

Management Board  
Aareal Bank AG („Aareal“)  
Paulinenstraße 15  
65189 Wiesbaden

London, 18 February 2022

Dear Mr Klösges, dear Mr Hess,

in preparation of your year-end 2021 results presentation on 24 February 2022, we refer to your press release of 4 February 2022 where you have outlined certain parameters of Aareal's strategy and outlook. Against your announced plan to communicate with shareholders, we, as your largest investor, have not heard from you and have therefore decided to put our thoughts into writing.

By voting down the unattractive under-bid by Advent and Centerbridge your shareholders have made clear they see more value in Aareal than you and the Supervisory Board. As per our press release of 4 February 2022, we believe such value will not be realised by doing more of the same. The 2021 results presentation is a last chance for you to show that you have understood this clear message.

We consequently believe you need to cover and explain the following points on 24 February:

**(1) Strategic Direction of Aareon**

It is without doubt that Aareon needs to embark on an aggressive growth course to exploit its fantastic market opportunity. However, growth and profitability, since Advent's investment in Q4 2020, have been highly unsatisfactory. The much-needed CEO change has taken very long. Many questions remain regarding the ability of Aareal as the majority shareholder to fully develop the potential of Aareon. We thus stick to our view that Aareon's growth strategy is best executed as a stand-alone entity following a spin-off to Aareal shareholders.

Your communication regarding the future ownership structure has been very opaque and misleading. We therefore urgently demand clarification of the following points:

**a) Impact of a Separation on your Deposit Business**

According to Aareal's communication dating back as far as February 2020, Aareon is legally and technologically separated from Aareal's banking operations. Customers who choose to purchase software from Aareon AG (Mainz) and payment processing solutions from Aareal Bank AG (Wiesbaden) need to enter separate contractual agreements. From previous discussions with Aareal's top management, we have understood that after an ownership separation of Aareon AG and Aareal Bank AG, the current business approach could be continued in the form of a long-term joint venture between Aareon and Aareal. In fact, we believe that the collaboration of Aareon and Aareal could be extended from Germany and Austria to cover other jurisdictions where Aareon has strong operations (e.g. Netherlands, France, UK).

→ Please confirm that Aareon AG and Aareal Bank AG are technologically and legally separated.

→ Please confirm that the current approach towards customers and, hence, deposits can be continued in the form of a joint venture – after a separation of ownership.

→ Please explain how an IPO – as communicated by Advent as their planned exit route for their 30% investment<sup>1</sup> – would be structured, especially regarding the deposit business of Aareal Bank AG.

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<sup>1</sup> <https://www.bloomberg.com/news/articles/2022-01-14/aareal-bank-s-2-billion-buyout-threatened-by-hidden-tech-gem>.  
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→ As per your press release from 18 January 2022, the spun-off entity would be subject to statutory secondary liability (Nachhaftung) for five years. You assume – without any fundamental backing – that this will result in a lower sum-of-the-parts valuation than the current setup. Please explain how this statement can be understood in combination with the news reports on Advent considering a future IPO exit for its Aareon stake.

## **b) Advent's Right to Block a Spin-off**

Following our written questions of 17 January 2022 to the Management Board and Supervisory Board of Aareal, Jochen Klösger/Aareal in your press release per 18 January 2022 seem to have suggested that Advent has certain blocking rights regarding a sale or spin-off of the 70% in Aareon owned by Aareal. We note that this is in direct contrast to the clear communication by Aareal's previous CEO Hermann Merkens to investors. We would be surprised by such an agreement, as it raises significant questions both commercially and from a regulatory perspective.

→ Please clarify in detail the situation regarding a separation in ownership of Aareon and Aareal.

→ What has been discussed and/or agreed with Advent with respect to the planned IPO of Aareon?

## **(2) Growing RWAs in Commercial Real Estate Financing**

As we have repeatedly had to point out, Aareal's bank operations have never<sup>2</sup> earned their cost of equity ('CoE'). We deem such CoE to be at least 8-10%. The research community covering Aareal applies an average CoE of c. 10%<sup>3</sup> for the banking operations.

Deploying capital at a return below its CoE destroys value which jeopardises a sustainable future of the bank – shrinking operations and returning capital to shareholders can be worth more than unreasonable growth. To secure a sustainable future for Aareal's banking operations, we have therefore consistently demanded that Aareal improve its cost structure and assess adding RWA-light revenue streams to its core CRE operations.

Based on our value range for Aareon of €1.7 billion to €2.3 billion (100% EV), we calculate an implicit valuation of Aareal's bank operations of 0.05x to 0.21x<sup>4</sup> book value. This means that the capital market is prepared to pay no more than 5% to 21% for every Euro of capital you deploy in the bank operations.

From your press release, we have to assume you want to further grow the asset-heavy CRE lending book.

→ Please explain how you justify deploying more capital to your CRE book while you are not achieving your CoE – even at run-rate guidance – and while you are trading at a massive discount to your book value?

→ Please explain what cost measures have been analysed since Mr Klösger has joined Aareal?

→ Please explain whether Aareal has plans to add commission/fee revenues in the core CRE operations?

Following the failure of the Advent/Centerbridge under-bid and the arrival of a new CEO, the Aareal Group needs to seize the opportunity to 'get it right'. We expect that you answer our questions to our satisfaction on 24 February.

Sincerely,



Klaus Umek  
Managing Partner



Till Hufnagel  
Partner

<sup>2</sup> At least for the time series that Aareal publishes financial information on its website. ROEs excluding one-off items such as negative goodwill from acquisitions.

<sup>3</sup> Includes Kepler, Baader and Warburg Research. CoE ranges from 8.1% to 11.9%.

<sup>4</sup> Factset as per 17-Feb-2021.