hines European Development Fund Limited Partnership, Wilmington, USA[1]	9.90	9.90	EUR	61,892,000.00	-747,000.00
65	Next Commerce Accelerator Beteiligungsgesellschaft mbH & Co. KG, Hamburg	16.39	16.39	EUR	1,999,231.89	-20,768.11
66	Next Commerce Accelerator GmbH, Hamburg	16.67	16.67	EUR	37,309.08	-42,690.92
67	RSU Rating Service Unit GmbH & Co KG, Munich	13.60	13.60	EUR	14,030,218.77	909,363.72
68	Society for Worldwide Interbank Financial Telecommunication (S.W.I.F.T. SCRL), La Hulpe, Belgium	0.03	0.03	EUR	469,330,000.00	45,119,000.00
69	True Sale International GmbH, Frankfurt am Main	7.69	7.69	EUR	4,928,143.76	119,247.90
70	Vofü-Fonds I Hamburgische Grundbesitz und Anlage GmbH & Co. KG, Hamburg	5.10	5.09	EUR	106,513.06	1,542,002.50

1) Indirect holding.
2) A profit transfer agreement with the company is in place.
3) There is a profit transfer agreement with HSH Facility Management GmbH.
4) No data available.
5) Only data as at 31 December 2015 is available.
6) Only data as at 29 February 2016 is available.
7) Only data as at 30 June 2016 is available.
8) Only data as at 31 December 2016 is available.
9) Only data as at 31 July 2017 is available.
10) Only data as at 09 December 2017 is available.
11) This is not a subsidiary due to the requirement for a qualified voting majority for important decisions.
12) Structured entity.

Foreign exchange rates for € 1 as at 31 December 2018

Great Britain	GBP	0.8945
USA	USD	1.1450

66. Other disclosures in accordance with German commercial law

I. Basic principles

Under the terms of Section 315e (1) HGB, Hamburg Commercial Bank AG, which has its registered office in Hamburg (Hamburg commercial register number HRB 87366) and Kiel (Kiel commercial register number HRB 6127 KI) is required to observe the standards of the German Commercial Code in preparing and presenting the annual financial statements, as well as the IFRS standards. You may request the unabridged IFRS Group financial statements by following this link: www.hcob-bank.com. The complete list of equity holdings is set out in Note 65.

HSH Facility Management GmbH, Hamburg, and its subsidiaries HSH Care+Clean GmbH, Hamburg, HSH Gastro+Event GmbH, Hamburg, and HSH Move+More GmbH, Kiel, make use of the exemption from disclosure obligations in accordance with Section 264 (3) HGB.

II. Number of employees

The average number of employees as of the reporting date is calculated on the basis of staff figures at quarter-end for all fully consolidated companies:

Number of employees

	2018			2017
	Male	Female	Total	Total
Full-time employees	1,032	358	1,390	1,583
Part-time employees	104	438	542	636
Total	**1,136**	**796**	**1,932**	**2,219**
Apprentices/trainees	16	14	30	36

III. Corporate governance code

Hamburg Commercial Bank AG supports the aims of the German Corporate Governance Code and has recognised the Code's rules on a voluntary basis as an unlisted company. The Management Board and Supervisory Board of Hamburg Commercial Bank AG have given a declaration of conformity pursuant to Section 161 of the German Stock Corporation Act (AktG) that the recommendations of the German Corporate Governance Code Commission together with the restrictions have been complied with and will be complied with until the subsequent declaration is made. The Declaration of Conformity is published on the website of Hamburg Commercial Bank AG. The Declaration of Conformity does not form part of the Notes to the Group financial statements.

IV. Fees and activities of the auditor

AUDITOR'S ACTIVITIES

PricewaterhouseCoopers GmbH Wirtschaftsprüfungsgesellschaft audited the annual financial statements and Group financial statements of Hamburg Commercial Bank as at 31 December 2018 and conducted various audits of annual financial statements at subsidiaries. In addition, the review of the half-year financial report as at 30 June 2018 and, to a lesser extent, certain services relating confirmations for guarantee schemes were performed. In addition, tax consultancy services and services were provided in the form of opinions on technical issues and agreed investigations.

