ANNUAL REPORT
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L-BANK
Staatsbank für Baden-Württemberg

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GREETINGS FROM THE CHAIRMAN OF THE BOARD

Dear Business Associates,

A change of perspective can sometimes be beneficial. A critical view from the outside can help identify one's weaknesses – and can also shed new light on one's strengths. This was how things went for us last year, when the French political and business press launched a discussion of the paradigmatic value of "le Mittelstand allemand" – German SMEs. Here in Baden-Württemberg, we are of course very aware of the fact that the ongoing development of our state depends on our small and medium-sized enterprises. We are proud of the sheer inventiveness of our businesses, of our "hidden champions", and of our twin-track education and training system. In the course of the discussion, the French analysis focused in particular on Germany's underlying financial system and the various products available to SMEs. L-Bank was among the institutions quizzed by representatives of Fonds Stratégique d'Investissement (FSI), who wanted to know more about our development programmes and products. FSI's conclusion: public-sector finance makes a material contribution to the success of the Mittelstand in Baden-Württemberg. The regional principle, whereby local commercial banks work closely together with the relevant state development bank, plays a key role in creating the financial flexibility necessary for developing businesses. The specialist agencies that work at national and regional level are seen as stabilising factors from which Germany's economy benefits in times of crisis. Both France and the UK are currently endeavouring to apply insights from the German model to their own existing structures.

At present, the main task facing German development banks is to secure and further extend this successful principle. Like all banks, our institutions are affected by EU regulations. Looking ahead to Basle III, I can say that L-Bank's preparations are making good headway in the right direction. This applies to all the requisite elements – weighted capital, leverage ratio and liquidity provisioning. Liquidity reserves were raised in light of supervisory requirements in 2012 and are to be increased further.

The important goal of regulation is to make banks and financial markets more stable and crisis-proof. Nevertheless, the question arises as to whether these requirements will allow development banks to perform their duties in future in quite the way their public-sector masters intend. This will only be possible if due allowance is made for the differences between development finance institutions and commercial banks in the course of devising appropriate capital adequacy rules and banking supervision. After all, development banks represent no systemic risk whatsoever, and are unable – because of their state guarantees – to go into liquidation. Above all, they must be in a position to fulfil their public-service mandates, and not just during crises; they are indispensable instruments for use by federal and state governments in supporting structural change.

The green-energy revolution is the best example of this. Idealism can stimulate social change, but without high levels of investment, the ambitious goals of the Federal Republic of Germany and the State of Baden-Württemberg cannot be achieved. It must be possible to finance the necessary initiatives – and this is precisely where development banks provide the underlying impetus required to put these far-reaching changes into effect. The finance packages we offer are generating widespread interest; the very high level of demand for these products clearly shows that our low-interest loans are a suitable vehicle for driving the green-energy revolution forward.

This is just one of the building blocks we are using to support the federal state's sustainable economic, social and environmental development. Our commitment is reflected in our sustainability management system, now firmly established as an integral part of our own institution. In the final analysis, it is all about behaving reliably and responsibly at all levels – within the Bank, in our dealings with the state, and in our collaboration with investors worldwide.

Christian Brand

Christian Brand
Chairman of the Board of Management of L-Bank

MANAGEMENT REPORT – REPORT OF THE BOARD OF MANAGEMENT OF L-BANK FOR FISCAL YEAR 2012

As the State Bank of Baden-Württemberg, L-Bank helps the federal state government to fulfil its economic, structural and social policies. It employs a broad range of financial instruments for this purpose. As a public-law institution with its head office in Karlsruhe and a branch office in Stuttgart, L-Bank is subject to the supervision of the federal state government.

MACROECONOMIC ENVIRONMENT

In fiscal year 2012, the macroeconomic situation continued to be dominated by the sovereign debt crisis and the associated loss of confidence across Europe. During the first six months, the German economy was characterised by mild growth, but this slackened off over the second half of the year. Over the year as a whole, Federal Statistical Office figures indicated that Germany's gross domestic product (GDP) grew by just 0.7% compared to the previous year (as at 15 January 2013). Growing problems in the countries most affected by the eurozone crisis impacted the confidence of German firms, and this was clearly reflected in lower levels of investment. Exports within the eurozone also fell sharply, but fortunately this was offset by an increase in the volume of exports to countries outside Europe, thanks to the weakened euro. In spite of this difficult environment, employment in Germany proved to be remarkably resilient, reaching a new peak of nearly 41.6 million people during the fiscal year; the average unemployment rate over the year as a whole was 6.8% (Federal Statistical Office, as at 15 January 2013), the lowest level since the mid-1990s.

Over 2012, Baden-Württemberg's economy grew faster than the German economy as a whole, with GDP up by 1.25% (Statistical Office of Baden-Württemberg, as at December 2012). This is primarily due to the fact that economic activity in the federal state remained more robust during the second half of the year than in the country as a whole. While private consumption benefited from the positive labour market trend, Baden-Württemberg's industrial products were hampered by weak domestic demand. This was offset by continuing strong demand for capital goods in the emerging economies, which in Baden-Württemberg's case helped to compensate for declining demand in other European countries. During the first three quarters of 2012, figures provided by the Statistical Office of Baden-Württemberg indicate that exports rose by 5% (as at December 2012).

KEY DEVELOPMENTS AT L-BANK

In 2012, the volume of L-Bank's new business rose by 47.0% to EUR 12,769.5 million* (2011: EUR 8,683.8 million, with significant increases in the business development and housing sectors in particular. Development funding in both sectors focused primarily on measures to improve energy efficiency in residential and commercial buildings,

* Figures and data for new business development (including comparative figures for the previous year) were collected using a new system, which is why not all of them are directly comparable with the figures appearing in last year's management report.

as well as small and medium-sized enterprises. There was also a marked increase in funding for infrastructural projects.

BUSINESS DEVELOPMENT

In order to stimulate sustainable growth in Baden-Württemberg's economy, thereby safeguarding jobs in the federal state over the long term, L-Bank works in close partnership with commercial banks to support business start-ups, small and medium-sized enterprises (SMEs) and agricultural businesses. To do so, the Bank issues low-interest loans and grants, and assumes certain specific kinds of risk. In 2012, the volume of new business in the business development sector came to EUR 3,057.6 million, exceeding the already high level of business in the previous year (EUR 2,555.7 million) by 19.6%. Over the last fiscal year, the Bank focused on the implementation of energy-saving schemes and initiatives in SMEs.

The Bank issued loans totalling EUR 395.4 million to business start-ups and fledgling companies (2011: EUR 407.6 million). The volume of funding approved for the Bank's “Start-up Finance” programme – the programme with the highest volume – came to EUR 341.6 million (2011: EUR 361.7 million). The slight decline in the volume of approvals is due to restrictions on applicant eligibility introduced in 2011 and associated anticipatory effects.

L-Bank supported established companies during fiscal year 2012 with a total volume of EUR 2,273.5 million (2011: EUR 1,841.1 million) in funding. Accompanied by extensive marketing activities, the Bank worked closely with State of Baden-Württemberg to launch the “Energieeffizienzfinanzierung – Mittelstand” (Energy Efficiency for SMEs) programme on 1 April 2012. As part of this programme, small and medium-sized businesses seeking to improve the energy efficiency of their business premises and equipment are provided with heavily interest-subsidised loans. This development campaign is part of L-Bank's efforts to drive forward the green-energy revolution in Baden-Württemberg. The volume of funding approved for the programme amounted to EUR 323.6 million. The two other programmes to show positive development were the Bank's “Growth Finance” and “Liquidity Facility” programmes, due to attractive lending conditions and strong investment activity on the part of the target market segments. The Growth Finance programme, which specialises in long-term lending on favourable terms, provided funding for investment projects totalling EUR 879.1 million (2011: EUR 765.8 million). The volume of funding under the Liquidity Facility programme, which provides low-interest loans on short and medium-term maturities, rose by 38.4% to EUR 241.5 million (2011: EUR 174.5 million). In addition, businesses investing in rural projects in the year under review were provided with low-interest loans totalling EUR 317.4 million (2011: 286.6 million) through the “Investment Finance” programme.

Alongside the Bank's traditional lending business, L-Bank also supports – on a competitively neutral basis – large-scale investment projects by companies registered or based in Baden-Württemberg. However, in fiscal year 2012 the volume of approved loans to clients in this market segment declined to EUR 87.0 million (2011: EUR 138.5 million), due to the general downturn in the syndicated loan market.

The Bank's guarantee programme – whereby L-Bank assumes risk on behalf of commercial banks involved in financing larger corporate borrowings or projects – also experienced a slight decline. Over the year under review the volume of new business fell to EUR 41.2 million (2011: EUR 45.9 million).

In the agricultural sector, new development finance figures came in slightly above the preceding year at EUR 182.3 million (2011: EUR 147.9 million). The “Agricultural Growth” programme, which aims to improve production conditions in agriculture, benefited from changes in legal and associated capital expenditure requirements; the resultant 75.1% increase – representing a funding volume of EUR 84.8 million (2011: EUR 48.4 million) – made a significant contribution to the increased volume of new business. Only in our "New Energy – Energy from the Countryside" programme did the volume of approvals decline to EUR 59.0 million (2011: EUR 90.6 million), because new investment in photovoltaic and biogas installations in Baden-Württemberg fell as a consequence of reduced feed-in tariffs.

HOUSING DEVELOPMENT

L-Bank uses low-interest loans and grants to create incentives for the construction, acquisition and renovation of residential property for rental or owner occupation. The Bank's newly introduced energy-efficiency funding schemes for residential housing, launched on 1 April 2012 in support of the green-energy revolution, generated a significant increase in new business figures in the housing assistance sector. The volume of approved funding rose to EUR 1,476.1 million, representing a 61.2% increase over the previous year (2011: EUR 915.8 million).

In terms of financial assistance for home ownership, the Bank approved loans and grants totalling EUR 1,232.2 million (2011: EUR 676.3 million), representing an increase of 82.2%. Of this volume, EUR 166.1 million (2011: EUR 222.1 million) were awarded under the aegis of the state housing assistance programme. The main factors responsible for the fall in demand were low capital-market interest rates and more rigorous application requirements imposed by higher energy standards. Very much in demand, however, were our new energy-efficiency finance programmes, which reached a volume of EUR 611.6 million. Of this amount, loans totalling EUR 318.3 million were issued under our "Energy Efficiency Finance – Construction" programme, which supports the building and acquisition of energy-saving housing and condominiums. Our "Energy Efficiency Finance – Renovation" programme provided a total of EUR 293.3 million in financial assistance for property renovation and refurbishment. This programme variant funds individual schemes for making significant energy savings, as well as housing conversions that aim to meet the "Effizienzhaus" (Efficient House) quality standard. Because it can be combined with our energy-efficiency programmes, the Bank's existing "Living the Future: Renewable Energy" programme – which supports installations of heating systems based on renewable energy sources – doubled in volume over the previous year, rising to EUR 85.7 million (2011: EUR 39.3 million). The Bank also assisted families to purchase or build their own homes through the "Living with Children" programme. However, despite an increase in the number of cases processed, lower funding ceilings meant that the programme volume fell to EUR 284.7 million (2011: EUR 332.9 million).

In addition to financial assistance for home ownership, L-Bank also provides support for the construction and modernisation of rental accommodation in Baden-Württemberg, issuing funds totalling EUR 237.9 million (2011: EUR 239.6 million) for this purpose. The volume of funding approved under the state housing assistance programme remained much the same as in the previous year, at EUR 15.7 million (EUR 15.9 million). The expected increase in volume was not achieved – primarily due to low capital-market interest rates and the terms and conditions associated with the funding. The Bank's own financial assistance programme for rental accommodation continued to be successful, achieving similar levels to the preceding year at EUR 34.3 million (2011: EUR 36.0 million).

Since the start of fiscal year 2012, apartment owners' associations also have the option of applying to L-Bank for subsidised loans to finance the conversion or modernisation of residential buildings for greater energy efficiency or accessibility. This makes L-Bank one of the few development banks in Germany to provide apartment owners' associations with access to lending products. Because owners' associations are often heterogeneous, the application process generally requires longer lead times compared to applications by individuals. Hence the volume of approvals was still low, at just EUR 5.9 million.

REFINANCING AND BANK MANAGEMENT

As the State Bank of Baden-Württemberg, L-Bank is able to call on the federal state's maintenance and public (statutory) guarantee obligation, as well as an explicit state guarantee. The latter means L-Bank enjoys a de facto identical credit rating to the State of Baden-Württemberg. Credit rating agencies Moody's Investors Service and Standard & Poor's consequently continue to bestow their top ratings on L-Bank (Aaa and AAA, respectively).

By taking a selective approach to utilisation of the refinancing alternatives on offer, L-Bank was once again able to meet its objectives for funding volumes, maturity profiles and structure over the year under review. In strategic terms, both medium and long-term refinancing focused on maturities ranging from two to five years. The central instrument here is the Bank's Debt Issuance Programme, with a funding limit of EUR 30.0 billion, of which EUR 20,524.2 million were utilised as at 31 December 2012 (2011: EUR 19,012.8 million). L-Bank issued two five-year benchmark bonds in the year under review: one EUR 1.0 billion bond and one USD 1.0 billion bond. In addition, the Bank issued private placements in various currencies, denominated primarily in US dollars, British pounds sterling and Japanese yen. In 2012, the total volume of medium and long-term refinancing through borrowings on the capital markets came to EUR 9,405.3 million (2011: EUR 9,997.0 million). As at year end, utilisation of the Commercial Paper Programme, which has an upper funding limit of EUR 15.0 billion (2011: EUR 10.0 billion) and is used for short-term refinancing, amounted to EUR 9,179.7 million (2011: EUR 9,372.0 million).

In terms of asset and liability management, L-Bank continued to pursue a conservative investment strategy, focused rigorously on debtor grades with credit ratings ranging from good to very good. The portfolio consists mainly of securities with AAA and AA ratings. The Bank did not do any new securitisation business over the past fiscal year.

OTHER DEVELOPMENTS

In order to maintain the efficiency of Baden-Württemberg's infrastructure as a major economic asset, L-Bank distributed funds totalling EUR 2,404.6 million in the year under review (2011: EUR 1,798.9 million), largely in the form of loans and guarantees. As financial partner to the State of Baden-Württemberg, the Bank made funds totalling EUR 1,749.9 million (2011: EUR 821.0 million) available for state-run projects. Baden-Württemberg's municipalities are in good financial standing and consequently have very limited need for external financing, which resulted in a significant decrease in the volume of funding approved under the "Investment Lending Direct – Local Authorities" programme, which provides low-interest loans in support of municipal infrastructure projects; in the year under review, demand fell to just EUR 88.1 million (2011: EUR 204.2 million).

As a service provider, L-Bank performs a wide variety of duties connected with the provision of financial aid on behalf of the State of Baden-Württemberg. During the year under review, the Bank processed approved funds totalling EUR 908.5 million (2011: EUR 941.6 million) in support of various financial aid schemes. The bulk of the funding came out of the federal state budget (EUR 793.0 million; 2011: EUR 833.0 million) and EU budget (EUR 81.8 million; 2011: EUR 69.0 million). Despite the discontinuation of a one-off funding increase in 2011, the largest item, at EUR 357.0 million (2011: EUR 436.9 million), remained finance for hospitals. Other significant items comprised school construction projects – including full-day schools – at

EUR 102.0 million (2011: EUR 89.0 million) and projects involving water, sewage, flood protection and contaminated sites, at EUR 99.0 million (2011: EUR 117.1 million). Pre-school language learning was redesigned as planned; in addition, as part of our Climate Change Plus contract with the Ministry of the Environment, Climate and Energy, we issued funding under our new "Climate-neutral Municipalities" programme.

To provide financial support to families with children, L-Bank distributes federal family allowances and state educational allowances on behalf of the German federal and state governments. The total volume of approvals rose slightly during the year under review. The total volume of federal family allowances came to EUR 688.1 million (2011: EUR 676.0 million), and the Bank approved EUR 33.2 million (2011: EUR 36.9 million) in state educational allowances. Following a resolution by the state government, the awarding of state educational allowances was discontinued for births and adoptions from 1 October 2012 onwards. Due to the preceding uptake of family allowances, however, the effects were not noticeable in the year under review. With the abolition of tuition fees as from summer semester 2012, the student loan programme was also discontinued.

As at the balance-sheet date, L-Bank's shareholdings in companies had a total book value of EUR 524.7 million (2011: EUR 509.6 million). The portfolio includes strategic and credit-equivalent interests in companies based in Baden-Württemberg, as well as shares in subsidiaries involved in Baden-Württemberg's regional development.

As at year-end 2012, the book value of the strategic investments held by L-Bank on behalf of the federal state amounted to EUR 457.1 million (2011: EUR 443.2 million). The change compared to the previous year is primarily the result of a capital reserve increase at one of the portfolio companies.