Auditors' fees within the meaning of IDW AcPS HFA 36 (new version)

Auditor'S fees

(€ m)	2018	2017
Audits of financial statements PWC GmbH (previous year: KPMG AG)	4	6
Other certification and valuation services PWC GmbH (previous year: KPMG AG)	–	1
Tax advisory services PWC GmbH (previous year: KPMG AG)	1	–
Other services PWC GmbH (previous year: KPMG AG)	–	2
Total	**5**	**9**

Seats on supervisory bodies

On the reporting date, the following seats are held by members of the Management Board on statutory supervisory bodies of major corporations or financial institutions:

ULRIK LACKSCHEWITZ
HSH Securities S.A., Luxembourg
Chair of the Supervisory Board

67. Names of Board members and directorships held

I. The Supervisory Board of the Hamburg Commercial Bank Group

JUAN RODRÍGUEZ INCIARTE, MADRID
Chair
CEO of Sareema Inversiones S.A.
(from 28 November 2018)

DR THOMAS MIROW, HAMBURG
Chair
Former President of the European Bank for Reconstruction and Development, London
(until 28 November 2018)

OLAF BEHM, HAMBURG
Deputy Chair
Employee of Hamburg Commercial Bank AG

GEOFFREY ADAMSON, NEW YORK
Partner GoldenTree Asset Management
(from 28 November 2018)

PETER AXMANN, HAMBURG
Employee of Hamburg Commercial Bank AG

MICHAEL CHRISTNER, ANDORRA
Managing Director J.C. Flowers & Co. UK LLP
(from 28 November 2018)

JAMES CHRISTOPHER FLOWERS, NEW YORK
Founder and Managing Director of J.C. Flowers & Co. LLC
(from 28 November 2018)

ALLEN GIBSON, COLUMBUS
Chief Investment Officer Centaurus Capital LP
(from 28 November 2018)

MANUEL GONZÁLEZ CID, MADRID
Senior Advisor Cerberus Global Investment Advisors, LLC
(from 28 November 2018)

SIMONE GRAF, ALTENHOLZ
Employee of Hamburg Commercial Bank AG

SILKE GRIMM, REINBEK
Member of the Board of Euler Hermes Deutschland AG
(until 28 November 2018)

CORNELIA HINTZ, DORTMUND
Federal state secretary ver.di district North Rhine-Westphalia

STEFAN JÜTTE, BONN
Former Chair of the Management Board of Deutsche Postbank AG
(until 28 November 2018)

DR RAINER KLEMMT-NISSEN, HAMBURG
Managing Director, HGV Hamburger Gesellschaft für Vermögens- und Beteiligungsmanagement mbH
(until 28 November 2018)

CHAD LEAT, NEW YORK
Financial Advisor
(from 28 November 2018)

RIEKA MEETZ-SCHAWALLER, KIEL
Employee of Hamburg Commercial Bank AG

BERT MICHELS, HAMBURG
Employee of Hamburg Commercial Bank AG

DR DAVID MORGAN, LONDON
Managing Director J.C. Flowers & Co UK LLP
(until 28 November 2018)

MARK NEPORENT, ARMONK
Chief Operating Officer, Senior Legal Officer and
Senior Managing Director Cerberus Capital Management, L.P.
(from 28 November 2018)

DR PHILIPP NIMMERMANN, KIEL
Secretary of State at the Schleswig-Holstein Ministry of Finance
(until 28 November 2018)

STEFAN SCHLATERMUND, HAMBURG
Employee of Hamburg Commercial Bank AG

KLAUS-DIETER SCHWETTSCHER, REINBEK
Representative of ver.di's federal management board

ELKE WEBER-BRAUN, HAMBURG
Independent chartered accountant
(until 28 November 2018)

MARK WERNER, NEW YORK
Financial Advisor
(from 28 November 2018)

PAULUS DE WILT, BREUKELEN
Chief Executive Officer NIBC Bank NV
(from 28 November 2018)

JÖRG WOHLERS, RELLINGEN
Former Member of the Board of Hamburger Sparkasse AG
and HASPA Finanzholding
(until 28 November 2018)

II. Members of the Risk Committee

CHAD LEAT
Chair
(from 28 November 2018)

STEFAN JÜTTE
Chair (until 28 November 2018)

GEOFF ADAMSON
(from 28 November 2018)

OLAF BEHM

MICHAEL CHRISTNER
(from 28 November 2018)

ALLEN GIBSON
(from 28 November 2018)

SIMONE GRAF

DR RAINER KLEMMT-NISSEN
(until 28 November 2018)

RIEKA MEETZ-SCHAWALLER
(until 28 November 2018)

DR THOMAS MIROW
(until 28 November 2018)

DR PHILIPP NIMMERMANN
(until 28 November 2018)

STEFAN SCHLATERMUND

MARK WERNER
(from 28 November 2018)

III. Members of the Audit Committee

PAULUS DE WILT
Chair
(from 28 November 2018)

ELKE WEBER-BRAUN
Chair
(until 28 November 2018)

PETER AXMANN

OLAF BEHM

MANUEL GONZÁLEZ CID
(from 28 November 2018)

BERT MICHELS

DR PHILIPP NIMMERMANN
(until 28 November 2018)

MARK WERNER
(from 28 November 2018)

JÖRG WOHLERS
(until 28 November 2018)