Through L-EA Mittelstandsfonds, which has aggregate capital commitments of EUR 500.0 million, L-Bank either takes an interest – generally speaking as a co-investor – in well-established SMEs based in Baden-Württemberg, or supports them with tailor-made mezzanine financing instruments. The strong demand for L-EA Mittelstandsfonds products continues unabated. During 2012, the Bank entered into three new commitments and continued to fund seven existing investments. The volume of investment – including subordinated loans – came to a total of EUR 56.7 million (2011: EUR 12.7 million). As at the balance-sheet date, the portfolio comprised a total of 22 commitments (investments in three funds, ten individual holdings, nine subordinated loans), currently representing a total investment volume of EUR 158.4 million (2011: EUR 119.6 million).

The technology and business parks operated by L-Bank's subsidiaries in Karlsruhe, Reutlingen, Stuttgart and Tübingen help to make these towns and cities, already well known for their universities and research facilities, even more attractive. Some 313 companies with a total of 8,530 employees have already established themselves in the parks. After divestments, of the total original investment of EUR 469.0 million (2011: EUR 466.4 million) some EUR 163.0 million (2011: EUR 158.2 million) were still invested as at the balance-sheet date.

BALANCE SHEET TOTAL AND OPERATING RESULT

During the year under review, L-Bank's balance-sheet total rose by 3.9% to EUR 70,629.8 million (2011: EUR 67,991.9 million). The increase is reflected primarily in receivables from customers, which rose by EUR 1,502.0 million or 6.6%, as well as investments in securities, which rose by EUR 2,042.5 million or 9.6%. Receivables from banks, on the other hand, showed a slight decline. On the liabilities side, the rise in the balance-sheet total resulted primarily from refinancing at banks and increased utilisation of the Bank's Debt Issuance Programme.

By comparison, the volume of business that also includes guarantee obligations and irrevocable loan commitments increased by just 1.9% to EUR 79,647.2 million (2011: EUR 78,161.7 million), due to low contingent liabilities at the balance-sheet date.

Ordinary income – comprising net interest income, net commission income and other operating income – rose by 3.6% to EUR 494.2 million (2011: EUR 477.0 million). Net interest income is still the key element in the Bank's income and increased by EUR 17.0 million or 4.0% in the year under review. Interest subsidies paid out by L-Bank, valued under commercial law as interest expenses, are treated in the summary of operational income below as a service to the State of Baden-Württemberg, hence – in accounting terms – as an appropriation of profits.

Administrative expenses, which include personnel expenses, general expenses and depreciation on tangible assets, rose by 5.2% over the previous year to EUR 143.5 million (2011: EUR 136.4 million). Personnel expenses actually declined, mainly due to special items in the preceding year, so the main reason for this year's increase was a rise in general expenses relating to our banking business, associated primarily with the ongoing development of our IT systems and renovation of one of our bank buildings. Other operating expenses also increased.

At EUR 341.2 million, the operating result before valuation adjustments was slightly higher than in the preceding year (EUR 335.0 million). Income from asset revaluation remained positive at EUR 8.5 million. While this represents a sharp decline compared to the previous year's EUR 411.7 million, the very high figure for 2011 was largely the result of a reversal of contingency reserves totalling EUR 352.7 million. Taking these valuation adjustments into account, the Bank's distributable income is calculated at EUR 302.9 million (2011: EUR 750.7 million).

APPROPRIATION OF PROFITS

Out of the Bank's profit for the year, the State of Baden-Württemberg received a total of EUR 155.5 million (2011: EUR 109.7 million). Of this, EUR 140.2 million (2011: EUR 94.4 million) was spent on interest subsidies and grants. The Bank's contribution to Baden-Württemberg's road construction programme remained unchanged at EUR 15.3 million. Out of net income totalling EUR 148.3 million, an amount of EUR 148.0 million was transferred to other retained earnings in order to increase the Bank's Tier I (core) capital ratio, and the remaining amount of EUR 0.3 million was carried forward.

SUMMARY OF INCOME FROM AN OPERATIONAL PERSPECTIVE in EUR million

	01.01.2012 to 31.12.2012	01.01.2011 to 31.12.2011	Change	Change in %
Net interest income	437.8	420.8	17.0	4.0
Net commission income	39.1	42.2	–3.1	–7.3
Net result from other income/expenses	7.8	8.4	–0.6	–7.1
Administrative expenses	143.5	136.4	7.1	5.2
Operating result before risk provisions/ valuations	341.2	335.0	6.2	1.9
Income from asset revaluation	8.5	411.7	–403.2	–97.9
Addition to fund for general banking risks	46.0	0.0	46.0	–
Operating income after risk provisions/ valuations	303.7	746.7	–443.0	–59.3
Extraordinary operating result	0.0	4.9	–4.9	–100.0
Net income before taxes	303.7	751.6	–447.9	–59.6
Taxes on income	0.8	0.9	–0.1	–11.1
Distributable income	302.9	750.7	–447.8	–59.7
Expenses for interest subsidies and other subsidies	140.2	94.4	45.8	48.5
Contribution to road construction programme	15.3	15.3	0.0	0.0
Net income	147.4	641.0	–493.6	–77.0

RISK REPORT

To manage risks associated with L-Bank's business activities, the Bank has installed a risk management system with the aim of enabling the Bank to:

- assess the Bank's overall risk exposure at any time,
- immediately identify, value, communicate and control individual risks
- identify risk-related developments combined with possible courses of action.

The Bank's risk management concept is based on the premise that in the event of unexpected losses, the Bank's survival should be sustainably assured even without the support of the State of Baden-Württemberg (going-concern approach). It is based primarily on:

- application of a coherent business strategy and resulting risk strategy,
- constant monitoring of the Bank's risk-bearing capacity,
- full documentation in writing of the Bank's corporate structure and all business processes involving risks,
- creating and continuously updating risk management and risk control processes, and
- ongoing process-dependent as well as process-independent monitoring of all the Bank's processes.

HOW RISK MANAGEMENT IS ORGANISED

The design of the risk management system is specific to the Bank and is largely determined by its statutory development mandate. By setting up development programmes, targeting specific market segments for financial support, and determining the regional focus, the State of Baden-Württemberg effectively defines the Bank's business activities. In return, the State of Baden-Württemberg explicitly guarantees the Bank's liabilities through a public (statutory) guarantee and maintenance obligation.

On the basis of the Bank's public development mandate, the business strategy produced by the Board of Management formulates the key principles underpinning the Bank's business activities, which are set down in detail in the Bank's risk strategy – with particular attention to the Bank's risk-bearing capacity – and defined operationally in the Bank's procedures and workflows.

On this basis, the Treasury department is responsible for implementing the interest rate and currency risk profiles defined by the Board of Management, and for managing liquidity risk. The Bank's individual lending departments manage counterparty default risk through a system of competencies and limits. Operational risks are managed by "risk managers". The latter are divided into central risk managers, who manage operational risks affecting the entire Bank, and decentralised risk managers, who manage the risks associated with specific working procedures. Whereas central risk managers are appointed by senior management, the role of decentralised risk manager is generally fulfilled by the heads of the individual departments, who may also delegate specific tasks to departmental staff as part of their organisational remit.

The Controlling department, working together with the risk managers, is responsible for the quantitative and qualitative assessment and communication of risks. The Controlling department is also responsible for monitoring compliance with all risk management policies, and for reporting on the risk situation to the Board of Management.

The Credit Analysis department assesses the credit standing of individual borrowers and specific portfolios, and proposes appropriate individual lending limits to the Board of Management, as well as lending limits for portfolios and countries. The Credit Analysis department also casts the back-office vote on business decisions involving risk. In order to assess risk exposure in qualitative terms, the stress committee carries out regular stress analyses. Risk concentrations are a particular focus of concern.

Taking a risk-focused, process-independent approach, the Audit department reviews and assesses the effectiveness and adequacy of the Bank's risk management system, as well as the orderly conduct of all L-Bank's key activities and processes, on behalf of the Board of Management. This department is directly accountable and reports to the Board of Management as a whole. The Audit department carries out its duties independently and impartially, and is not required to accept instructions regarding the evaluation or reporting of audit results.

BUSINESS STRATEGY AND RISK STRATEGY

In the Bank's business strategy, the Board of Management sets targets for Tier I capital and cost-income ratios, and decides which products should be used to meet the Bank's public-service mandate through development programmes and other development business. The Board of Management uses the development business matrix to allocate selected products to the Bank's respective business activities. The Bank's statutory public-service mandate results in concentrations of default risk (cluster risks) in particular industries, types of collateral, and regions. In order to achieve a balanced aggregate risk profile, the Board of Management sets down in the Bank's business strategy quality requirements for the portfolio structure as a whole. These include policies that define the credit rating criteria (risk categories) for new business that must be satisfied by borrowers who are not involved in the Bank's development programmes.

The Bank's risk strategy is derived from the business strategy. In the risk strategy, the Board of Management specifies the procedures that should be used to audit the Bank's risk-bearing capacity, lays down policies for new products and markets, and defines the strategies for dealing with counterparty default risk, market price risk, liquidity risk and operational risks.

As part of a quantitative assessment of the Bank's risk-bearing capacity, the Board of Management uses the risk strategy to define risk tolerance limits by specifying the scope of risk coverage capital that should be set aside as cover for losses. This process identifies the extent to which counterparty default risk, market price risk, liquidity risk, operational risk and general business risk constitute types of material risk. The quantitative assessment of the Bank's risk-bearing capacity is supplemented by stress analyses, with a particular emphasis on risk tolerances.

With respect to managing credit risk, the risk strategy includes policies specifying borrowers' minimum credit ratings and credit risk margins, and obliges business units to take on collateral that is deemed to be recoverable. In addition, the Board of Management budgets and imposes ceilings for aggregate lending by each business unit over the next three years. Budgets for development programmes are based on the amount of subsidy funding that has been made available in each case. Budgets for other development business carried out in collaboration with commercial banks are based primarily on levels of demand from the commercial banks. Lending business associated with liquidity management is primarily determined by the refinancing options available. Any investments made for this purpose must meet exceptionally high standards of creditworthiness. Taking risk-bearing capacity into account, the risk strategy accordingly shows – after making due allowance for existing risk concentrations – the projected scope of future counterparty default risks.

With respect to market price risks, the Bank pursues a strategy of following its view of interest rate developments to generate predictable levels of income with acceptable levels of risk. The underlying view of interest rate developments is derived from capital market parameters. Due to the current volatility, these transactions are intensively monitored on a daily basis, with ongoing reviews by senior management on – as a minimum – a weekly basis.

In order to obtain refinancing on favourable structural and cost conditions, the Bank has recourse to the national and international capital markets. The public guarantee and maintenance obligation provided by the State of Baden-Württemberg means that the Bank benefits from the latter's excellent credit standing on the capital markets. Potential liquidity risks due solely to a substantial downgrade of the federal state's credit rating are classified as negligible over the long term.

The Bank controls operational risks by applying the principle of profitability. This means that regardless of the existing comprehensive internal control procedures, and regardless of statutory or regulatory requirements, the Bank only takes special mitigation or avoidance measures if the potential loss exceeds the costs of taking such measures.

RISK-BEARING CAPACITY

Monitoring risk coverage capability via dual control mechanisms

The aim of monitoring the Bank's risk-bearing capacity is to safeguard the Bank's continuing existence over the long term without relying on external support by the guarantor (going-concern approach). In parallel, the Bank uses a second control mechanism to calculate its risk-bearing capacity based on the "liquidation approach".

Going-concern approach

Calculations of the relevant economic risk coverage capability are based on profit and loss projections. Initially, only equity that is not required to satisfy the capital adequacy requirements of the German Solvency Regulation (SolvV) is taken into account. For reasons of prudence, the Bank uses a higher overall ratio of 8.4% to calculate the amount of capital required for regulatory compliance. The Bank then supplements the resulting disposable equity components with any reserves that, in terms of their loss-compensation function, are comparable in quality to the available equity capital and – when calculating the Bank's risk exposure as defined by regulatory requirements – are not considered as risk-reducing factors. In addition, "write-up reserves" that stem from the fall in value of interest-subsidised loans and pre-date BilMoG are also taken into account. Anticipated losses are already covered by the Bank's compliance with regulatory capital adequacy requirements: any remaining economic risk coverage capital is used to offset unanticipated losses.

Value-at-risk limits are specified for all material types of risk, based on a uniform confidence level of 99.0%; these are offset against the Bank's risk coverage capability. The sum total of these value-at-risk limits represents the aggregate loss ceiling as defined by the Bank, which, in view of the requirement to secure the Bank's long-term survival, may not exceed more than 80.0% of the Bank's risk coverage capital. These limits are monitored on an ongoing basis, which also helps to safeguard the Bank's risk-bearing capacity.

The following table illustrates the development of the respective risk coverage capabilities as well as the specific risks to which they pertain. "Risk exposure" includes the capital charges for counterparty risks and the sum of capital charges for market price risks and operational risks (both multiplied by a factor of 12.5). The Bank calculates credit risk using the standardised approach to credit risk, market price risks using the standard method, and operational risks using the basic indicator approach.

REGULATORY CAPITAL ADEQUACY REQUIREMENTS

Regulatory capital ratios	31.03.2012	30.06.2012	30.09.2012	31.12.2012
Risk exposure in EUR millions	19,206.1	19,249.6	19,384.3	18,376.8
Tier I capital in EUR millions	1,937.1	2,607.8	2,601.1	2,662.4
Tier I capital requirement in EUR millions	875.1	901.8	901.1	866.1
Disposable Tier I capital in EUR millions	1,062.0	1,706.0	1,700.0	1,734.0
Equity in EUR millions	3,119.8	3,675.2	3,541.0	3,504.2
Tier I capital ratio in %	10.1	13.6	13.4	14.2
Total capital ratio in %	16.2	19.1	18.3	19.1

As at the balance-sheet date, with disposable Tier I capital amounting to EUR 1,734.0 million, a profit for the preceding year of EUR 244.2 million (before additions to reserves pursuant to Art. 340f, g HGB), and eligible reserves totalling around EUR 83.2 million, the Bank's P&L-based risk coverage capability amounted to EUR 2,061.5 million. This risk coverage capability is counterbalanced by the aggregate loss ceiling of EUR 1,395.0 million, as specified by the Board of Management in line with the Bank's business and risk strategies. As at the balance-sheet date, this limit was distributed as follows:

AGGREGATE LOSS CEILING AND INDIVIDUAL LOSS CEILINGS AS AT 31.12.2012 in EUR millions

	Limit
Aggregate loss ceiling	1,395.0
Counterparty default risks	705.0
Market price risks	240.0
Liquidity risks	65.0
Operational risks	20.0
Real property risks	20.0
Modelling risk	70.5
Immaterial business transactions	7.0
PIIGS buffer	100.0
Modelling/market data buffer	150.0
Buffer	17.5
Proportion of risk coverage capital taken up by aggregate loss ceiling	67.7 %

Thus the aggregate loss ceiling accounted for 67.7% of the Bank's economic risk coverage capability as at the balance-sheet date. Over the past fiscal year, this proportion has varied between 52.4% and 72.3%.

Liquidation approach

In the second control mechanism, the value of the Bank as a whole is used as economic risk coverage capability. This is counterbalanced by the aggregate loss ceiling, but also by hidden liabilities in fixed assets resulting from the avoidance of lower of cost or market write-downs and negative market values, as well as spread risks. In agreement with the Supervisory Board, the Board of Management has resolved to adjust the risk structure such that the total amount of the aggregate loss ceiling, hidden liabilities and spread risks should not exceed 80.0% of the Bank's economic risk coverage capability (calculated by value). To assess changes in hidden liabilities and negative market values, the Bank continuously subjects them to a variety of stress tests.

As at the balance-sheet date, the business portfolio's net present value is calculated as EUR 5,118.3 million. This is offset – taking business risk into account – by imputed personnel and general expenses totalling EUR 854.7 million, plus imputed risk provisioning costs of EUR 630.1 million, resulting in a value-based risk coverage capability of EUR 3,633.4 million. In turn, 65.0% of this is taken up by a combination of the aggregate loss ceiling of EUR 1,395.0 million, plus hidden liabilities and migration and spread risks totalling EUR 967.8 million. Utilisation of the value-based aggregate loss ceiling rose over the past fiscal year from 35.9% to 65.0%. One of the reasons for this is the Q2 decision to increase the aggregate loss ceiling from EUR 995.0 million to EUR 1,395.0 million. This increase was not intended to extend the Bank's exposure, but to cover rising risk ratios due to model-driven adjustments of market price risks. In addition, buffers were set up to cover possible downgrades in the credit ratings of Portugal, Italy, Ireland, Greece and Spain (the PIIGS nations), and for another model-driven increase in reportable risks. Uptake was further increased by taking business risks and spread risks – in the form of both individual migration risks and market-wide spread risks – into consideration. The liquidation approach takes account of business risks due to increased administrative expenses. Migration risk is assessed with the help of a Monte Carlo simulation, based on the risk of a decline in the value of securities due to issuers' deteriorating credit ratings. Market-wide spread risk is assessed with the help of historical simulations, based on the risk of a rating-independent decline in the value of securities due to market-wide spread movements.

Preparing for Basle III

Regardless of the precise timing of the implementation of Basle III reforms, there is likely to be an increase in the capital required to cover bank business activities over the next few years. Consequently, the Bank has generated medium-term simulations based on its current and anticipated risk exposure, using regulatory drafts that have already been published and, where necessary, approximations of open questions of interpretation. Based on these preliminary calculations, the Bank can affirm that its risk-bearing capacity meets the criteria of both control mechanism 1 (going-concern approach) and control mechanism 2 (liquidation approach).