IV. Members of the General/ Nominating Committee

JUAN RODRÍGUEZ INCIARTE
Chair
(from 28 November 2018)

DR THOMAS MIROW
Chair (until 28 November 2018)

OLAF BEHM

MICHAEL CHRISTNER
(from 28 November 2018)

MANUEL GONZÁLEZ CID
(from 28 November 2018)

SIMONE GRAF
(until 28 November 2018)

DR RAINER KLEMMT-NISSEN
(until 28 November 2018)

DR DAVID MORGAN
(until 28 November 2018)

DR PHILIPP NIMMERMANN
(until 28 November 2018)

JÖRG WOHLERS
(until 28 November 2018)

V. Members of the Remuneration Control Committee

JUAN RODRÍGUEZ INCIARTE
Chair
(from 28 November 2018)

DR THOMAS MIROW
Chair (until 28 November 2018)

OLAF BEHM
(until 28 November 2018)

MICHAEL CHRISTNER
(from 28 November 2018)

ALLEN GIBSON
(from 28 November 2018)

SIMONE GRAF

SILKE GRIMM
(until 28 November 2018)

DR RAINER KLEMMT-NISSEN
(until 28 November 2018)

DR PHILIPP NIMMERMANN
(until 28 November 2018)

VI. Members of the Mediation Committee

JUAN RODRÍGUEZ INCIARTE
Chair
(from 28 November 2018)

DR THOMAS MIROW
Chair (until 28 November 2018)

OLAF BEHM

MICHAEL CHRISTNER
(from 28 November 2018)

DR RAINER KLEMMT-NISSEN
(until 28 November 2018)

RIEKA MEETZ-SCHAWALLER

VII. The Management Board of the Hamburg Commercial Bank Group

STEFAN ERMISCH
Born in 1966
Chief Executive Officer (CEO)

ULRIK LACKSCHEWITZ
Born in 1968
Chief Risk Officer (CRO) and Deputy CEO since 10 December 2018

DR NICOLAS BLANCHARD
Born in 1968
Chief Clients and Products Officer (CCO) (since 10 December 2018)

OLIVER GATZKE
Born in 1968
Chief Financial Officer (CFO)

TORSTEN TEMP
Born in 1960
Management Board member responsible for the Market divisions (until 31 December 2018)

Annex to the Group financial statements

Country-by-Country Reporting 2018

Basic principles

The requirements for country-specific reporting, referred to as country-by-country reporting in Article 89 of the Directive 2013/36/EU (Capital Requirement Directive, CRD IV), have been transposed into German law in Section 26a (1) of the German Banking Act (KWG).

Disclosure at Hamburg Commercial Bank
Hamburg Commercial Bank's country-by-country reporting includes the necessary information for all the subsidiaries fully consolidated in the Group financial statements as of this reporting date. Entities that were deconsolidated during the reporting year are not included in the figures presented. The geographical allocation is made on the basis of the location of a company's registered office. Branches are disclosed as independent companies. Representative offices are not listed. All accounting-related information is based on IFRS accounting.

In this report, Hamburg Commercial Bank defines the required size of turnover as the sum of total income as presented in the income statement and Other operating income (gross amounts before consolidation). The consolidated non-bank entities in particular report their turnover in Other operating income.

The profit or loss before tax disclosed in this report corresponds to the result before taxes of the individual entities presented. The tax position also corresponds to the definition under IFRS standards in the income statement.

The figure for the number of employees corresponds to the arrangement of Section 267 (5) of the German Commercial Code (HGB) for the entities still included in the Group financial statements as of the reporting date.

The information on the type of activities of the relevant companies is presented in line with the definitions used in Article 4 (1) CRR once the CRR came into effect.

The return on capital to be disclosed as at 31 December 2018, calculated as the quotient of net profit (Group net result after taxes) and total assets, is 0.14%.

Reporting
Country-specific details of turnover, profit or loss and taxes as well as employee numbers

(€ m/number) 2018 Country	Turnover	Profit or loss before tax	Tax on profit or loss (+) expense/ (-) income	Employees
EU				
Germany	1,714	146	11	1,840
Luxembourg	57	-8	–	56
Greece	2	–	–	8
Third countries				
Singapore	43	32	8	28
British Channel Islands	3	3	–	–
Hong Kong	4	4	–	–
Cayman Islands	1	1	–	–

(€ m) 2018	Germany	Luxembourg	Singapore
P&L amounts			
Hedging effect of the second loss guarantee	-67	64	3
Hedging effect of credit derivative second loss guarantee	39	-89	-
Net result from second loss guarantee financial instruments categorised as FVPL	80	-	-
Net result from compensation item	-30	-	-
Expenses for government guarantees	-149	-6	-3

Nature of activities and geographical location of the branches and fully consolidated subsidiaries