Performing stress analyses

Value-at-risk models are used to carry out quantitative risk measurements. By their nature, the actuarial models used for risk measurement assume, when setting various influencing parameters, a degree of stability in financial market conditions. But the ongoing financial crisis, which has now lasted for several years, has revealed obvious limits to the predictive powers of quantitative risk models in various key areas. To minimise the risk of model-driven misjudgements of the Bank's risk exposure, all quantitative risk assessments are continuously rounded out by comprehensive analyses in the form of stress scenarios. By performing stress-scenario analyses, the Bank identifies clusters of risk factors that may have a major impact on the Bank's assets, liabilities, financial position and profit or loss.

In these analyses, the Bank starts by developing and analysing scenarios that, in terms of their effects, have an isolated impact on a single type of risk (e.g. counterparty default risk, market price risk, liquidity risk, operational risk). In a second stage, the key risk factors for each individual risk type are defined as actual risk carriers (e.g. unemployment as a factor in counterparty default risk), and the Bank then investigates how they interact with risk factors affecting other types of risk. At this stage of the process, the analysis is based on, inter alia, the Bank's in-house expertise combined with a scoring method. By identifying the interactions between risk factors, the Bank gains an insight into risk concentrations both within individual risk types and across all risk types. This enables the Bank to formulate stress scenarios that match the interactions between risk factors.

The analytical system described above does not entirely preclude the possibility that certain scenarios threatening the Bank's existence may never be identified. So in order to clarify the limits of the Bank's risk-bearing capacity, the Bank makes certain assumptions regarding charges arising from losses, and retroactively determines the conditions under which such losses might arise (using inverse stress tests).

Currently, identifying the quantitative impact of the formulated scenarios is dependent on expert estimates from which quantitative data are derived. These estimates – hence also their quantitative implications – are of course subject to heightened uncertainty. For this reason, the Bank is currently developing a multidimensional scoring system by means of which the quantitative, one-dimensional expert estimate can be further developed into a qualitative, multidimensional analysis. The latter can then be combined with time-series analyses of observable risk factors. The Bank takes the view that this approach will allow in-house expertise to be used more comprehensively for quantitative analysis than is possible with the method currently in use.

For default risks, the applied scenarios result in increasing credit risks and consequently in a greater need for regulatory and economic capital. With an eye to Baden-Württemberg's economic structure, one of the scenarios is predicated on a severe cyclical downturn in the automotive industry. With respect to market price risk, various extraordinary changes in yield curves are modelled on the basis of interest rate curves over the past 20 years. These include exceptionally large interest rate rises and falls, as well as changes in the shape of the yield curve. In stress analyses of liquidity risk, underlying criteria for market-wide effects include a change in the Central Bank's refinancing policy and capital market-driven changes in refinancing conditions. With respect to the Bank itself, the scenarios explore the impact of a downward shift in the Bank's own credit rating, as well as changes in client and investor behaviour. Operational risks are also identified and assessed by means of scenario analyses. For the purposes of stress scenarios, it is assumed that both the probability of occurrence and quantitative impact of these loss scenarios are heightened.

RISK MANAGEMENT AND RISK CONTROL

L-Bank's risk management and risk controlling processes include the identification, assessment, management, monitoring and communication of material risks.

DEFAULT RISK

Default risk refers to a possible loss from a lending transaction within the meaning of the German Banking Act (Art. 19 KWG) in the event that the counterparty does not meet its contractual obligations. The reason for non-fulfilment of a contract may be specific, or related to the borrower's credit standing or surrounding circumstances, or political in nature.

Quantitative assessment of value-at-risk calculations

Risks on unanticipated losses are restricted by applying the value-at-risk limits enshrined in the risk-bearing capacity concept.

Unanticipated losses are always estimated using the Monte Carlo simulation method based on internal and external ratings, as well as rating-dependent probabilities of default provided by rating agencies. The calculation assumes a 12-month holding period and a confidence level of 99.0%. These estimates also take into consideration correlations with the borrowers' respective home countries. The value-at-risk calculation deliberately takes a conservative approach: only selected types of collateral are assumed to have risk-mitigating effects, based on highly restrictive premises. Furthermore, standardised recovery rates (currently 30.0%) are only applied to the Bank's "Companies in the financial sector" and "Public sector" business lines. Due to the structure of the Bank's portfolio, transfer risks associated with currency transactions as a whole are only of secondary importance. The risk that L-Bank might incur losses as a result of restrictions on payment transactions due to legal constraints in the various countries concerned is consequently regarded as very minor.

Due to the specific characteristics of the Bank's housing development activities (associated with its public-service mandate), it makes little sense to apply a "market model". For this reason, unanticipated losses in the Bank's housing development business are calculated using an in-house statistical risk-assessment method. When calculating the value at risk, proceeds from the realisation of any collateral provided are taken into account: L-Bank adjusts the recovery ratios to match current realisation values in each case. In view of the fact that the Bank's housing development business is characterised by a large number of homogeneous borrowers, correlations between individual borrowers are not taken into consideration. The probability that a borrower will default is assessed by reference to weighted average annual defaults in the target market segment over the past 25 years.

The following table provides an overview of the proportion of the aggregate loss ceiling taken up by counterparty default risks in the course of 2012:

VALUE AT RISK FOR COUNTERPARTY DEFAULT RISKS IN 2012 in EUR millions

	01.01.2012		31.03.2012		30.06.2012		30.09.2012		31.12.2012	
	Limit	Used	Limit	Used	Limit	Used	Limit	Used	Limit	Used
Aggregate loss ceiling	995.0	595.5	995.0	690.4	1,395.0	753.4	1,395.0	706.3	1,395.0	645.6
Share of counterparty default risks in %	65.3	77.0	70.9	73.8	50.5	62.3	50.5	63.8	50.5	63.8
Counterparty default risks	650.0	458.4	705.0	509.8	705.0	469.0	705.0	450.3	705.0	411.7
Private clients	15.0	5.0	15.0	5.8	15.0	5.7	15.0	5.5	15.0	5.4
Companies in the financial sector	250.0	230.0	250.0	218.5	250.0	210.1	250.0	190.3	250.0	183.5
Other companies	350.0	190.0	350.0	206.4	350.0	189.6	350.0	190.8	350.0	178.2
Public sector	35.0	33.4	90.0	79.1	90.0	63.7	90.0	63.7	90.0	44.6

In the case of "Other companies", c. EUR 40.0 million relates to housing development (finance for housing companies). A significant proportion of the remaining value at risk arises from credit-equivalent shareholdings (L-EA Mittelstandsfonds, L-EA Garantiefonds, L-EA Venture Fonds) and finance for projects in the infrastructural sector where L-Bank is de-risking other banks. At c. EUR 85.4 million, the value at risk for "Companies in the financial sector" relates to the "borrower's bank" principle underpinning our business development activities. Of the value at risk in our "Public sector" business, EUR 33.4 million relates to the PIIGS nations.

Timely and adequate risk provisions

L-Bank makes adequate allowance for risks that have become acute by setting aside provisions. For this purpose, the Bank has set up dedicated processes based on the various tools used for the early detection of risks, and issued appropriate guidelines. The following table shows the changing value adjustments for each business unit, as well as their associated risks. It includes valuation allowances that are deducted from net present values when calculating the capital required to determine net positions pursuant to the Solvency Regulation (SolvV). Any valuation adjustments that are not deducted from book values when calculating the capital required under the Solvency Regulation remain available to L-Bank as risk coverage capital under the going-concern approach (e.g. reserves pursuant to Art. 340f HGB). The corresponding risk portfolios are comprised of the gross book values of loans, the net present values of securities and investments, as well as surety balances and credit-equivalent levels of interest-rate derivatives calculated in compliance with the Solvency Regulation, and taking netting and collateral agreements into account.

VALUE ADJUSTMENT RATIOS AS AT 31.12.2012 in EUR millions

	Private clients		Companies in the financial sector		Other companies		Public sector		Total		Ratio in %
	Adjustm.	Portfolio	Adjustm.	Portfolio	Adjustm.	Portfolio	Adjustm.	Portfolio	Adjustm.	Portfolio	
31.12.2009	91.4	8,195.8	31.6	35,584.0	788.0	14,408.5	0.0	8,907.2	910.9	67,095.6	1.4
31.12.2010	87.9	7,749.9	31.6	34,156.0	674.2	11,887.1	0.0	14,273.0	793.7	68,066.0	1.2
31.12.2011	100.4	7,251.9	31.6	33,710.5	567.1	11,659.9	0.0	20,177.2	699.1	72,799.5	1.0
31.03.2012	99.1	7,128.7	31.6	34,397.8	549.8	12,074.4	0.0	21,190.0	680.5	74,790.9	0.9
30.06.2012	96.2	6,995.9	31.6	36,552.7	556.9	11,957.1	0.0	22,513.6	684.7	78,019.4	0.9
30.09.2012	92.7	6,880.8	31.6	32,046.4	525.5	11,757.4	0.0	23,244.4	649.8	73,929.0	0.9
31.12.2012	88.6	6,771.8	31.6	31,236.1	505.8	10,959.8	0.0	23,941.6	626.0	72,909.2	0.9

Qualitative assessment of credit-rating and collateral classifications

For the qualitative assessment of default risks, each borrower is assigned a credit rating expressed as a class of risk (e.g. risk category 1). In assigning individual ratings, L-Bank takes account of the peculiarities of the relevant client's structure. For borrowers involved in development finance for owner-occupied housing, the homogeneity of the customer group means that they are assigned a default rating based on the average probability of default. A flat rating is also used for commitments under the various L-EA funds (L-EA Mittelstandsfonds, L-EA Garantiefonds, L-EA Venture Fonds). These clients are always provided with intensive support and subjected to continuous monitoring. The following table shows the default probabilities of the individual risk categories and shows internal risk categories against the corresponding external risk categories.

Organisation units responsible for issuing loans are always obliged to ensure that lending decisions are backed by sufficient collateral, in order to reduce both the unsecured portion and loss exposure. L-Bank has specified acceptable types of collateral, and also specified the maximum value that should be assigned to each type when determining the unsecured portion. Collateral that – for material or formal reasons – may not be assigned any explicit collateral value must still be accepted when granting loans if the acceptance of such collateral is standard industry practice and if, in the event of realisation, the Bank can expect to realise recovery proceeds.

To indicate the loss exposure, the risk-mitigating effects of certain types of collateral are taken into account. Payables from regional banks that are guaranteed by "grandfathering" and are underwritten by public guarantee and maintenance obligations are assigned to risk category 1. Similarly, loans that are guaranteed by local authorities and real-estate loans secured on residential properties in Baden-Württemberg are also allocated to risk category 1. Where collateral is provided in the form of property charges on residential property in Baden-Württemberg – independent of the real-estate loan, but within the relevant lending ratio – it is assigned to risk category 4. In the case of Pfandbriefe and similar bond issues (e.g. Covered Bonds), priority is given to the external rating of the issue.

RISK CATEGORIES AND CORRESPONDING DEFAULT PROBABILITIES

Risk category	1	2	3	4	5	6	7	8	9	10	11	12	13	14
Mean probability of default in %	0.01	0.03	0.06	0.13	0.27	0.56	1.15	2.35	4.75	9.37	17.63	30.72	100	100
Range of default probability in %	0.01	0.02	0.04	0.09	0.19	0.39	0.80	1.65	3.35	6.70	12.95	23.55		
	0.02	0.04	0.09	0.19	0.39	0.80	1.65	3.35	6.70	12.95	23.55	100	100	100
External		AA+		A		BBB			BB–	B	CCC+	CC		
	AAA	AA	A+	A–	BBB+	BBB–	BB+	BB	B+	B–	CCC	C	Default	Default
		AA–									CCC–			
	Investment Grade						Non-Investment Grade							

The following table shows the risk portfolios for each of the Bank's business units. They comprise the gross book values of loans, the net present values of securities and investments, as well as surety balances and credit-equivalent levels of interest rate derivatives, calculated in compliance with the Solvency Regulation and taking netting and collateral agreements into account.

RISK STRUCTURE OF THE BANK'S LOAN PORTFOLIO AS AT 31.12.2012 in EUR millions

	Private clients	Companies in the financial sector	Other companies and self-employed persons	Public sector	L-Bank total	Percentage
Risk category 1	2,744.6	9,724.9	4,529.2	19,596.9	36,595.5	50.2
Risk category 2	16.1	2,675.1	415.8	3,693.7	6,800.7	9.3
Risk category 3	3,353.4	4,914.5	1,020.2	22.8	9,311.0	12.8
Risk category 4	82.6	11,814.3	1,498.9	452.2	13,848.0	19.0
Risk category 5	0.0	1,283.4	1,038.5	0.0	2,322.0	3.2
Risk category 6	484.5	224.1	603.0	87.9	1,399.5	1.9
Risk category 7	0.1	196.7	700.5	88.1	985.5	1.4
Risk category 8	0.0	327.4	126.6	0.0	454.0	0.6
Risk category 9	0.3	50.8	319.7	0.0	370.8	0.5
Risk category 10	0.0	22.5	307.3	0.0	329.9	0.5
Risk category 11	0.0	0.0	29.4	0.0	29.4	0.0
Risk category 12	57.6	0.2	123.1	0.0	180.8	0.2
Risk category 13	0.0	0.0	111.0	0.0	111.0	0.2
Risk category 14	32.6	1.9	136.7	0.0	171.2	0.2
Total	6,771.8	31,236.1	10,959.8	23,941.6	72,909.2	100.0

The total exposure shown above, amounting to EUR 72,909.2 million, includes securities and CDS totalling EUR 27,029.3 million. L-Bank aims to hold securities and CDS to final maturity (no trading book) and consequently treats them as loans. The Bank applies a moderated form of the lower of cost or market principle. Due to anticipated permanent impairments, L-Bank has written down securities totalling EUR 4.7 million and reduced the book value accordingly. A further risk provision of EUR 30.0 million was set up for the uncollateralised securities portfolio, applying flat-rate principles. The credit quality of the securities and CDS is shown below. Any savings on the lower of cost or market value of securities or negative market values of CDS are included in hidden liabilities.

RISK STRUCTURE OF THE SECURITIES/CDS PORTFOLIO AS AT 31.12.2012 in EUR millions			
Risk category	Portfolio	Hidden liabilities	Spread risks
1	15,686.3	14.4	457.2
2	2,800.0	2.3	82.0
3	2,409.6	23.1	13.0
4	3,805.8	17.0	59.2
5	1,576.2	18.2	34.6
6	421.1	0.4	3.9
7	202.3	3.4	3.5
8	57.1	1.5	2.1
9	50.8	12.4	7.2
10	20.1	0.0	0.0
Total	27,029.3	92.7	662.7

Monitoring of problem loans

L-Bank defines problem loans as loans where there are strong indications that in order to avert or minimise losses, actions may be necessary that go beyond the normal scope of loan administration and intensified contact with the client, and may extend to the requirement for the provision of additional collateral as part of collaboration with the client in an intensive support process. In addition to payment defaults or interruptions, such indications include low credit ratings (risk category 9 or worse). L-Bank distinguishes between problem loans that are being restructured (risk categories 9 to 13) and problem loans at the workout stage (risk category 14).

As at 31 December 2012, the Bank's portfolio of problem loans amounted to EUR 1,261.5 million. This was distributed between the Bank's business units as shown below.

PROBLEM LOAN PORTFOLIO AS AT 31.12.2012 in EUR millions

	Risk portfolio	Problem loan portfolio					
	Total	Total	%	Restructuring	Workout	Workout ratio %	Value adjustments
Private clients	6,771.8	266.8	3.9	206.6	60.2	0.9	88.6
Companies in the financial sector	31,236.1	9.0	0.0	7.1	1.9	0.0	31.6
Other companies and self-employed persons	10,959.8	985.7	9.0	847.9	137.8	1.3	505.8
Public sector	23,941.6	0.0	0.0	0.0	0.0	0.0	0.0
Total	72,909.2	1,261.5	1.7	1,061.6	199.9	0.3	626.0

Assessing risk concentrations

Due to our public-service mandate, L-Bank is exposed to certain risk concentrations.

In housing development, for example, there is a concentration risk associated with the collateral provided. The value of residential property is determined according to the provisions of the Lending

Value Ordinance, whereby L-Bank claims the privileges associated with small loans and generally omits onsite inspections. Due to the conditions in the housing development market, a proportion of c. 44.0% is not secured by real-estate loans. Instead, collateral takes the form of land charges covered by contract.