Serial. no.	Name of the company	City	Country	Nature of activities
1	Hamburg Commercial Bank AG	Hamburg, Kiel	Germany	Bank
2	Hamburg Commercial Bank AG, Luxembourg branch	Luxembourg	Luxembourg	Bank
3	Hamburg Commercial Bank AG, Singapore branch	Singapore	Singapore	Bank
4	Hamburg Commercial Bank AG, Athens branch	Athens	Greece	Bank
5	Adessa Grundstücksverwaltungsgesellschaft mbH & Co. Vermietungs KG	Mainz	Germany	Miscellaneous activities
6	Avia Management S.à.r.l.	Luxembourg	Luxembourg	Financial institution
7	BINNENALSTER-Beteiligungsgesellschaft mbH	Hamburg	Germany	Financial institution
8	Bu Wi Beteiligungsholding GmbH	Hamburg	Germany	Financial institution
9	CAPCELLENCE Dritte Fondsbeteiligung GmbH	Hamburg	Germany	Financial institution
10	CAPCELLENCE Erste Fondsbeteiligung GmbH	Hamburg	Germany	Financial institution
11	CAPCELLENCE Holding GmbH & Co KG	Hamburg	Germany	Financial institution
12	CAPCELLENCE Zweite Fondsbeteiligung GmbH	Hamburg	Germany	Financial institution
13	Capcellence Vintage Year 06/07 Beteiligungen GmbH & Co. KG	Hamburg	Germany	Financial institution
14	Capcellence Vintage Year 07/08 Beteiligungen GmbH & Co. KG	Hamburg	Germany	Financial institution
15	CAPCELLENCE Vintage Year 11 Beteiligungen GmbH & Co. KG	Hamburg	Germany	Financial institution
16	CAPCELLENCE Vintage Year 13 Beteiligungen GmbH & Co. KG	Hamburg	Germany	Financial institution
17	CAPCELLENCE Vintage Year 16 Beteiligungen GmbH & Co. KG	Hamburg	Germany	Financial institution
18	GmbH Altstadt Grundstücksgesellschaft	Mainz	Germany	Financial institution
19	HSH Auffang- und Holdinggesellschaft mbH & Co. KG	Hamburg	Germany	Financial institution
20	HSH Care+Clean GmbH	Hamburg	Germany	Miscellaneous activities
21	HSH Facility Management GmbH	Hamburg	Germany	Provider of ancillary services
22	HSH Gastro+Event GmbH	Hamburg	Germany	Miscellaneous activities
23	HSH Move+More GmbH	Kiel	Germany	Miscellaneous activities
24	HSH N Finance (Guernsey) Limited	St. Peter Port	Guernsey	Financial institution
25	HSH N Funding II	George Town	Cayman Islands	Financial institution
26	HSH Nordbank Securities S.A.	Luxembourg	Luxembourg	Bank
27	HSH N Residual Value Ltd.	Hamilton	Bermuda	Insurance company
28	HSH Private Equity GmbH	Hamburg	Germany	Financial institution
29	Neptune Finance Partner S.à.r.l.	Luxembourg	Luxembourg	Financial institution
30	Neptune Finance Partner II S.à.r.l.	Luxembourg	Luxembourg	Financial institution
31	Next Generation Aircraft Finance 2 S.à.r.l.	Findel	Luxembourg	Miscellaneous activities
32	Next Generation Aircraft Finance 3 S.à.r.l.	Findel	Luxembourg	Miscellaneous activities
33	OCEAN Funding 2013 GmbH	Frankfurt am Main	Germany	Miscellaneous activities
34	RESPARCS Funding Limited Partnership I	Hong Kong	Hong Kong	Financial institution
35	RESPARCS Funding II Limited Partnership	St. Helier	Jersey	Financial institution
36	Senior Assured Investment S.A.	Luxembourg	Luxembourg	Miscellaneous activities

Date of release for publication

The Management Board of Hamburg Commercial Bank has prepared the Group financial statements on 15 March 2019 and released these for forwarding to the Supervisory Board. The Supervisory Board is responsible for reviewing the Group financial statements and approving of these.

Hamburg/Kiel, 15 March 2019

Stefan Ermisch Ulrik Lackschewitz

Dr Nicolas Blanchard Oliver Gatzke

INDEPENDENT AUDITOR'S REPORT

To Hamburg Commercial Bank AG, Hamburg/Kiel

REPORT ON THE AUDIT OF THE CONSOLIDATED FINANCIAL STATEMENTS AND OF THE GROUP MANAGEMENT REPORT

AUDIT OPINIONS

We have audited the consolidated financial statements of Hamburg Commercial Bank AG, Hamburg/Kiel (formerly HSH Nordbank AG, Hamburg/Kiel), and its subsidiaries (the Group) which comprise the Group statement of financial position at at 31 December 2018, the Group statement of income, the Group statement of comprehensive income, the Group statement of changes in equity, the Group cash flow statement for the financial year from 1 January to 31 December 2018 and Group explanatory notes, including a summary of significant accounting policies. In addition, we have audited the group management report of Hamburg Commercial Bank AG, which is combined with the Company's management report, for the financial year from 1 January to 31 December 2018. In accordance with the German legal requirements, we have not audited the content of the statement on corporate governance pursuant to § [Article] 289f HGB [Handelsgesetzbuch: German Commercial Code] and § 315d HGB.

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

- the accompanying consolidated financial statements comply, in all material respects, with the IFRSs as adopted by the EU, and the additional requirements of German commercial law pursuant to § 315e Abs. [paragraph] 1 HGB and, in compliance with these requirements, give a true and fair view of the assets, liabilities and financial position of the Group as at 31 December 2018 and of its financial performance for the financial year from 1 January to 31 December 2018, and

- the accompanying group management report as a whole provides an appropriate view of the Group's position. In all material respects, this group management report is consistent with the consolidated financial statements, complies with German legal requirements and appropriately presents the opportunities and risks of future development. Our audit opinion on the group management report does not cover the content of the statement on corporate governance referred to above.

Pursuant to § 322 Abs. 3 Satz [sentence] 1 HGB, we declare that our audit has not led to any reservations relating to the legal compliance of the consolidated financial statements and of the group management report.

BASIS FOR THE AUDIT OPINIONS

We conducted our audit of the consolidated financial statements and of the management report in accordance with § 317 HGB and the EU Audit Regulation (No. 537/2014, referred to subsequently as "EU Audit Regulation") in compliance with German Generally Accepted Standards for Financial Statement Audits promulgated by the Institut der Wirtschaftsprüfer [Institute of Public Auditors in Germany] (IDW). Our responsibilities under those requirements and principles are further described in the "Auditor's Responsibilities for the Audit of the Consolidated Financial Statements and of the Group Management Report" section of our auditor's report. We are inde-pendent of the group entities in accordance with the requirements of European law and German commercial and professional law, and we have fulfilled our other German professional responsibilities in accordance with these requirements. In addition, in accordance with Article 10 (2) point (f) of the EU Audit Regulation, we declare that we have not provided non-audit services prohibited under Article 5 (1) of the EU Audit Regulation. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinions on the consolidated financial statements and on the management report.

KEY AUDIT MATTERS IN THE AUDIT OF THE CONSOLIDATED FINANCIAL STATEMENTS

Key audit matters are those matters that, in our professional judgment, were of most significance in our audit of the consolidated financial statements for the financial year from 1 January to 31 December 2018. These matters were addressed in the context of our audit of the consolidated financial statements as a whole, and in forming our audit opinion thereon; we do not provide a separate audit opinion on these matters.

In our view, the matters of most significance in our audit were as follows:

❶ Provisions for Restructuring in the context of the "Reset & Go" strategic program

❷ Accounting issues in connection with hybrid capital instruments

❸ Risk provisions in the customer lending business

❹ Deferred tax assets

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

① Matter and issue

② Audit approach and findings

③ Reference to further information

Hereinafter we present the key audit matters:

❶ **Provisions for Restructuring in the context of the "Reset & Go" strategic program**

① At the beginning of financial year 2018, Hamburg Commercial Bank AG announced its "Reset & Go" strategic program. As part of the new strategy, the Company is focussing on future customer requirements, structuring overarching business models at the bank and using new IT solutions. In the context of the closing in connection with the privatization on 28 November 2018, the outcomes of "Reset & Go" were used as a basis for developing a transformation agenda in 2018 which sets the overriding goal of increasing the Bank's profitability. To that end, a target operating model on a reduced cost basis was defined which calls for significant staff cuts, among other measures. In December 2018, employees were notified and negotiations with the employee representative bodies were initiated. The Company recognized an expense for a provision for restructuring amounting to EUR 282 million in 2018 in connection with the planned transformation measures. In our view, this matter was of particular significance for our audit, as the measurement of the restructuring provisions is significant in terms of its amount, and is based on estimates and assumptions made by the executive directors.

② The requirement for recognizing a provision for restructuring is first of all that the definition of restructuring measures pursuant to IAS 37.10 has been met. Afterwards, the general recognition and measurement criteria for provisions and the further criteria from IAS 37.72 have to be assessed. If the provision is a provision for termination benefits, the requirements of IAS 19 apply. In the context of our audit, we assessed whether the individual recognition criteria were met and whether the measurement of the restructuring provision was appropriate. For that purpose, we obtained and evaluated relevant evidence from the executive directors of the Company. We were able to satisfy ourselves that the matter as well as the estimates and assumptions made by the executive directors in connection with the recognition and measurement of a restructuring provision were sufficiently documented and substantiated. The measurement occurred within ranges considered by us to be reasonable.