Because housing development funding is restricted to the jurisdiction in which the guarantor is located, the Bank's housing development activities are associated with a concentration risk linked to residential property in Baden-Württemberg. In the event of a severe economic downturn, first, the default rate would rise, and second, earnings from the realisation of collateral would fall. In order to assess this risk, L-Bank analysed the cyclical sensitivity of the various regions in Baden-Württemberg. To do so, the Bank analysed regional risks threatening the solvency of borrowers in the individual regions in the event of a severe economic downturn. The risk that a borrower in a given region becomes insolvent increases as a function of the regional economy's dependence on exports, as well as the level of unemployment in the region. The risk of insolvency decreases if price levels for residential property in the region are low and the region has a well-integrated infrastructure. The risk of insolvency is expressed as the variance between the level of borrowers' risk in the region and the risk confronting an average borrower in Baden-Württemberg. The Bank used a scoring system to determine the relative exposure in each case. The table below shows L-Bank's housing finance portfolio broken down accordingly. The highest rank indicates the highest level of relative risk. 57.4% of the Bank's housing development finance is committed in regions with above-average sensitivity to economic cycles (ranked 1 to 4 inclusive). Thus, measured in terms of the federal state's economic sensitivity, the economic sensitivity of the loan portfolio rates as slightly above average.

FINANCE FOR RESIDENTIAL PROPERTY IN BADEN-WÜRTTEMBERG AS AT 31.12.2012

Rank	Portfolio in EUR millions	Percentage of total portfolio in %
1	514.7	5.0
2	2,648.7	25.6
3	1,154.9	11.2
4	1,612.3	15.6
5	1,427.5	13.8
6	970.4	9.4
7	811.2	7.9
8	1,192.2	11.5
Total	10,331.9	100.0

Guarantees are subject to another collateral-related concentration risk. Of the guarantees received (without public guarantee or maintenance obligation) worth c. EUR 11,241.7 million, the State of Baden-Württemberg accounts for some EUR 7,627.3 million. Due to the credit standing of the State of Baden-Württemberg, L-Bank regards this risk as negligible. Another EUR 2,123.5 million is associated with sureties/guarantees provided by other local authorities in Germany. A total of EUR 1,187.6 million is based on sureties/guarantees provided by private individuals, companies, banks, public-sector bodies in Germany that are not local authorities, and central and regional governments abroad.

Due to L-Bank's business model, there is a further concentration risk associated with receivables from banks (EUR 29,714.3 million). The Bank's obligation to issue development loans through borrowers' banks (excepting loans awarded through the various housing development schemes and programmes) means that L-Bank's exposure to banks amounted to EUR 11,758.3 million as at 31 December 2012. These lendings to banks are secured by claims on end-clients. Another EUR 1,878.9 million is attributable to the fact that L-Bank has underwritten the commercial banks' exposure to end-client risk. This means that

c. 46.0% of the Bank's total lending commitment relates to business development. EUR 16,077.1 million of the Bank's total lending commitment relate to transactions carried out by L-Bank in addition to development business, where the Bank invests low-cost funds from refinancing in low-risk or risk-free issuers. Of this amount, EUR 10,617.2 million is secured by public guarantee/maintenance obligation, and EUR 1,586.2 million against Pfandbriefe. Of the remaining EUR 3,873.9 million, roughly 92.0% is assigned to risk categories 1 to 4. Approximately 8.0% is allocated to risk categories 5 to 8. Just EUR 0.9 million is allocated to risk categories 9 and 10.

In regional terms, the Bank's public-service mandate means that it is exposed to a concentration risk for the region "Germany". A total of 85.5% of the risk portfolio is assignable to Germany. In turn, 63.0% of this is associated with the federal state of Baden-Württemberg and the Free State of Saxony.

REGIONAL STRUCTURE OF THE LOAN PORTFOLIO AS AT 31.12.2012 in EUR millions

	Private clients	Companies in the financial sector	Other companies and self-employed persons	Public sector	L-Bank total	Percentage
Germany total	6,771.3	24,884.8	10,593.3	20,108.8	62,358.1	85.5
Belgium	0.0	10.0	0.0	205.9	215.9	0.3
Finland	0.0	0.8	0.0	319.6	320.5	0.4
France	0.4	712.1	20.0	531.9	1,264.5	1.7
Greece	0.0	0.0	0.0	0.0	0.0	0.0
Ireland	0.0	622.4	5.0	0.0	627.4	0.9
Italy	0.0	261.4	0.0	452.2	713.6	1.0
Luxembourg	0.0	70.5	0.0	0.0	70.5	0.1
Netherlands	0.0	811.0	49.3	475.5	1,335.7	1.8
Austria	0.0	685.3	31.5	785.1	1,501.9	2.1
Portugal	0.0	0.0	25.2	88.1	113.3	0.2
Spain	0.0	673.9	0.0	87.9	761.8	1.0
Denmark	0.0	143.2	0.0	259.6	402.8	0.6
Great Britain*	0.0	1,212.4	0.0	175.9	1,388.3	1.9
Switzerland	0.1	272.0	82.4	41.4	395.9	0.5
Rest of Europe	0.0	13.5	0.0	409.6	423.1	0.6
Europe total	0.5	5,488.5	213.3	3,832.8	9,535.2	13.1
USA	0.0	174.2	131.4	0.0	305.6	0.4
Other countries	0.0	688.6	21.8	0.0	710.4	1.0
Overseas total	0.5	6,351.3	366.5	3,832.8	10,551.2	14.5
Total	6,771.8	31,236.1	10,959.8	23,941.6	72,909.2	100.0

* Including Guernsey, Jersey, Isle of Man and Cayman Islands

The table also includes securitised assets. These are allocated to specific countries on the basis of the home country of the special-purpose issuing vehicle.

The Bank's risk exposure in the crisis-affected PIIGS nations stood at c. EUR 2,216.1 million as at 31 December 2012. Of this, some EUR 781.0 million (35.0%) is secured against public-sector Pfandbriefe, Pfandbriefe or Covered Bonds. Roughly EUR 626.0 million (28.0%) is payable by national or regional governments. Around 26.0% or EUR 574.0 million is associated with uncollateralised securitised loans. Unsecured claims against banks amount to a total of c. EUR 165.0 million (7.0%).

Managing and monitoring counterparty default risk

Counterparty default risk is managed by setting individual limits for issuers, counterparties and borrowers. The Bank limits cluster risk by establishing portfolio limits for risk categories, industries and regions. In this respect, L-Bank's public-service mandate imposes tight constraints. Consequently, the representation of cluster risks is useful above all as a means of raising awareness of the concentration risks associated with the Bank's public-service mandate. The maximum loan amount that L-Bank can issue to a single borrower incurring a commercial risk outside the Federal Republic of Germany is restricted by appropriate limits set at national level (country limits).

The issuer, counterparty and borrower limits are set by the Board of Management, based on an internal analysis of credit quality and monitored on a daily basis. When any of these limits are exceeded, appropriate risk response measures are initiated on the same day.

Cluster risks in the Bank's lending business are managed by applying portfolio limits to industries and regions. These limits are set by the Board of Management as part of the business and risk strategy. Compliance with the portfolio limits is monitored on a quarterly basis. If these limits are exceeded, the Board of Management is notified and possible risk response measures are proposed.

As part of the Bank's risk strategy, the Board of Management specifies the credit quality requirements that development business not associated with specific programmes must satisfy, since such business is primarily conducted as part of the bank management strategy and L-Bank wishes to generate income from refinancing, not by assuming risks. To ensure risks are managed adequately, it has been stipulated that in the case of transactions where development policy does not specify a binding margin in advance, a risk-based margin should be applied in line with standard market practice.

The operational management of counterparty default risk is based on first-time, ongoing and incident-related evaluations of credit standing and collateral. The latter are used for managing portfolios when extending credit, and also for initiating risk response measures at the earliest possible moment, thereby minimising lending losses. In the context of this risk early warning system, the Bank analyses deteriorating credit ratings at client level, analyses loans at the intensive processing or problem loan stage, and analyses levels of compliance with Art. 18 KWG, as well as changes in earnings ratios for defaulted loans in the housing development sector.

The specified processes for dealing with problem loans and non-performing commitments include a tightly controlled system of warning processes, which ensures that claims are safeguarded and outstanding debts are settled as early as possible.

MARKET PRICE RISK

Market price risk refers to potential losses caused by unfavourable price movements on the money and capital markets. L-Bank has no trading book. Thus market price risks only arise in the non-trading portfolio (bank book). When analysing market price risks, L-Bank distinguishes between

- interest rate risks,
- currency risks,
- risks on stocks and shares and other equity positions (= shareholdings), and
- option risks.

Market price risk is managed primarily by means of interest-rate swaps and cross-currency interest-rate swaps. As at 31 December 2012, the portfolio of interest rate swaps (incl. swaptions) had a nominal value of EUR 78,620.0 million. Cross-currency interest-rate swaps had a nominal value of EUR 12,220.0 million.

Quantitative assessment based on value at risk

Risks from unanticipated losses are calculated using a value-at-risk model. For this purpose, the Bank uses the historical simulation method with a confidence level of 99.0%. To take full account of different market patterns, a total of ten models are produced, and the highest risk value from these calculations is then used in the daily utilisation statement. The following table shows the different types of model currently in use:

TYPES OF MODEL USED IN HISTORICAL SIMULATIONS

	Holding period	Historical period under observation
Absolute interest-rate changes	10 trading days	250 trading days
Relative interest-rate changes	10 trading days	250 trading days
Absolute interest-rate changes, mirrored	10 trading days	250 trading days
Relative interest-rate changes, mirrored	10 trading days	250 trading days
Absolute interest-rate changes	25 trading days	250 trading days
Relative interest-rate changes	25 trading days	250 trading days
Absolute interest-rate changes, mirrored	25 trading days	250 trading days
Relative interest-rate changes, mirrored	25 trading days	250 trading days
Weighted interest-rate changes	10 trading days	1,000 trading days
Weighted interest-rate changes	25 trading days	1,000 trading days

The following table provides an overview of the proportion of the aggregate loss ceiling taken up by market price risks in the course of 2012:

VALUE AT RISK FOR MARKET PRICE EXPOSURE IN 2012 in EUR millions	01.01.2012		31.03.2012		30.06.2012		30.09.2012		31.12.2012	
	Limit	Used	Limit	Used	Limit	Used	Limit	Used	Limit	Used
Aggregate loss ceiling	995.0	595.5	995.0	690.4	1,395.0	753.4	1,395.0	706.3	1,395.0	645.6
Percentage of market price risk	10.6	8.9	11.0	10.4	17.2	21.7	17.2	19.7	17.2	20.4
Market price risks	105.0	53.0	109.0	71.5	240.0	163.5	240.0	138.8	240.0	131.6

Qualitative assessment based on stress scenarios

VaR values allow potential unanticipated losses to be quantified based on the assumption of certain market continuities. Because such steady, linear market trends can no longer be taken for granted – especially in view of the experience of the last few years – the Bank also systematically simulates stress, extreme and worst-case scenarios.

L-Bank uses the stress tests to investigate potential losses as a result of various, more or less extreme, market changes. For example, the impact of a regulatory scenario involving a parallel shift in the yield curve by 200 basis points upwards or downwards is explored with a view to assessing the impact of any resulting loss on liable equity capital. The following table shows the loss of market value in the event of such a parallel shift of the yield curve.

Managing market price risks

The value-at-risk (VaR) limits specified by the Board of Management are used as the basis for managing market price risks. To further limit interest rate risk in the non-trading portfolio, the Board of Management regularly defines a maturity-based target risk structure. This sets out the target interest rate risk profile. The permissible variance of actual from target risk structure is restricted by setting a limit for each maturity band.

NEGATIVE CHANGES IN NET PRESENT VALUE DUE TO A SHIFT OF 200 BASIS POINTS IN THE YIELD CURVE

	Year-end 31.12.2012	Maximum 26.01./ 31.01.2012	Minimum 02.01./ 31.10.2012	2012 average
Loss of net present value in EUR millions	469.4	541.9	425.9	486.5
Percentage of liable equity capital pursuant to Art. 10 KWG	13.4	17.3	12.5	14.4

The Controlling department is responsible for monitoring interest-rate risk and currency risk by comparing the value-at-risk figures calculated each day with the specified limits. A daily risk report is submitted to the individual board members responsible for risk controlling and the trading departments. The entire board is also informed about market price risks in a full monthly report.

LIQUIDITY RISK

Liquidity risk includes, first, the risk that payment obligations cannot be met when they fall due (liquidity risk in the narrow sense). Also, it includes the risk that transactions either cannot be concluded at all, or cannot be concluded at the expected price (market liquidity risk). Furthermore, it includes the risk that sufficient liquidity cannot be obtained on the expected terms when required (rollover refunding risk).

In the year under review, L-Bank's excellent position on the capital markets – supported by the State of Baden-Württemberg's guarantee – meant that refinancing could be obtained on terms favourable to both the Bank and its investors. Overall, with respect to cost and structure, the Bank was able to obtain refinancing on optimum terms corresponding to budgetary projections. At no time did the Bank have to resort to its liquidity reserves.

Quantitative assessment using value at risk

Value at risk for liquidity risks (liquidity funding risk) is calculated on the basis of historical trends in L-Bank's refinancing terms. The underlying assumption is that the Bank is only able to refinance net disbursements on less advantageous terms. The net present value of the resulting expenses represents the value at risk.

The value at risk for market liquidity risk describes the potential loss incurred if the Bank is unable respectively to buy or to sell certain positions within 24 hours, but instead only within ten days, due to little or no demand on the capital markets.

Liquidity funding risk equates to the risk of a potential deterioration in the refinancing options available to the Bank. To avoid dual calculations, only the liquidity funding risk is taken into account when calculating the VaR for liquidity risk.

VALUE AT RISK FOR LIQUIDITY RISK IN 2012 in EUR millions

	01.01.2012		31.03.2012		30.06.2012		30.09.2012		31.12.2012	
	Limit	Used	Limit	Used	Limit	Used	Limit	Used	Limit	Used
Aggregate loss ceiling	995.0	595.5	995.0	690.4	1,395.0	753.4	1,395.0	706.3	1,395.0	645.6
Percentage of liquidity risk	6.5	2.9	6.5	5.5	4.7	6.2	4.7	6.3	4.7	5.2
Liquidity risks	65.0	17.3	65.0	37.8	65.0	46.6	65.0	44.5	65.0	33.3

Quantitative assessment using regulatory ratios

Liquidity risk in the narrow sense is monitored by the Controlling department using the ratios specified in the German Liquidity Regulation. As required by the regulation, the liquidity ratio is calculated and reported on a monthly basis. The calculation compares anticipated payments over the next 30 days with anticipated disbursements over the same period. In the period under review, incoming payments should exceed outgoing disbursements. As at year-end, the liquidity ratio was 2.4. The mean liquidity ratio over the year was 2.7.

LIQUIDITY RATIO IN 2012 PURSUANT TO THE LIQUIDITY REGULATION

Month	Liquidity ratio
January	2.3
February	2.2
March	1.9
April	2.1
May	2.7
June	2.6
July	2.8
August	3.5
September	3.3
October	3.7
November	3.4
December	2.4
Average ratio	2.7

Quantitative assessment based on stress scenarios

L-Bank holds liquidity reserves in order to cover short-term refinancing needs. To calculate these liquidity reserves, the securities portfolio is broken down into highly liquid (7-day liquidity buffer), liquid (30-day liquidity buffer) and other securities. It is important to ensure that the Bank's liquidity requirements for time frames of one week or one month are covered by appropriate liquidity buffers.

L-Bank also ensures that it has liquidity reserves capable of bridging any additional funding needs that may arise from stress scenarios over time frames of at least one month. For this purpose the Bank analyses stress scenarios based on in-house, market-driven or combined causes. Liquidity buffers are reviewed on a monthly basis. By limiting and monitoring – on a daily basis – the maximum liquidity requirements for one month, the Bank ensures that the liquidity buffer is not just sufficient to cover the funding needs on the reporting date, but over the whole of the following month.

For the liquidity forecast, when reviewing the liquidity buffer that equates to the liquidity required over days eight to 30, the Bank assumes – for reasons of prudence – that the maximum permissible monthly liquidity threshold of EUR 10.5 billion (less the liquidity requirement for days one to seven) will be required, even if the liquidity forecast indicates that the actual liquidity requirement will be lower. In the stress scenarios, when reviewing the liquidity buffer that equates to the liquidity required over days eight to 30, the Bank assumes that the maximum amount of the maximum monthly permissible liquidity threshold (less the liquidity requirement for days one to seven), plus the liquidity requirement calculated on the basis of the relevant stress scenario, will be required.

LIQUIDITY BUFFER SUBJECTED TO STRESS SCENARIOS AS AT 31.12.2012 in EUR millions

		Stress scenario		
	Liquidity forecast	In-house causes	Market causes	In-house and market causes combined
Day 1 to day 7				
Liquidity buffer	13,180.6	13,180.6	12,591.3	12,591.3
Liquidity requirements	3,257.2	3,257.2	3,275.1	3,275.1
Disposable liquidity buffer	9,923.4	9,923.4	9,316.2	9,316.2
Day 8 to day 30				
Liquidity buffer	12,758.6	12,758.6	11,806.2	11,806.2
Liquidity requirements	7,242.8	7,242.8	7,242.8	7,242.8
Disposable liquidity buffer	5,515.7	5,515.7	4,563.3	4,563.3

The minimal variance between the liquidity forecast and the stress scenarios is due, on the one hand, to the fact that the liquidity forecast is drawn up in line with the principle of prudence, so for example the Bank does not assume that the maturities of due time deposits will be extended. In addition, thanks to L-Bank's business model, in terms of refinancing it only has a very negligible amount of indeterminate cash flows that could, in stress situations, create an unexpected need for liquidity.

Management policies

Operational liquidity management comes under the remit of the Treasury department. The system is based on a computer-assisted liquidity forecast that depicts all anticipated cash flows over the next ten years. The system produces a daily analysis for the current month and the two months following. A monthly analysis is produced for any months remaining in the fiscal year, and for the following fiscal year. An annual analysis is produced for years three to ten. When producing this liquidity forecast, the Bank assumes that contractual maturities shall apply. For future interest rate adjustments relating to housing development, the Bank extrapolates the current nominal interest rate. No assumptions are made regarding the prolongation of time deposits. These are updated on a daily basis as part of liquidity management. Budgeted figures for anticipated disbursements are updated monthly, based on new business forecasts.

The Bank has formulated a number of policies for managing liquidity risk. Limits have been placed on participation in individual securities issues and on liquidity requirements for a single month. Holdings of ECB-eligible securities and securities that can be converted on demand may not fall below a minimum threshold.

Liquidity risk is assessed on a daily basis and included with market price risk in a daily report submitted to the Board members responsible.

OPERATIONAL RISK

Operational risk represents the risk of losses due to the inadequacy or failure of internal processes, individuals or systems, or as a result of external events. This definition includes legal risks.

Assessment procedures and management

For operational risks, VaR is estimated using a model similar to that used in the insurance industry to determine the risk of major disasters. The model is based on historical observations and expert estimates of the probability of occurrence of, and extent of damage resulting from, disruptions in any risk-bearing process at the Bank. The estimates, which are audited, are aggregated to arrive at an overall VaR for the Bank as a whole. The Bank is obliged to resort to estimates simply because to date, the Bank has only experienced a limited number of loss events associated with operational risks, and the consequential damages have been negligible. Hence, it is not possible to provide an informed calculation of the VaR on the basis of historical data sets.

The size and scope of operational risks are identified and assessed with the aid of structured interviews across all departments. The identified risks are assigned to five categories. These are defined in terms of both the impact on L-Bank's financial status of a potential risk were it to materialise, and also the anticipated frequency of such an occurrence.

In addition to insurance taken out in order to reduce the business impact of certain loss events, an extensive system of internal controls has been set up. This acts as the basis for avoiding operational risks, and includes comprehensive implicit and explicit procedures for safeguarding the Bank's process workflows (e.g. two-person verification, random spot checks, a new product process governing new types of transactions or processes, explicit authorisation of payments exceeding EUR 1.0 million, an IT permissions management system that excludes conflicts of interest between incompatible activities, rigorous selection criteria for new recruits). The system as a whole is based on the Bank's written documentation, which takes a modular approach to the formulation of the rules governing corporate structure and workflow.

With respect to workflow organisation, the Bank differentiates between operational directives – which represent binding prescriptions for action – and operational manuals. Operational directives always apply, regardless of the underlying workflow or IT systems used. Operational manuals, on the other hand, are either IT user manuals or describe specific processes. L-Bank has broken down the entire loan administration process into multiple stages: granting of loans, further processing of loans, processing of problem loans, loan restructuring and loan workout (settlement). Criteria have been established for each stage in the process and must be complied with when a loan is being processed. These processing criteria constitute the master lending process. A master process has also been established for trading transactions. This sets down the processing criteria for reviewing opportunities for trades; for agreeing, recording, forwarding and changing closing dates; for updating the trading portfolio; for the legal form of contracts; for closing trades outside the Bank's own trading rooms and normal working hours (late trades); for recording and monitoring telephone calls; and for ongoing supervisory activities relating to settlement and controls.

The rules governing corporate structure describe where particular business activities are carried out (organisation chart and schedule of responsibilities). The rules governing "management and representation" describe who may carry out specific business activities. Statutory requirements pertaining to employment law and industrial relations are managed by service agreements and employment policies.

BUSINESS RISK

Business risk is defined as the risk that development programme uptake declines, earnings are reduced, and the Bank is unable to cut costs to the same extent. L-Bank can only generate income through transactions that comply with the Bank's public-service mandate. In this sense, a business risk is a risk that L-Bank cannot avoid.

Assessment procedures and management

Personnel expenses and staffing levels are managed – inasmuch as is reasonably possible – by means of productivity analyses. The main aim of productivity analysis is to determine optimum staffing levels required for the performance of assigned duties based on target task times. This means that it is easy to identify spare capacity if the volume of business changes; this in turn means that costs can be reduced.

Taking the "liquidation approach", business risk is factored into the Bank's risk coverage capability based on net present value; fixed personnel and general costs, to which the Bank is exposed by declining development programmes, are also taken into account. The level of these personnel and general expenses is determined through appraisal by qualified experts.

KEY FEATURES OF THE INTERNAL CONTROL AND RISK MANAGEMENT SYSTEM IN TERMS OF THE ACCOUNTING PROCESS

With respect to the accounting process, L-Bank has put a comprehensive internal control and risk management system in place that is being continuously reviewed and developed. The system includes specific rules relating to corporate structure and workflow management. These rules ensure compliance with existing accounting standards and regulations, as well as the orderliness and reliability of the Bank's accounting functions. The accounting process set down in the system covers everything from the booking and processing of a transaction through to the preparation of the annual financial statements. L-Bank's Board of Management is responsible for defining the Bank's internal control and risk management system as it relates to the accounting function. System implementation is the responsibility of the Accounting department, in collaboration with the Controlling and Payment Transactions departments. In addition, the Audit department carries out regular, process-independent checks in order to monitor the reliability of the internal control and risk management system as it affects accounting.

L-Bank prepares its financial statements in accordance with the provisions of the German Commercial Code (HGB) and German Bank Accounting Directive (RechKredV), with due regard for generally accepted accounting principles. The practical interpretation of these regulations is set out in internal manuals and directives governing the various workflows within L-Bank. The Accounting department is responsible for monitoring internal documents on a regular basis, and for adapting them in line with any legal or regulatory changes. The comprehensive management reporting function and Accounting department's involvement in the standardised process for launching new products also help to ensure that the accounting treatment of new products is correct.

Documentation of the accounting process is carefully organised so that it is easy to understand. All relevant documents are stored in compliance with statutory time frames.

The two departments most heavily involved in the accounting process have clearly separated functions: the Payment Transactions department manages sub ledgers for loans, securities and debt and equity accounting. The data is automatically transferred by an interface to the general ledger. The Accounting department is responsible for managing the general ledger, laying down rules for assigning items to accounts, operating the bookkeeping and ledger management system and administrating the financial accounting system.

For financial accounting purposes, L-Bank uses standard software which supports the following functions:
- prevention of unauthorised access by a system of permissions based on authorisation levels,
- prevention of errors by means of plausibility checks, and
- detection of errors by means of two-person verification, standardised reconciliation routines and comparisons of budgeted with actual figures.

These measures also serve to ensure that assets and liabilities are correctly assigned and reported and also plausibly valued.

Up-to-date, reliable and relevant reports on the risk management system as it relates to accounting are regularly submitted to the Board of Management and heads of department. The Board of Management provides the Supervisory Board and its committees with regular updates on the progress of the Bank's business activities, and also provides up-to-date reports on exceptional events.

COMPLIANCE, MONEY LAUNDERING AND FRAUD PREVENTION, DATA PROTECTION

Adherence to existing statutory regulations governing compliance, prevention of money laundering and fraud, and data protection, is assured by appropriate organisational measures and ongoing monitoring of relevant business transactions. In the year under review, the Bank's internal operational directives for preventing money laundering, together with the related procedures, were adjusted in response to changes in the Money Laundering Act as a result of the entry into force of the Act to Optimise the Prevention of Money Laundering (as from 29 December 2011). The Bank's data protection activities focused on organising in-depth training courses for the Data Protection Officers in each of the departments, and updating the list of procedures which the Bank is obliged to maintain under the State Data Protection Act. During the year under review, no extraordinary events were recorded in any of the above areas of responsibility.

PERSONNEL REPORT

As at 31 December 2012, L-Bank employed a total of 1,225 members of staff (2011: 1,218). The increased headcount is due in particular to uptake of the Bank's residential and commercial energy efficiency programmes, which have made a very successful start. Furthermore, additional appointments were made in the corporate support and back-office departments, in line with regulatory requirements. Employee turnover remained very low, at just 4.8% (2011: 2.8%). 13 people left the Bank of their own accord, and 42 employees retired.

At 57% (2011: 56.6%), the proportion of female employees in the workforce remained at a high level typical of the industry. Of the employees entrusted with managerial responsibilities, 75 were women, equivalent to a ratio of 34.4% (2011: 33.0%).

To provide support for employees' family affairs and make it easier to reconcile family life with work life, L-Bank offers flexible working hours (flexitime) and takes employees' individual working time preferences into consideration. A total of 318 employees currently work part-time (2011: 302). In addition, L-Bank has organised places in nurseries, for example, and also offers a comprehensive advisory service on childcare and dependent relatives through a third-party specialist.

L-Bank also keeps close track of demographic trends and the many challenges they present to sustainable business operations. In 2012, the average age of our employees was 45.4, slightly down on the previous year (45.6). The average length of service remains almost unchanged, at 16.7 years (2011: 16.8 years). Over the long term, the Bank expects a further ageing of the workforce, and has responded in the year under review by offering new health-care management and occupational pension schemes. L-Bank recruits new talent primarily among students graduating from the Baden-Württemberg Cooperative State University in Karlsruhe and Stuttgart. The Bank also recruited

17 school-leavers at the end of the 2012 (dual) academic year (2011: 10); as at the balance-sheet date, a total of 38 students and school-leavers were working at L-Bank.

The Bank's remuneration systems are aligned with the performance objectives set out in the current business and risk strategies, and are reviewed at least once a year to ensure they are still appropriate. There was no need for any adjustment in the year under review. L-Bank publishes a detailed Compensation Report online, as part of its public Disclosure Report.

SUPPLEMENTARY REPORT

No other incidents or events of particular significance occurred after the fiscal year ending 31 December 2012.

OUTLOOK

After the economic slowdown in Q4 2012, the German Council of Economic Experts anticipates an improvement in Germany's economic situation during 2013. The Council is predicting that Germany's gross domestic product (GDP) will grow by 0.8% (as at November 2012), unless the euro crisis intensifies. Rising exports to non-European countries in particular – supported by demand from emerging economies – are expected to play a leading role. Domestic demand should also contribute to macroeconomic growth, driven by a slight increase in private consumption and stable levels of business investment. As for employment, both L-Bank and the Council of Economic Experts anticipate a mild slowdown of the upswing observed in 2012, resulting in a slight rise in unemployment.

As for Baden-Württemberg, the Statistical Office of Baden-Württemberg is predicting economic growth (measured by GDP) of 1.25% (as at December 2012). L-Bank expects the positive situation on the labour market to continue, and this in turn should stabilise consumption. Nevertheless, many businesses could continue to maintain a waiting stance, which is why the Bank does not expect investment demand to drive any strong growth in the near future. Despite the slowdown in demand from EU countries, L-Bank is expecting exports to rise in 2013, since for both Baden-Württemberg's economy and indeed the German economy as a whole, demand is likely to be driven primarily by non-European markets.

In these volatile conditions, L-Bank is predicting a decline in operating income before risk provisions/valuations over the next two fiscal years, 2013 and 2014. The main reason for the decline will be reduced net interest income due to low interest rates. Furthermore, the modest economic expectations mean that the Bank is anticipating mildly negative valuation results, which in turn will have a negative impact on the operating result after risk provisions/valuations. The Bank is expecting the balance sheet total for 2013 to reach a level similar to 2012, after which it is likely to fall slightly.

The Bank is not anticipating any structural changes in its business activities over the next fiscal year, only the usual slight adjustments to individual development programmes.

Working closely with the commercial banks, L-Bank will continue to support Baden-Württemberg's entrepreneurs and SMEs in the future, providing a variety of financial products to fund their projects. The Bank will endeavour to continue its business development activities by relying primarily on the existing product range and targeting a persistently high volume of new business. Over the coming year, the Bank will continue to focus its business development efforts on finance for energy efficiency. With respect to risk assumption, there will be a shift in the jurisdictional boundary between Bürgschaftsbank Baden-Württemberg GmbH and L-Bank during 2013. To date, Bürgschaftsbank has been responsible for assuming risks up to a threshold of EUR 1.0 million, and L-Bank has been responsible for amounts exceeding this threshold. The threshold will now be raised to EUR 1.25 million. It is not yet possible to assess the extent to which this will impact new business under the Bank's guarantee programme.

In view of the high demand to date, one of the priorities of the Bank's housing assistance activities over the next few years is expected to be ongoing support for programmes financing energy efficiency. In addition, the funding conditions for the state's housing assistance programme in 2013 will be made much more attractive than before. For example, the maximum levels of finance available for home ownership schemes will be increased, and the requirement that purchasers of investment properties should renovate them to meet very high standards of energy efficiency will be waived. Rental housing assistance will become more attractive as a result of lower interest rates and less rigorous lending conditions. Because individual programme adjustments may have to be negotiated in advance with the EU Competition Commission, however, it is possible that the programme launch may be delayed. Conditions of finance for apartment owners' associations will also improve due to further interest subsidies and a relaxation of the conditions governing the eligibility of projects for assistance. Due to this proliferation of programme incentives, a higher volume of commitments is expected across all segments of the state housing assistance programme during 2013. Similar volumes of new business under similar conditions are expected in fiscal year 2014. Even so, the developments under the state housing assistance programme that have just been described depend entirely on the extent to which both federal and state governments will be able to make funding available in 2014.

As a services provider, L-Bank will continue to act as an important partner to the state government in distributing future financial aid. The Bank is currently holding discussions with various ministries to decide whether L-Bank should take over additional duties, and about launching new programmes. In addition, preparations for the next European Social Fund (ESF) and European Regional Development Fund (EDRF) programming periods – both due to start in 2014 – have already begun and are being given high priority. The ESF provides targeted funding to boost employment opportunities for European citizens; the ERDF provides funding to boost research and development in Baden-Württemberg, together with ongoing support for environmental protection. As part of the preparations for the new funding period, the EU Commission is planning the mandatory, phased implementation of large-scale IT systems to support primarily electronic communication between the beneficiaries of financial assistance and the funding agencies, under the heading of "e-cohesion". L-Bank is planning to implement a suitable concept in the medium term.

Even after the state government's decisions to abolish tuition fees and the state educational allowance, processing of existing commitments will still take some time to complete. Due to the earlier uptake of family allowance entitlements – in some cases for up to 14 months – and resultant delays in application submissions, it is likely that the last batch of applications for state educational allowances will only be approved in 2014. Furthermore, in November 2012 the Federal Parliament resolved to introduce a childcare allowance as from 1 August 2013. In the event that L-Bank is entrusted with distributing the childcare allowance, current estimates show that additional staffing would be required. This would only be partially offset by the simultaneous elimination of the state educational allowance.

In the course of 2013, the Bank is planning to construct new buildings in the technology parks in Karlsruhe, Stuttgart and Reutlingen, with a total budget of EUR 39.4 million. This will ensure that the technology parks continue to develop steadily and reliably: the main beneficiaries will be the small and medium-sized businesses that are already based there. As well as the technology and business parks in Baden-Württemberg, which are all operated through management subsidiaries, the Bank also maintains – as part of its regional development remit – a German Centre in Jakarta, Indonesia. The aim of the German Centre concept, originally developed in the 1990s, is to provide support to SMEs interested in entering and building a position in the Indonesian marketplace. In view of changes to Jakarta's infrastructural conditions, combined with the changing requirements of Germany's SMEs, L-Bank is intending – in consultation with the Ministry of Finance and Economic Affairs – to carry out a restructuring of the Bank's activities in Indonesia in 2013.

Thanks to the Bank's well-diversified refinancing on the national and international money and capital markets, coupled with the Bank's excellent credit standing, the Bank does not expect to have any difficulty raising funds. The volume of borrowing over 2013 and 2014 will remain more or less unchanged from previous years.

The range of supervisory issues currently being discussed at a political level is going to pose major challenges to banks in Germany and Europe over the next few years, primarily relating to the various banks' capitalisation, organisational structures and processes. Thus, Germany's Federal Financial Supervisory Authority (BaFin) has amended the Minimum Requirements for Risk Management (MaRisk), effective as from 1 January 2013, and at the same time introduced additional standards relating to banks' operational and organisational structures. L-Bank is already fulfilling the key provisions of the amended regulation, and is in the process of implementing the remaining requirements. In addition, banks are awaiting numerous new regulations in the wake of the package of reforms imposed by Basle III. However, since the latter has not yet been successfully implemented under European and German law – meaning that the new regulations have not entered into force in early 2013, as originally planned – there is continuing uncertainty about the precise contents of the new legislation. It is, however, conceivable that the Supervisory Board, for example, in its capacity as the Bank's governing body, will find that the impact of the new regulations on operating procedures will oblige the board to restructure its committees and reorganise its working practices.

REPORT OF THE SUPERVISORY BOARD

The Board of Management kept the Supervisory Board and its committees informed of the Bank's development as well as major business transactions throughout the year under review. Their regular reports included in particular reports on business strategy, risk strategy and business development, as well as quarterly reports on the Bank's risk exposure, a report summarising the results of internal audits, and a report on the structure of L-Bank's remuneration systems.