③ The Company's disclosures relating to the provisions are contained in the notes to the financial statements in section 7 "Accounting and measurement principles" and in section 19 "Net income from restructuring and privatisation".

❷ **Accounting issues in connection with hybrid capital instruments**

① Hamburg Commercial Bank AG is party to several agreements concerning the establishment of silent partnerships, through which investors participate in the bank's commercial activities as silent partners ("hybrid capital investors"). These are hybrid capital instruments that are either entered into bilaterally with institutional investors or placed on the capital market. As a measure to restructure and optimize capital (so-called "liability management exercise"), the bank terminated all existing silent contributions during the financial year with effect from 31 December 2020. As a result of this, these silent contributions will be repaid by no later than financial year 2021 in accordance with the contractual terms and conditions. Due to the termination, the expected repayment amount must be re-estimated. The bank expects that the amounts to be repaid are likely to be significantly lower than the nominal amounts. In this connection, claims are being asserted against the Company in and out of the courts, calling for the instruments to be recovered, profit participations to be paid in arrears and the terminations to be invalid, among other things. The bank has recognized a provision for legal disputes in the consolidated financial statements. The effect of the re-estimate of cash flows (including compounded interest) from hybrid capital instruments, reported in the interest result, amounts to EUR 994 million. In our view, the issue as to whether and in what amount a provision to cover this risk had to be recognized and the re-estimate of expected cash flows were of significance for our audit, as the assumptions underlying the estimates were subject to considerable scope for judgment on the part of the executive directors.

② As part of our audit, we, among other things, assessed the process established by the Company for the recording, risk assessment and reporting of the legal disputes in the financial statements. We also assessed the measures established to estimate cash flows in the context of remeasuring the provision. Our assessment also included an examination of the substance of the bank's corporate planning. In addition, we analyzed the necessity of recognizing provisions in accordance with IAS 37 for the legal disputes in connection with the hybrid capital investors. Our assessment took into account the knowledge gained in the course of our regular meetings with the bank's legal department as well as from the assessments provided to us in writing on the outcomes of the respective proceedings. In addition, we have obtained confirmations from external lawyers. We have assessed the presentation of the matter and the associated accounting effects in the consolidated financial statements and consider them reasonable.

③ The new estimates of cash flows and the provisions for legal risks are discussed in the notes to the financial statements in section 7 "Accounting and measurement principles". In addition, the provisions for litigation risks and expenses are discussed in greater detail in note 41 "Provisions".

❸ Loan loss provisions in the customer lending business

① In the Company's consolidated financial statements loan receivables amounting to EUR 32,791 million are reported under the "Loans to customers" balance sheet item. The risk provision recognized for this amounted to EUR 831 million, which was reported in a separate item. The bank calculated the risk provision during the financial year using a 3-step model based on the expected credit loss system in accordance with IFRS 9, which became mandatory for the first time. For financial instruments in levels 1 and 2, mathematical-statistical techniques are used; for financial instruments in level 3, the expected credit losses are calcu-lated based on estimated future cash flows at the level of the individual financial instrument. The measurement of the expected credit loss depends in particular on how executive directors' estimates with respect to classification of financial instruments into levels as well as certain parameters such as the loss on default, probability of default and loss ratio at the time of default and – as is the case for financial instruments classified in level 3 – by estimates of the future cash flows, taking into account existing collateral. In addition, valuation-relevant risk factors are taken into account in the context of so-called model overlays, to the extent these are not already covered by the parameters of the models. The calculation of the risk provisions is highly significant for the assets, liabilities and financial performance of the Company and they involve considerable judgment on the part of the executive directors. Es-timating the aforementioned parameters and factoring in future-oriented macroeconomic information have a material influence on the recognition and amount of risk provisions. Against this background, this matter was of particular significance during our audit.

② As part of our audit, we initially assessed the appropriateness of the design of the controls in the Company's relevant internal control systems and tested the controls' effectiveness. In doing so, we considered the business organization, the IT systems and the relevant measurement models. Moreover, we evaluated the measurement of the customer loans, including the appropriateness of estimated values, on the basis of sample testing of loan engagements. For this purpose, we assessed, among other things, the available documentation of the Company with respect to the economic circumstances as well as the recoverability of the related collaterals. For real estate as collateral, we obtained an understanding of and critically assessed the source data, measurement parameters applied and assumptions made on which the expert valuations provided to us by the Company were based and evaluated whether they lay within an acceptable range. With the assistance of our specialists in mathematical finance, we examined the suitability and functioning of the models applied to calculate the risk provisions. In addition, we examined the assumptions and derivation of the applied parameters for classification of the financial instruments and for calculating the expected credit loss. We assessed the appropriateness of the inclusion of additional valuation-relevant risk factors based on the current economic uncertainties. Based on our audit procedures, we were able to satisfy ourselves that overall the assumptions made by the executive directors for the purpose of testing the recoverability of the loan portfolio are appropriate, and that the processes implemented by the Company are appropriate and effective.