Ernst & Young GmbH Wirtschaftsprüfungsgesellschaft, Stuttgart, carried out the statutory annual audit for fiscal year 2012. They issued an unqualified auditor's opinion. The auditor took part in discussions of the 2012 annual financial statements by the Supervisory Board, Audit Committee and Credit Committee. In these discussions, the auditors reported on the main findings of their audit activities, answered questions and provided additional information. The Supervisory Board discussed the auditor's report and did not raise any objections to the final outcome of the audit.

In a meeting on 12 April 2013, the Supervisory Board examined and approved the Bank's annual financial statements for fiscal year 2012 and took note of the Management Report.

The Supervisory Board approved the Board of Management's proposal to allocate EUR 148,000,000.00 of the net income for fiscal year 2012 (totalling EUR 148,294,239.82) to other retained earnings and carry forward the remaining amount of EUR 294,239.82.

Stuttgart, 12 April 2013

Chairman of the Supervisory Board
Dr. Nils Schmid MdL
Minister of Finance and Economic Affairs
for the State of Baden-Württemberg

LANDESKREDITBANK BADEN-WÜRTTEMBERG – FÖRDERBANK
BALANCE SHEET AS AT 31.12.2012

ASSETS	31.12.2012 EUR	31.12.2012 EUR	31.12.2012 EUR	31.12.2011 EUR
1. CASH RESERVE				
a) cash in hand		32,473.64		36,164.05
b) current balances with central banks thereof: with Deutsche Bundesbank EUR 557,329,510.73 (EUR 528,187,892.17)		557,329,510.73		528,187,892.17
c) current balances with postal giro offices		–.–		–.–
			557,361,984.37	**528,224,056.22**
2. RECEIVABLES FROM BANKS				
a) due on demand		11,243,703.88		10,328,652.70
b) other claims		20,683,113,709.96		21,100,095,993.16
			20,694,357,413.84	**21,110,424,645.86**
3. RECEIVABLES FROM CUSTOMERS thereof: secured through real-estate liens EUR 7,051,035,020.94 (EUR 7,762,618,484.40) municipal loans EUR 9,341,857,878.07 (EUR 7,704,722,287.17)			**24,288,356,256.53**	**22,786,390,528.59**
4. DEBENTURES AND OTHER FIXED-INTEREST SECURITIES				
a) money market securities				
aa) from public issuers thereof: eligible as collateral with Deutsche Bundesbank EUR –.– (EUR –.–)	–.–			–.–
ab) from other issuers thereof: eligible as collateral with Deutsche Bundesbank EUR –.– (EUR –.–)	–.–	–.–		–.–
		–.–		–.–
b) bonds and debentures				
ba) from public issuers thereof: eligible as collateral with Deutsche Bundesbank EUR 4,721,842,330.74 (EUR 3,654,466,617.60)	4,975,945,874.31			3,871,655,966.14
bb) from other issuers thereof: eligible as collateral with Deutsche Bundesbank EUR 15,213,763,625.08 (EUR 14,639,072,823.76)	17,967,424,061.93			17,263,178,835.29
		22,943,369,936.24		21,134,834,801.43
c) own notes nominal value: EUR 447,755,000.00 (EUR 212,319,000.00)		449,705,827.94		215,789,154.24
			23,393,075,764.18	**21,350,623,955.67**
Carried forward			**68,933,151,418.92**	**65,775,663,186.34**

ASSETS	31.12.2012 EUR	31.12.2011 EUR
Carried over	68,933,151,418.92	65,775,663,186.34
5. SHARES AND OTHER NON-FIXED-INTEREST SECURITIES	–.–	–.–
6. SHAREHOLDINGS thereof: in financial institutions EUR 301,986,360.47 (EUR 301,986,360.47) in financial services institutions EUR –.– (EUR –.–)	501,386,150.89	484,771,272.79
7. HOLDINGS IN AFFILIATED COMPANIES thereof: in financial institutions EUR –.– (EUR –.–) in financial services institutions EUR –.– (EUR –.–)	23,309,201.51	24,809,201.51
8. FIDUCIARY ASSETS thereof: fiduciary loans EUR 83,058,729.42 (EUR 95,090,222.57)	83,845,914.32	95,910,018.69
9. INTANGIBLE ASSETS		
a) purchased licences, industrial property rights and similar rights and assets as well as licences to such rights and assets	8,176,235.31	9,972,163.71
10. TANGIBLE FIXED ASSETS	122,019,002.32	126,794,277.80
11. OTHER ASSETS	358,051,014.08	1,106,543,224.40
12. ACCRUED ITEMS	599,869,479.61	367,474,101.73
TOTAL ASSETS	70,629,808,416.96	67,991,937,446.97

LANDESKREDITBANK BADEN-WÜRTTEMBERG – FÖRDERBANK
BALANCE SHEET AS AT 31.12.2012

LIABILITIES	31.12.2012 EUR	31.12.2012 EUR	31.12.2012 EUR	31.12.2011 EUR
1. LIABILITIES TO BANKS				
a) due on demand		90,887,916.84		80,726,007.33
b) with agreed term or notice period		20,423,049,080.39		17,717,181,640.37
			20,513,936,997.23	**17,797,907,647.70**
2. LIABILITIES TO CUSTOMERS				
a) savings deposits				
aa) with agreed notice period of three months	–.–			–.–
ab) with agreed notice period of more than three months	–.–			–.–
b) other liabilities				
ba) due on demand	109,233,579.68			84,857,521.07
bb) with agreed term or notice period	8,259,081,566.82			8,278,553,009.22
		8,368,315,146.50	**8,368,315,146.50**	**8,363,410,530.29**
3. SECURITISED LIABILITIES				
a) notes issued		35,917,564,141.53		36,755,194,091.32
b) other securitised liabilities thereof: money market securities EUR –.– (EUR –.–) own acceptances and promissory notes in circulation EUR –.– (EUR –.–)		–.–		–.–
			35,917,564,141.53	**36,755,194,091.32**
4. FIDUCIARY LIABILITIES thereof: fiduciary loans EUR 83,058,729.42 (EUR 95,090,222.57)			**83,845,914.32**	**95,910,018.69**
5. OTHER LIABILITIES			**225,073,483.20**	**148,794,300.08**
6. DEFERRED ITEMS			**1,011,265,194.94**	**497,702,135.89**
7. PROVISIONS				
a) provisions for pensions and similar obligations		168,306,797.00		154,641,099.00
b) tax provisions		180,000.00		–.–
c) other provisions		184,862,954.62		194,993,485.32
			353,349,751.62	**349,634,584.32**
8. SUBORDINATED LIABILITIES			**750,386,958.11**	**770,666,820.04**
Carried forward			**67,223,737,587.45**	**64,779,220,128.33**

LIABILITIES	31.12.2012 EUR	31.12.2012 EUR	31.12.2011 EUR
Carried over		67,223,737,587.45	64,779,220,128.33
9. PROFIT-SHARING RIGHTS OUTSTANDING thereof: due within two years EUR –.– (EUR –.–)		539,925,800.00	539,925,800.00
10. FUND FOR GENERAL BANKING RISKS		350,000,000.00	304,000,000.00
11. EQUITY			
a) subscribed capital	250,000,000.00		250,000,000.00
b) capital reserve	950,850,789.69		950,850,789.69
c) retained earnings			
ca) legal reserve	–.–		–.–
cb) reserve for shares in a company with a controlling or majority interest	–.–		–.–
cc) statutory reserves	–.–		–.–
cd) other retained earnings	1,167,000,000.00		526,000,000.00
d) net income	148,294,239.82		641,940,728.95
		2,516,145,029.51	2,368,791,518.64
TOTAL LIABILITIES		70,629,808,416.96	67,991,937,446.97

1. CONTINGENT LIABILITIES			
a) contingent liabilities from settled bills of exchange passed on	–.–		–.–
b) liabilities from sureties and guarantee contracts	6,671,334,850.98		8,124,300,021.20
c) liability from the provision of collateral for external debts	–.–		–.–
		6,671,334,850.98	8,124,300,021.20
2. OTHER COMMITMENTS			
a) repurchase commitments from reverse repurchase transactions	–.–		–.–
b) placement and underwriting commitments	–.–		–.–
c) irrevocable lending commitments	2,346,015,605.75		2,045,511,798.48
		2,346,015,605.75	2,045,511,798.48

LANDESKREDITBANK BADEN-WÜRTTEMBERG – FÖRDERBANK
STATEMENT OF INCOME FOR THE FISCAL YEAR 1 JANUARY TO 31 DECEMBER 2012

	2012 EUR	2012 EUR	2012 EUR	2011 EUR
1. INTEREST EARNINGS FROM				
a) lending and money market transactions	1,575,316,821.51			1,589,394,628.89
b) fixed-interest and book-entry securities	637,102,068.50			633,381,682.69
		2,212,418,890.01		2,222,776,311.58
2. INTEREST EXPENSES thereof: from interest subsidies on loans EUR 136,352,729.95 (EUR 90,613,387.00)		1,916,986,833.68		1,898,379,048.36
			295,432,056.33	324,397,263.22
3. CURRENT INCOME FROM				
a) shares and other non-fixed-interest securities		–.–		–.–
b) shareholdings		6,031,035.64		5,749,195.03
c) holdings in affiliated companies		–.–		–.–
			6,031,035.64	5,749,195.03
4. COMMISSION EARNINGS			45,243,425.81	47,043,983.51
5. COMMISSION EXPENSES			6,180,046.18	4,818,069.74
6. OTHER OPERATING INCOME			17,317,768.20	19,803,373.86
7. GENERAL ADMINISTRATIVE EXPENSES				
a) personnel expenses				
aa) wages and salaries	69,014,609.31			71,678,263.20
ab) social security contributions and expenses for pensions and other benefits thereof: for pension provision EUR 6,183,388.81 (EUR 5,576,071.18)	16,901,478.45			16,350,190.04
		85,916,087.76		88,028,453.24
b) other administrative expenses		45,378,262.66		37,218,833.12
			131,294,350.42	125,247,286.36
8. WRITE-DOWNS AND VALUE ADJUSTMENTS ON INTANGIBLE AND ASSETS			12,161,188.56	11,156,712.85
9. OTHER OPERATING EXPENSES			28,507,122.36	25,487,169.90
Carried forward			185,881,578.46	230,284,576.77

	2012 EUR	2011 EUR
Carried over	185,881,578.46	230,284,576.77
10. WRITE-DOWNS AND VALUE ADJUSTMENTS ON RECEIVABLES AND CERTAIN SECURITIES AS WELL AS ADDITIONS TO PROVISIONS FOR LOAN LOSSES Addition to "Fund for general banking risks" EUR 46,000,000.00 (EUR –.–)	52,774,710.25	–.–
11. INCOME FROM REVALUATION OF RECEIVABLES AND CERTAIN SECURITIES AS WELL AS THE REVERSAL OF PROVISIONS FOR LOAN LOSSES	–.–	390,068,283.20
12. WRITE-DOWNS AND VALUE ADJUSTMENTS ON SHAREHOLDINGS, SHARES IN AFFILIATED COMPANIES AND SECURITIES TREATED AS FIXED ASSETS	–.–	–.–
13. INCOME FROM REVALUATION OF SHAREHOLDINGS, SHARES IN AFFILIATED COMPANIES AND SECURITIES TREATED AS FIXED ASSETS	15,267,116.35	21,642,157.02
14. INCOME FROM NORMAL BUSINESS ACTIVITIES	148,373,984.56	641,995,016.99
15. TAXES ON INCOME AND EARNINGS	836,629.43	852,260.53
16. OTHER TAXES NOT STATED UNDER LINE ITEM 9	183,844.26	184,230.72
17. NET INCOME	147,353,510.87	640,958,525.74
18. PROFIT CARRIED FORWARD FROM THE PREVIOUS YEAR	940,728.95	982,203.21
	148,294,239.82	641,940,728.95
19. ALLOCATIONS TO RETAINED EARNINGS a) to other retained earnings	–.–	–.–
20. NET INCOME	148,294,239.82	641,940,728.95

L-BANK CASH FLOW STATEMENT AS AT 31.12.2012

	01.01.–31.12.2012 EURk	01.01.–31.12.2011 EURk
Net profit/loss for the period	**147,354**	**640,959**
NON-CASH ITEMS INCLUDED UNDER NET PROFIT/LOSS FOR THE PERIOD AND RECONCILIATION WITH CASH FLOW FROM OPERATING ACTIVITIES		
1. Depreciation, value adjustments and write-ups on receivables including contingent liabilities and securities	73,418	–378,872
2. Depreciation, value adjustments and write-ups on fixed assets	12,161	11,157
3. Depreciation, value adjustments and write-ups on financial assets	–4,471	4,212
4. Changes in provisions (excluding loan loss provisions)	36,019	–20,801
5. Other non-cash expenses/income	0	0
6. Profit/loss on the sale of tangible fixed assets	–29	–1,210
7. Profit/loss on the sale of financial assets	–17,867	–2,853
8. Other adjustments (net)	–539,725	–190,026
Subtotal	**–293,140**	**62,566**
CHANGES TO ASSETS AND LIABILITIES FROM OPERATING ACTIVITIES		
9. Receivables from banks	414,622	–1,919,797
10. Receivables from customers	–1,583,274	–697,179
11. Securities	–2,053,558	–3,261,377
12. Other assets	531,161	–552,801
13. Liabilities to banks	2,716,029	–731,275
14. Liabilities to customers	4,905	678,100
15. Securitised liabilities	–837,630	6,432,757
16. Other liabilities	591,635	123,073
17. Interest and dividends received	2,435,833	1,900,110
18. Interest paid	–1,895,270	–1,709,233
19. Extraordinary income/expenditure	0	0
20. Income tax payments	–837	–852
Cash flow from operating activities	**30,476**	**324,092**
21. Proceeds from sales of financial assets	36,101	5,378
22. Proceeds from sales of fixed assets	117	5,102
23. Disbursements for investments in financial assets	–31,878	–19,747
24. Disbursements for investments in fixed assets	–5,678	–7,501
25. Cash flows from other investment activities (net)	0	0
Cash flow from investment activities	**–1,338**	**–16,768**
26. Proceeds from equity contributions	0	0
27. Disbursements to company owners and minority shareholders	0	–130,000
28. Cash flows from other capital (net)	0	0
Cash flow from financing activities	**0**	**–130,000**
Net change in cash and cash equivalents	**29,138**	**177,324**
Effects of exchange rate movements and valuation changes on cash and cash equivalents	0	0
Cash and cash equivalents at the start of the period	528,224	350,900
Cash and cash equivalents at the end of the period	557,362	528,224
	29,138	**177,324**

L-BANK STATEMENT OF CHANGES IN EQUITY AS AT 31.12.2012

	Subscribed capital EURk	Capital reserve EURk	Statement of changes in equity Retained earnings EURk	Net income EURk	Equity EURk
Balance as at 31.12.2010	250,000	950,851	507,000	149,982	1,857,833
Dividend payout				–130,000	–130,000
Capital increase					0
Capital reserve increase					0
Withdrawal from capital reserve					0
Allocation to retained earnings			19,000	–19,000	0
Withdrawal from retained earnings					0
2011 net income for the year				640,959	640,959
Balance as at 31.12.2011	250,000	950,851	526,000	641,941	2,368,792
Dividend payout					0
Capital increase					0
Capital reserve increase					0
Withdrawal from capital reserve					0
Allocation to retained earnings			641,000	–641,000	0
Withdrawal from retained earnings					0
2012 net income for the year				147,354	147,354
Balance as at 31.12.2012	250,000	950,851	1,167,000	148,295	2,516,146

NOTES TO THE ANNUAL FINANCIAL STATEMENTS FOR L-BANK AS AT 31.12.2012

GENERAL PRINCIPLES

L-Bank (Landeskreditbank Baden-Württemberg – Förderbank) was established by a law passed on 11 November 1998, effective as from 1 December 1998. Article 2, para. 1, clause 1 of the above-mentioned law established the share capital of L-Bank at EUR 250 million.

The balance sheet of L-Bank was prepared in accordance with the provisions of the German Commercial Code (HGB) and the applicable accounting directive for banks and financial services institutions (RechKredV).

The balance sheet and statement of income comply with the standard forms in RechKredV. The "Interest expenses" item has been supplemented to include an "of which" note (Art. 265, para. 5, HGB).

When taken together the majority shareholdings reported are of secondary importance. Preparation of a consolidated financial statement was thus waived pursuant to Art. 290, para. 5, HGB and Art. 296, para. 2, HGB.

PRINCIPLES OF CURRENCY CONVERSION

Currency conversion has been carried out according to the provisions in Art. 256a in conjunction with Art. 340h HGB and in IDW RS BFA Opinion 4. Assets and liabilities denominated in foreign currencies, as well as all pending foreign currency cash transactions, are converted at the mean spot rate on 28 December 2012. In the case of forward currency contracts, the forward rate is divided into cash and interest portions.

For currency conversion purposes the Bank calculates currency exposure by offsetting the claims and obligations from on-balance-sheet and off-balance-sheet transactions in the respective currency against each other. These transactions are classified and valued as separately hedged in each currency. Accordingly, all expenses and income from currency conversion within the meaning of Art. 340h HGB are included in the statement of income.

ACCOUNTING AND VALUATION METHODS

Assets, liabilities and pending transactions are valued according to the general provisions of Art. 252 et seq. HGB, taking into account the specific provisions applying to financial institutions (Art. 340e et seq. HGB).

FINANCIAL ASSETS AND LIABILITIES

Receivables from financial institutions and customers are always stated at their nominal value, whereas liabilities are stated at repayment value. Differences (premiums and discounts) with respect to claims and liabilities are stated under accrued or deferred items and written back on a pro rata basis. Administrative charges are collected immediately. Low-interest and zero-interest receivables are discounted. Zero bonds issued and similar liabilities are stated at the offer price plus any prorated interest accrued at the balance-sheet date.

The Bank treats loans linked to development programmes for which it subsidises the interest portion as low-interest lending transactions. Such development programme loans are stated at their net present value. Provisions have been made for interest subsidies on irrevocable lending commitments related to development programmes. Earnings from interest subsidies carried by the Bank are stated under net interest income.

All identifiable individual lending risks as well as country risks have been adequately provided for by making specific loan loss allowances or provisions. General bad-debt provisions have been set up for latent lending risks. Individual and general loan loss allowances are offset against assets or stated under provisions.

Securities in the liquidity reserve are stated at either cost of acquisition or the lower of stock exchange or market price at the balance-sheet date, in accordance with the strict "lower of cost or market" principle. Where possible, stock market quotations have been used to determine market values. Where no active markets are available, model values have been used, based in turn on market data (yield curves, spread curves) and other available information (e.g. probabilities of default).

Securities treated as fixed assets are stated at their depreciated historical costs, whereby differences between the book value and the repayment amount are treated as income in proportion to their term. Depreciation on securities in the financial investment portfolio is only applied in the event of permanent loss of value. A general provision has been set up for latent risks.

Holdings and shares in affiliated companies are stated at acquisition cost or, in the event of an enduring loss of value, at the lower fair value as at the balance-sheet date, analogous to the rules governing fixed assets. Where there is no further likelihood of a permanent loss of value, the original value has been reinstated as appropriate.

FIXED AND INTANGIBLE ASSETS

Intangible assets and tangible fixed assets are valued at acquisition or production cost, less scheduled depreciation. Where necessary, i.e. where it is anticipated that a reduction in value may be permanent, extraordinary write-downs are made. Minor-value assets are combined in an annual summary item and depreciated over five years.

PROVISIONS

Provisions for pensions and similar obligations are determined according to actuarial principles using Dr. Heubeck's mortality tables (RT 2005 G). As a general rule, the Projected Unit Credit (PUC) method is used for valuation purposes. The rate of interest applied is currently 5.06% (2011: 5.13%). Future salary and pension adjustments are included in the calculation, based on a projected average increase of 2% p.a.

The remaining provisions are stated at the required repayment amount, and take into consideration all identifiable risks from doubtful liabilities and impending losses from pending transactions. Provisions with a remaining term of more than one year are discounted at the average market interest rate over the last seven fiscal years that corresponds to their remaining term.

Expense provisions within the meaning of Art. 249, para. 1, clause 3 HGB (old version) shall be maintained either until they are used for the purpose for which they were set up (i.e. the relevant event occurs) or until they are written back because the original reason for their existence ceases to exist.

Interest accruing on provisions (including provisions for pensions and similar obligations) totalling EUR 9.9 million (2011: EUR 8.6 million) is stated under interest income.

LOSS-FREE VALUATION OF THE NON-TRADING PORTFOLIO (BANK BOOK)

The review of the non-trading portfolio (bank book) within the meaning of BFA 3 with the aim of ensuring loss-free valuation is based on a net present value approach. The computation is based on book values (as in the balance sheet), discounted cash flows and risk costs, plus future administrative expenses incurred by the unwinding of positions.

The process of valuation continued to show there was no need to make provisions.

TREATMENT OF HEDGING TRANSACTIONS

In order to hedge balance-sheet risks, the Bank uses derivative hedging transactions and guarantees. The Bank enters into derivative transactions in order to hedge aggregate interest-rate risk exposure and/or individual transactions. Any contributions to earnings by derivatives are stated under net interest income.

Where necessary, hedged transactions and hedging instruments have been grouped together to create valuation units (macro hedges) within the meaning of Art. 254, HGB. The parameters used for the valuations underlying these macro hedges match perfectly (perfect hedges). In this case, the accounting treatment is based on the so-called “freezing method”, in which offsetting changes in value (i.e. equal and opposite changes in the fair values attributable to hedged transactions and hedging instruments as a result of the hedged risk) are not taken into account in the financial statements.

The hedged transactions in macro hedges within the meaning of Art. 254 HGB are presented in the table below. Where applicable, the stated book values have been converted into EUR at the mean spot rate on 28 December 2012.

PRINCIPLES OF THE GERMAN BANKING ACT (KWG)

In fiscal year 2012 the Bank complied at all times with the applicable regulations governing the equity capital and liquidity of financial institutions as set forth in the German Banking Act (KWG).

HEDGED TRANSACTION IN MACRO HEDGE

	Book value (EURk)	thereof interest rate risk	thereof currency risk	thereof price risk	thereof credit risk
Assets	890,058	82,599	–	489,278	318,181
Debts	1,009,489	944,731	64,758	–	–
Total	1,899,547	1,027,330	64,758	489,278	318,181

NOTES TO THE ANNUAL FINANCIAL STATEMENTS FOR L-BANK AS AT 31.12.2012

BREAKDOWN OF SELECTED ITEMS UNDER ASSETS AND LIABILITIES BY REMAINING TERM OR NOTICE PERIOD

	31.12.2012 EURk	31.12.2011 EURk
RECEIVABLES FROM BANKS		
due on demand	11,244	10,329
up to three months	2,559,132	3,284,496
more than three months to one year	3,045,246	1,827,305
more than one year to five years	8,789,148	9,938,654
more than five years	6,289,587	6,049,641
RECEIVABLES FROM CUSTOMERS		
up to three months	995,145	712,413
more than three months to one year	1,371,565	1,456,572
more than one year to five years	4,878,200	4,047,645
more than five years	17,043,446	16,569,761
DEBENTURES AND OTHER FIXED-INTEREST SECURITIES		
Bonds and debentures that mature in the following year	1,755,510	1,533,081
LIABILITIES TO BANKS		
due on demand	90,888	80,795
up to three months	1,702,087	2,205,782
more than three months to one year	1,188,181	1,223,827
more than one year to five years	8,371,822	6,024,300
more than five years	9,160,959	8,263,204
LIABILITIES TO CUSTOMERS		
due on demand	109,234	84,858
up to three months	1,679,350	1,519,884
more than three months to one year	296,390	24,251
more than one year to five years	613,609	976,531
more than five years	5,669,732	5,757,887
SECURITISED LIABILITIES		
up to three months	9,306,642	10,646,256
more than three months to one year	7,609,306	4,816,709
more than one year to five years	16,903,946	19,586,218
more than five years	2,097,670	1,706,011
thereof: maturing in the following year in the subitem “Debentures issued”: EUR 16,915,948,000 (2011: EUR 15,462,965,000)		

EXPLANATIONS OF INDIVIDUAL BALANCE-SHEET ITEMS

	31.12.2012 EURk	31.12.2011 EURk
RECEIVABLES FROM BANKS		
This item comprises:		
– receivables from affiliated companies	–	–
– receivables from companies in which an equity interest is held	5,859,215	5,366,979
RECEIVABLES FROM CUSTOMERS		
This item comprises:		
– receivables from affiliated companies	52,948	49,706
– receivables from companies in which an equity interest is held	150,035	191,516
– subordinated claims	53,983	58,474
DEBENTURES AND OTHER FIXED-INTEREST SECURITIES		
This item comprises:		
– receivables from companies in which an equity interest is held	2,078,184	2,083,050

The subitem "Bonds and debentures" does not contain any securitised subordinated claims or claims on affiliated companies or companies in which an equity interest is held.

Of the securities in this item that are eligible for listing, the following are:		
– listed	22,510,929	20,766,347
– not listed	882,147	604,277

Securities with a book value (excluding prorated interest accrued) of EUR 22,500,157,000 are assigned to investment assets. Of these, securities with a book value of EUR 3,630,110,000 have a market value of EUR 3,574,502,000. The remaining securities in fixed assets have a market value reserve of EUR 1,589,815,000.

SHARES AND OTHER NON-FIXED-INTEREST SECURITIES		
Of the securities in this item that are eligible for listing, the following are:		
– listed	–	–
– not listed	–	–

NOTES TO THE ANNUAL FINANCIAL STATEMENTS FOR L-BANK AS AT 31.12.2012

EXPLANATIONS OF INDIVIDUAL BALANCE-SHEET ITEMS

	31.12.2012 EURk	31.12.2011 EURk
SHAREHOLDINGS		
Of the securities eligible for listing that are included in shareholdings, the following are:		
– listed	68,895	68,884
– eligible for listing, but not listed	–	–
Because of the intention to retain these shareholdings over the long term, short-term fluctuations in value amounting to EUR 0.5 million do not appear in the financial statements.		
HOLDINGS IN AFFILIATED COMPANIES		
This item does not contain any shares that are securitised in the form of securities eligible for listing.		
FIDUCIARY ASSETS		
This item comprises:		
– Receivables from banks	67,902	75,561
– Receivables from customers	15,944	20,349
TANGIBLE FIXED ASSETS		
This item comprises:		
– Plots and buildings used for the Bank's own activities	106,412	111,293
– Plant and office equipment	7,138	6,067
OTHER ASSETS		
thereof subordinated	7,524	7,534
ACCRUED AND DEFERRED ITEMS ASSETS		
– Difference between disbursement amount or acquisition cost and lower nominal value of receivables (claims)	497,539	242,492
– Difference between issue price and higher repayable amount of liabilities	72,117	77,315
LIABILITIES TO BANKS		
This item comprises:		
– Liabilities to affiliated companies	–	–
– Liabilities to companies in which an equity interest is held	327,923	304,471
LIABILITIES TO CUSTOMERS		
This item comprises:		
– Liabilities to affiliated companies	40	–
– Liabilities to companies in which an equity interest is held	–	–

EXPLANATIONS OF INDIVIDUAL BALANCE-SHEET ITEMS

	31.12.2012 EURk	31.12.2011 EURk
FIDUCIARY LIABILITIES		
Fiduciary liabilities comprise		
– Liabilities to banks	7,927	11,369
– Liabilities to customers	75,919	84,541
ACCRUED AND DEFERRED ITEMS LIABILITIES		
– Difference between disbursement amount or acquisition cost and greater nominal value of receivables	13,463	19,816
– Difference between issue price and lower repayable amount of liabilities	5,117	11,285
SUBORDINATED LIABILITIES AND PROFIT-SHARING RIGHTS		
This item does not contain any liabilities to affiliated companies or companies in which an equity interest is held.		
Interest expenses incurred for subordinate liabilities amounted to	28,333	28,092
Interest expenses incurred for profit-sharing rights amounted to	26,004	26,003

A sole subordinated liability denominated in JPY with a value equivalent to EUR 88.1 million exceeds 10% of the total value of all subordinated liabilities. The interest rate is 2.14%; the term ends in 2018.

Subordinated liabilities are intended for use as supplementary capital and comply with the requirements of the German Banking Act (KWG). The important factor here is the subordinated nature of the Bank’s liability in relation to all non-subordinated liabilities towards other creditors. In the event of liquidation, the liabilities of all other creditors would be satisfied in full before any payments were made to subordinated creditors.

A retroactive limitation of the subordination, or of the original term (at least five years) or notice period is not possible.

Under state law, L-Bank is not capable of insolvency.

NOTES TO THE ANNUAL FINANCIAL STATEMENTS FOR L-BANK AS AT 31.12.2012

INDIVIDUAL AMOUNTS THAT MAY BE OF IMPORTANCE IN ASSESSING THE ANNUAL FINANCIAL STATEMENTS:

	31.12.2012 EURk	31.12.2011 EURk
OTHER ASSETS		
– Receivables from swaps	213,009	172,479
– Balancing item from currency conversion	104,304	897,895
– Works of art	14,468	14,244
– Participation certificates	7,524	7,534
– Receivables from the sale of developed property	5,051	6,622
– Options	–	2,580
OTHER LIABILITIES		
– Balancing item from currency conversion	–	–
– Single (bullet) repayments on swaps	173,754	137,431
– Purchase price payments received in advance	41,560	–
– Commitments from short option positions	–	2,580
DEFERRED INCOME		
– Single payments received in advance on swaps	992,622	466,578
PROVISIONS		
Among other provisions:		
– Provisions for undisbursed interest-subsidised loans	74,941	52,870
CONTINGENT LIABILITIES AND OTHER COMMITMENTS		
Before deduction of risk provisions, liabilities from sureties and guarantee contracts include:		
– Loan guarantees to financial institutions	1,093,843	1,724,031
– Credit default swaps	4,474,674	4,971,943
The overwhelming proportion of contingent liabilities comprise credit risks from borrowers with a first-class credit rating. A total of 95.5% of the total portfolio of contingent liabilities have an Investment Grade rating.		
COMMISSION EARNINGS		
– Income from other services	32,634	32,905
– Income from surety fees	12,609	14,139
COMMISSION EXPENSES		
– Consulting fees paid	3,849	2,401
– Surety fees paid	2,026	2,124
OTHER OPERATING INCOME		
– Rental income	5,082	5,488
– Income from services for third parties	5,079	5,012
– Write-back of provisions	3,922	3,686

INDIVIDUAL AMOUNTS THAT MAY BE OF IMPORTANCE IN ASSESSING THE ANNUAL FINANCIAL STATEMENTS:

	31.12.2012 EURk	31.12.2011 EURk
GENERAL ADMINISTRATIVE EXPENSES		
Other administrative expenses include auditor's fees (excl. sales tax):		
– for auditing services	365	365
– for other certification services	23	–
– for tax consulting services	11	–
WRITE-DOWNS AND VALUE ADJUSTMENTS ON INTANGIBLE AND TANGIBLE ASSETS		
– Portion relating to unscheduled write-downs	2,633	–
OTHER OPERATING EXPENSES		
– Expenses for subsidies awarded in the course of processing development programmes for the State of Baden-Württemberg	19,157	19,157
WRITE-DOWNS AND VALUE ADJUSTMENTS ON SHAREHOLDINGS, SHARES IN AFFILIATED COMPANIES AND SECURITIES TREATED AS FIXED ASSETS		
– Unscheduled write-downs	10,511	26,061
– Losses on price movements	4,454	0
TOTAL VALUE OF ASSETS AND LIABILITIES DENOMINATED IN FOREIGN CURRENCIES		
– Assets	2,201,591	1,321,303
– Debts	19,188,191	17,816,181
The exchange rate risk from foreign exchange balance-sheet items is essentially covered by off-balance-sheet hedging transactions. Currency conversion produced miscellaneous operating income in the sum of	45	183

PROVISION OF COLLATERAL

For refinancing purposes, securities with a total value of EUR 12,355.3 million (2011: EUR 12,778.5 million) were deposited with Deutsche Bundesbank. As at 31.12.2012, securities with a value of 2,000.0 million had been credited in the course of open-market transactions (2011: EUR –.–). As at 31.12.2012, no securities were subject to repurchase agreements (2011: EUR 346.6 million). As collateral for OTC transactions, the Bank paid out cash sureties totalling EUR 3,084.1 million (2011: EUR 1,547.1 million), stated under receivables from banks, and accepted cash sureties amounting to EUR 74.7 million (2011: 396.2 million), stated under liabilities to banks.

TRANSACTIONS WITH CLOSELY ASSOCIATED COMPANIES AND PERSONS

As at 31.12.2012, transactions concluded with closely associated companies and persons on conditions that do not conform with market conditions had a stated value of EUR 17.1 million (2011: EUR 16.9 million). These transactions consisted of shareholder loans.

OTHER FINANCIAL COMMITMENTS

With respect to equity investments, there are payment obligations for outstanding contributions to subscribed capital that have not yet been called in amounting to EUR 28.2 million. By acquiring a shareholding in Landesbank Baden-Württemberg (LBBW) with effect from 1 January 2005, L-Bank became a guarantor of LBBW. L-Bank assumed joint and several liability for all LBBW liabilities incurred prior to 18 July 2005, but internally is liable in proportion to its capital share. In the event of claims against L-Bank arising from liabilities incurred prior to 1 January 2005, the Bank is entitled to hold the previous guarantors jointly and severally liable in full. As at the balance-sheet date there are no transactions within the meaning of Art. 285, sections 3 and 3a HGB (new version) that are significant for an assessment of the Bank's financial situation.