③ The Company's disclosures on loan loss provisions are contained in the notes of the financial statements in section 6 "Management estimates and discretionary decisions" and section 7 "Accounting and measurement principles" under 7.I.D) and in sections 15 and 27 "Loan loss provisions". In addition, the management report contains the relevant disclosures in the report on economic performance (results of operations) and the risk report.

❹ Deferred tax assets

① In the consolidated financial statements of the Company deferred tax assets amounting to EUR 713 million after netting are reported. Deferred tax assets amounting to EUR 1,408 million are recognized before netting with matching deferred tax liabilities. The deferred tax assets were recognized to the extent that the executive directors consider it probable that taxable profit will be available in the foreseeable future which will enable the deductible temporary differences and unused tax losses to be utilized. For this purpose, if insufficient deferred tax liabilities are available, future taxable profits are projected on the basis of the adopted business plan. No deferred tax assets were recognized in respect of unused tax losses amounting in total to EUR 5,190 million since it is not probable that they will be utilized for tax purposes by means of offset against taxable profits.

From our point of view, the accounting treatment of deferred taxes was of particular significance in the context of our audit, as it depends to a large extent on the estimates and assumptions made by the executive directors and is therefore subject to uncertainties.

② As part of our audit, we assessed, among other things, the internal processes and controls for recording tax matters as well as the methodology used for the determination, accounting treatment and measurement of deferred taxes. We also assessed the recoverability of the deferred tax assets relating to deductible temporary differences and unused tax losses on the basis of the Company's internal forecasts of its future earnings situation, and the appropriateness of the underlying estimates and assumptions.

Based on our audit procedures, we were able to satisfy ourselves that the estimates and assumptions made by the executive directors are substantiated and sufficiently documented.

③ The Company's disclosures relating to deferred tax assets and liabilities are contained the notes of the financial statements in note 7 "Accounting and measurement principles" and notes 35 "Deferred tax assets".

OTHER INFORMATION

The executive directors are responsible for the other information. The other information comprises the statement on corporate governance pursuant to § 289f HGB and § 315d HGB.

The other information comprises further the remaining parts of the annual report – excluding cross-references to external information – with the exception of the audited consolidated financial statements, the audited management report and our auditor’s report, and the separate non-financial report pursuant to § 289b Abs. 3 HGB and § 315b Abs. 3 HGB.

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

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

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

RESPONSIBILITIES OF THE EXECUTIVE DIRECTORS AND THE SUPERVISORY BOARD FOR THE CONSOLIDATED FINANCIAL STATEMENTS AND THE GROUP MANAGEMENT REPORT

The executive directors are responsible for the preparation of the consolidated financial statements that comply, in all material respects, with IFRSs as adopted by the EU and the additional requirements of German commercial law pursuant to § 315e Abs. 1 HGB, and that the consolidated financial statements, in compliance with these requirements, give a true and fair view of the assets, liabilities, financial position and financial performance of the Group. In addition, the executive directors are responsible for such internal control as they have determined necessary to enable the preparation of consolidated financial statements that are free from material misstatement, whether due to fraud or error.

In preparing the consolidated financial statements, the executive directors are responsible for assessing the Group's ability to continue as a going concern. They also have the responsibility for disclosing, as applicable, matters related to going concern. In addition, they are responsible for financial reporting based on the going concern basis of accounting, unless there is an intention to liquidate the Group or to cease operations, or there is no realistic alternative but to do so.

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

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

AUDITOR'S RESPONSIBILITIES FOR THE AUDIT OF THE CONSOLIDATED FINANCIAL STATEMENTS AND OF THE GROUP MANAGEMENT REPORT

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

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

We exercise professional judgment and maintain professional skepticism throughout the audit. We also:

- Identify and assess the risks of material misstatement of the consolidated financial statements and of the management report, whether due to fraud or error, design and perform audit procedures responsive to those risks, and obtain audit evidence that is sufficient and appropriate to provide a basis for our audit opinions. The risk of not detecting a material misstatement resulting from fraud is higher than for one resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal controls.
- Obtain an understanding of internal control relevant to the audit of the consolidated financial statements and of arrangements and measures (systems) relevant to the audit of the group management report in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an audit opinion on the effectiveness of these systems.
- Evaluate the appropriateness of accounting policies used by the executive directors and the reasonableness of estimates made by the executive directors and related disclosures.
- Conclude on the appropriateness of the executive directors' use of the going concern basis of accounting and, based on the audit evidence obtained, whether a material uncertainty exists related to events or conditions that may cast significant doubt on the Group's ability to continue as a going concern. If we conclude that a material uncertainty exists, we are required to draw attention in the auditor's report to the related disclosures in the consolidated financial statements and in the group management report or, if such disclosures are inadequate, to modify our respective audit opinions. Our conclusions are based on the audit evidence obtained up to the date of our auditor's report. However, future events or conditions may cause

the Group to cease to be able to continue as a going concern.

- Evaluate the overall presentation, structure and content of the consolidated financial state-ments, including the disclosures, and whether the consolidated financial statements present the underlying transactions and events in a manner that the consolidated financial statements give a true and fair view of the assets, liabilities, financial position and financial per-formance of the Group in compliance with IFRSs as adopted by the EU and the additional requirements of German commercial law pursuant to § 315e Abs. 1 HGB.
- Obtain sufficient appropriate audit evidence regarding the financial information of the entities or business activities within the Group to express audit opinions on the consolidated financial statements and on the group management report. We are responsible for the direction, supervision and performance of the group audit. We remain solely responsible for our audit opinions.
- Evaluate the consistency of the group management report with the consolidated financial statements, its conformity with German law, and the view of the Group's position it provides.
- Perform audit procedures on the prospective information presented by the executive directors in the group management report. On the basis of sufficient appropriate audit evidence we evaluate, in particular, the significant assumptions used by the executive directors as a basis for the prospective information, and evaluate the proper derivation of the prospective information from these assumptions. We do not express a separate audit opinion on the prospective information and on the assumptions used as a basis. There is a substantial unavoidable risk that future events will differ materially from the prospective information.

We communicate with those charged with governance regarding, among other matters, the planned scope and timing of the audit and significant audit findings, including any significant deficiencies in internal control that we identify during our audit.
We also provide those charged with governance with a statement that we have complied with the relevant independence requirements, and communicate with them all relationships and other matters that may reasonably be thought to bear on our independence, and where applicable, the related safeguards.
From the matters communicated with those charged with governance, we determine those matters that were of most significance in the audit of the consolidated financial statements of the current period and are therefore the key audit matters. We describe these matters in our auditor's report unless law or regulation precludes public disclosure about the matter.

OTHER LEGAL AND REGULATORY REQUIREMENTS

Further Information pursuant to Article 10 of the EU Audit Regulation

We were elected as group auditor by the annual general meeting on 21 November 2017. We were engaged by the supervisory board on 23 January 2018. We have been the group auditor of the Hamburg Commercial Bank AG, Hamburg/Kiel without interruption since the financial year 2018.

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

GERMAN PUBLIC AUDITOR RESPONSIBLE FOR THE ENGAGEMENT

The German Public Auditor responsible for the engagement is Lothar Schreiber.

Hamburg, 15 March 2019
PricewaterhouseCoopers GmbH
Wirtschaftsprüfungsgesellschaft

Lothar Schreiber	ppa. Tim Brücken
Wirtschaftsprüfer	Wirtschaftsprüfer
(German Public Auditor)	(German Public Auditor)

Responsibility statement by the Management Board

We hereby affirm that to the best of our knowledge the Group financial statements have been prepared in accordance with the applicable accounting principles and give a true and fair view of the net assets, financial position and results of operations of the Hamburg Commercial Bank Group and that the Group management report presents the course of business, including the results of the business and the Hamburg Commercial Bank Group's situation, in such a manner that it gives a true and fair view and describes the main opportunities and risks for the Hamburg Commercial Bank Group's foreseeable performance.

Hamburg/Kiel, 15 March 2019

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Notice

If at times only the masculine form is used for certain terms relating to groups of people, this is not meant in a gender-specific manner, but occurs exclusively for the sake of better readability.

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This is an English translation of the original German version of the Annual Report.

Forward-looking Statements

This Annual Report includes certain forward-looking statements. These statements are based on our beliefs and assumptions as well as on conclusions drawn from information currently available to us from sources which we consider to be reliable. A forward-looking statement involves information that does not simply reflect historical facts, information relating to possible or anticipated future growth and future economic development.

Such forward-looking statements are based on a number of assumptions concerning future events and are subject to uncertainties, risks, and other factors, many of which are beyond our control. Therefore actual events may differ from those forecast in the forward-looking statements. In view of this, you are advised never to rely to an inappropriate degree on forward-looking statements. We cannot accept any liability for the accuracy or completeness of these statements or for the actual realisation of forecasts made in this Annual Report. Furthermore, we are not obliged to update the forward-looking statements following the publication of this information.
In addition, information contained in this Annual Report does not represent any kind of offer for the acquisition or sale of any type of securities of Hamburg Commercial Bank AG.

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