NOTES TO THE ANNUAL FINANCIAL STATEMENTS FOR L-BANK AS AT 31.12.2012

DERIVATIVE TRANSACTIONS

As at the balance-sheet date, L-Bank had concluded a number of derivative transactions (forward transactions within the meaning of Art. 36 RechKredv). With the exception of credit derivatives, they are used as hedges against interest-rate and currency risks. A breakdown of the derivatives portfolio appears below. For purposes of reporting derivative transactions, no netting of the positive and negative market values of contracts with the same counterparty was undertaken. As a general rule, insolvency-proof netting agreements are in place. Furthermore, L-Bank has entered into collateral agreements with the Bank's main business partners with the aim of reducing any existing mutual risk of default by providing collateral in the form of cash. Fully hedged derivative structures embedded in underlying transactions are not included in the tables. Derivative transactions valued using the market valuation method pursuant to Art. 285 section 18 HGB break down as follows:

DERIVATIVE TRANSACTIONS – SUMMARY OF AMOUNTS in million EUR	Nominal values 31.12.2012	Nominal values 31.12.2011	Market values positive 31.12.2012	Market values negative 31.12.2012	Market values positive 31.12.2011	Market values negative 31.12.2011
INTEREST-RATE RISKS						
– Interest-rate swaps	78,620	77,750	3,156	–6,217	2,531	–4,587
– Interest-rate options						
Purchases (long)	–	60	–	–	0	–
Sales (short)	–	60	–	–	–	0
Interest-rate risks – total	**78,620**	**77,690**	**3,156**	**–6,217**	**2,531**	**–4,587**
CURRENCY RISKS						
– Forward currency contracts/ swaps	8,280	7,189	1	–189	205	–2
– Currency swaps, cross-currency interest-rate swaps	12,220	11,446	665	–615	924	–306
Currency risks – total	**20,500**	**18,635**	**666**	**–804**	**1,129**	**–308**
SHARES AND OTHER PRICE RISKS						
– Equity forward contracts (no nominal value)						
Shares and other price risks – total	–	–	–	–	–	–
CREDIT DERIVATIVES (CDS)						
– Protection seller	4,475	4,972	1	–37	0	–214
– Protection buyer	–	–	–	–	–	–
Credit derivatives – total	**4,475**	**4,972**	**1**	**–37**	**0**	**–214**

On balance, no meaningful profit or loss on foreign exchange transactions or interest rate valuations is due from interest-rate/currency swaps and the corresponding hedged items, especially on debentures issued in foreign currencies. Positive market values of interest-rate/ currency swaps totalling EUR 104 million are due to changes in spot exchange rates. A balancing item from the currency conversion was set up in this amount on the asset side and stated under "Other assets".

Interest-rate swaps in the non-trading portfolio are used primarily to control total interest-rate exposure, and show a net negative market value of EUR 3,061 billion as at year-end 2012. These interest-rate swaps are not valued in the balance sheet, because both assets and liabilities contain interest-induced hidden reserves that are significantly greater than the negative market values of the interest-rate swaps.

Credit default swaps (CDS) for which L-Bank is selling protection are included under contingent liabilities at a nominal amount of EUR 4,475 million.

DERIVATIVE TRANSACTIONS – BY COUNTERPARTY in million EUR	Nominal values 31.12.2012	Nominal values 31.12.2011	Market values positive 31.12.2012	Market values negative 31.12.2012	Market values positive 31.12.2011	Market values negative 31.12.2011
– Banks in the OECD	90,513	92,645	3,423	–6,124	3,664	–4,627
– Public-sector agencies in the OECD	115	–	5	–9	–	–
– Other counterparties (incl. stock-exchange transactions)	12,967	8,652	395	–925	296	–482
Total	**103,595**	**101,297**	**3,823**	**–7,058**	**3,660**	**–5,109**

DERIVATIVE TRANSACTIONS – BY TERM Nominal values in million EUR	Interest-rate risks 31.12.2012	Interest-rate risks 31.12.2011	Currency risks 31.12.2012	Currency risks 31.12.2011	Credit derivatives 31.12.2012	Credit derivatives 31.12.2011
Remaining terms						
– up to 3 months	3,068	2,260	7,909	8,053	70	50
– up to 1 year	6,359	7,578	3,074	2,058	205	416
– up to 5 years	39,703	38,528	6,801	7,082	3,216	2,656
– more than 5 years	29,490	29,324	2,716	1,442	984	1,850
Total	**78,620**	**77,690**	**20,500**	**18,635**	**4,475**	**4,972**

The transactions reported here do not include commercial transactions.

VALUING DERIVATIVE FINANCIAL INSTRUMENTS

The market valuation of derivatives is based on market data as at 31.12.2012, including yield curves, exchange rates, CD spread curves, and CFC, swaption and FX volatilities obtained by the Bank from external providers. The parameters required for our interest rate structure models are, in part, obtained through calibration using historical time series (mean reversion parameters in Hull-White models, as well as correlation parameters).

Product group	Main valuation model
Interest rate and currency derivatives	DCF method
Caps/floors, swaptions	Black 76
Complex interest rate structures	Interest rate structure models (BGM model, Hull-White model, modified Hull-White modell for multiple currencies)
Credit derivatives	Intensity model

INFORMATION ON TAX LIABILITIES

In accordance with the applicable German tax statutes (Art. 5, para. 1 section 2, KStG and Art. 3, section 2, GewStG), L-Bank is exempt from corporate income and trade tax.

NOTES TO THE ANNUAL FINANCIAL STATEMENTS FOR L-BANK AS AT 31.12.2012

HOLDINGS PURSUANT TO ART. 285, SECTION 11, HGB / ART. 340A (4), SECTION 2, HGB

No.	Name, registered office	Direct shareholding in %	Equity* in EURk	Earnings* in EURk
1.	Austria Beteiligungsgesellschaft mbH, Stuttgart	33.34	35,351	2,029
2.	Baden-Württemberg International – Gesellschaft für internationale wirtschaftliche und wissenschaftliche Zusammenarbeit mbH, Stuttgart	24.00	3,484	–3,812
3.	BEONTRA AG, Karlsruhe	31.50	357	3
4.	CONTTEK Holding GmbH, Pforzheim	44.75	7,059	1,148
5.	DBAG Expansion Fund GmbH & Co. KG, Frankfurt/Main	22.68	786	–20
6.	Dorner GmbH, Gaildorf	40.00	***	***
7.	EB Automotive Group GmbH, Wallerstein	30.97	***	***
8.	greenovation Biotech GmbH, Heilbronn	22.84	239	–1,626
9.	GUTEX GmbH & Co. KG, Waldshut-Tiengen	36.50	18,000	9,733
10.	H. Henselmann Verwaltungs GmbH, Waldshut-Tiengen	36.57	398	86
11.	IntelliShop Holding GmbH, Karlsruhe	42.33	120	–167
12.	KOKI Technik Holding GmbH, Constance	36.55	9,859	–3,317
13.	MBG Mittelständische Beteiligungsgesellschaft Baden-Württemberg GmbH, Stuttgart	26.80	42,597	4,694
14.	Mellifera Dritte Beteiligungsgesellschaft mbH, Weinheim	26.00	9,421	–1,917
15.	Micropelt GmbH, Freiburg	20.10	–9,181	–3,569
16.	PT German Centre Indonesia, Tangerang, Indonesia	83.67	–3,224**	–1,545**
17.	Rhitex Bauplatten GmbH, Waldshut-Tiengen	36.55	87	4
18.	SeeTec AG, Philippsburg	47.61	640	–865
19.	StEP Stuttgarter EngineeringPark GmbH, Stuttgart	100.00	7,237	1,967

HOLDINGS PURSUANT TO ART. 285, SECTION 11, HGB / ART. 340A (4), SECTION 2, HGB

No. Name, registered office	Direct shareholding in %	Equity* in EURk	Earnings* in EURk
20. Strohheker Holding GmbH, Pforzheim	49.50	1,947	41
21. SYMPORE GmbH, Tübingen	34.98	***	***
22. Technologiepark Karlsruhe GmbH, Karlsruhe	96.00	9,841	1,159
23. Technologieparks Tübingen-Reutlingen GmbH, Tübingen	100.00	8,465	97
24. ulrich GmbH & Co. KG, Ulm	21.29	7,508	3,964
25. ulrich Verwaltungs GmbH, Ulm	21.32	59	4
26. Wessel-Werk Beteiligungsverwaltung GmbH, Karlsruhe	35.00	***	***

* As at the last fiscal year available in each case
** Conversion rate: 1 EUR = IDR 12,705
*** No annual financial statements were prepared due to insolvency.

NOTES TO THE ANNUAL FINANCIAL STATEMENTS FOR L-BANK AS AT 31.12.2012

STATEMENT OF CHANGES IN FIXED ASSETS

<table>
<tr><th>Fixed assets
Balance-sheet items</th><th>Acquisition costs 01.01.2012
EURk</th><th>Additions
EURk</th><th>Retirements
EURk</th><th>Transfers
EURk</th><th>Write-ups
EURk</th><th>Total depreciation
EURk</th><th>Book value 31.12.2012
EURk</th><th>Depreciation 2012
EURk</th></tr>
<tr><td>Debentures and other fixed-interest securities</td><td>20,674,513</td><td rowspan="4" colspan="5">Net change pursuant to Art. 34 (3) clause 2 RechKredV: 1,549,971</td><td>22,500,157</td><td>–10,000</td></tr>
<tr><td>Shares and other non-fixed-interest securities</td><td>–</td><td>–</td><td>–</td></tr>
<tr><td>Shareholdings</td><td>765,575</td><td>501,386</td><td>–511</td></tr>
<tr><td>Holdings in affiliated companies</td><td>34,793</td><td>23,309</td><td>–</td></tr>
<tr><td>Intangible assets</td><td>24,463</td><td>2,125</td><td>–497</td><td>–</td><td>–</td><td>–17,915</td><td>8,176</td><td>–3,921</td></tr>
<tr><td>Fixed assets</td><td>219,164</td><td>3,554</td><td>–5,400</td><td>–</td><td>–</td><td>–95,299</td><td>122,019</td><td>–8,240</td></tr>
<tr><td>Other assets</td><td>14,266</td><td>224</td><td>–</td><td>–</td><td>–</td><td>–22</td><td>14,468</td><td>–</td></tr>
</table>

TOTAL REMUNERATION OF COMMITTEES AND EXECUTIVE BODIES OF L-BANK

Directors' remuneration	Fixed remuneration		Variable remuneration		Other remuneration		Sum total	
in EURk	2012	2011	2012	2011	2012	2011	2012	2011
Christian Brand	450	439	217	184	21	20	688	643
Jürgen Hägele	192	327	163	147	7	19	362	493
Prof. Dr. Manfred Schmitz-Kaiser	312	288	144	129	26	25	482	442
Dr. Karl Epple	279	272	87	74	18	15	384	361
	1,233	1,326	611	534	72	79	1,916	1,939

Provisions totalling EUR 615,000 have been made for variable remuneration due to be paid out in 2013. In 2012, the members of the Board of Management received benefits totalling EUR 62,000 according to their entitlements under civil-service law.
No remuneration is paid for directorships in fully owned Group companies.
A commitment has been made to the members of the Board of Management undertaking to pay a pension upon termination of their Board of Management contract. The amount of the pension is based on an agreed percentage of their last annual fixed salary.

	31.12.2012 EURk	31.12.2011 EURk
– Supervisory Board	157	150
– Payments to former members of the Board of Management or their surviving dependants	1,049	771
– Advisory Board remuneration (incl. travel costs)	132	125
– Pension provisions for former members of the Board of Management and their surviving dependants	13,760	10,334

LOANS TO EXECUTIVE BODIES (INCLUDING CONTINGENCIES AND COMMITMENTS)	31.12.2012 EURk	31.12.2011 EURk
– Supervisory Board	36	61
– Board of Management	287	650

All loans earn interest at standard market rates.

AVERAGE NUMBER OF EMPLOYEES IN 2012

	Male	Female	Total
Employees *	506	676	1,182
of whom: full-time employees	481	386	867
of whom: part-time employees	25	290	315

* Excluding vocational trainees and interns

DIRECTORSHIPS HELD BY BOARD OF MANAGEMENT MEMBERS AND EMPLOYEES OF L-BANK PURSUANT TO ART. 340A PARA. 4 SECTION 1, HGB

CHRISTIAN BRAND, CHAIRMAN OF THE BOARD OF MANAGEMENT

BWK GmbH Unternehmensbeteiligungsgesellschaft, Stuttgart	Member of the Supervisory Board
Sächsische Aufbaubank – Förderbank, Dresden	Member of the Administrative Board
Schwäbische Hüttenwerke Automotive GmbH, Wasseralfingen	Member of the Supervisory Board
SHW AG, Aalen	Member of the Supervisory Board
Vorarlberger Landes- und Hypothekenbank AG, Bregenz	Member of the Supervisory Board
Wüstenrot & Württembergische AG, Stuttgart	Member of the Supervisory Board
Wüstenrot Holding AG, Ludwigsburg	Vice-Chairman of the Supervisory Board

PROF. DR. MANFRED SCHMITZ-KAISER, VICE-CHAIRMAN OF THE BOARD OF MANAGEMENT

BioPro Baden-Württemberg GmbH, Stuttgart	Member of the Supervisory Board
MBG Mittelständische Beteiligungsgesellschaft Baden-Württemberg GmbH, Stuttgart	Member of the Supervisory Board
Tourismus-Marketing GmbH Baden-Württemberg, Stuttgart	Vice-Chairman of the Supervisory Board

DR. KARL EPPLE, MEMBER OF THE BOARD OF MANAGEMENT

Baden-Württembergische Spielbanken Managementgesellschaft mbH, Baden-Baden	Member of the Supervisory Board
Bau- und Wohnungsverein Stuttgart, Stuttgart	Chairman of the Administrative Board
Business-Park Göppingen GmbH, Göppingen	Vice-Chairman of the Supervisory Board
Sächsische Aufbaubank – Förderbank, Dresden	Deputy Member of the Administrative Board

EXECUTIVE BODIES OF L-BANK

BOARD OF MANAGEMENT

Christian Brand
Chairman

Jürgen Hägele
Vice-Chairman
until 31.07.2012

Prof. Dr. Manfred Schmitz-Kaiser
Vice-Chairman
since 01.08.2012

Dr. Karl Epple

SUPERVISORY BOARD MEMBER 2012

Regular members

Representatives of the state government*

Dr. Nils Schmid MdL
Minister of Finance and Economic Affairs
Chairman

Alexander Bonde
Minister of Rural Affairs and Consumer Protection
Vice-Chairman

Reinhold Gall MdL
Minister of the Interior
Vice-Chairman

Katrin Altpeter MdL
Minister of Labour and Social Affairs, Family, Women and Senior Citizens

Franz Untersteller MdL
Minister of the Environment, Climate and Energy

Klaus-Peter Murawski
State Secretary,
Ministry of State

Claus Schmiedel MdL
Chairman of the SPD parliamentary group

Edith Sitzmann MdL
Chairman of the Green Party parliamentary group

Other members**

Martin Lamm
Managing Director,
Bauunternehmung Lamm GmbH

Wirtsch.-Ing. Bernd Bechtold
President, Karlsruhe ICC

Roger Kehle
President,
Gemeindetag Baden-Württemberg e.V.
since 28.02.2012

Leni Breymaier
Regional Manager,
VER.DI Baden-Württemberg

Dr. Dieter Salomon
Vice-President,
Städtetag Baden-Württemberg e.V.
since 28.02.2012

Gerhard Burkhardt
Chairman of the Board of Management,
Verband baden-württembergischer Wohnungsunternehmen e.V.

Dr. Maximilian Dietzsch-Doertenbach
Managing Director,
Doertenbach & Co. GmbH

Consulting members

Clemens Meister
Chairman of the Central Staff Council of L-Bank, Karlsruhe

Tatjana Aster
Chairman of the Staff Council of L-Bank, Karlsruhe
since 19.12.2012

Reiner Enzmann
Chairman of the Staff Council of L-Bank, Karlsruhe
until 30.11.2012

Thomas Dörflinger
Chairman of the Staff Council of L-Bank, Stuttgart

* Members ex officio

** Personally appointed

Alternate members

State government deputies

Ingo Rust MdL
State Secretary,
Ministry of Finance and
Economic Affairs

Wolfgang Reimer
Permanent Secretary,
Ministry of Rural Affairs and
Consumer Protection

Dr. Herbert O. Zinell
Permanent Secretary,
Ministry of the Interior

Jürgen Lämmle
Permanent Secretary,
Ministry of Labour and Social Affairs,
Family, Women and Senior Citizens

Helmfried Meinel
Permanent Secretary,
Ministry of the Environment,
Climate and Energyw

Michael Kleiner
Assistant Secretary,
Head of Dept. I, Ministry of State

Peter Hofelich MdL

Andrea Lindlohr MdL
Vice-Chairman of the Green Party
parliamentary group

Deputies

Joachim Wohlfeil
President of the Karlsruhe Chamber of
Trades and Crafts

Dr.-Ing. Hansjörg Rieger
Managing Partner,
RUD Ketten Rieger & Dietz
GmbH & Co. KG

Gerhard Roßwog
President,
Baden-Württembergischer
Genossenschaftsverband e.V.

Roger Kehle
President,
Gemeindetag Baden-Württemberg e.V.
until 28.02.2012

Helmut M. Jahn
President,
Baden-Württemberg Association of
District Councils
since 28.02.2012

Andreas Schmitz
Speaker for the Board of Management,
HSBC Trinkaus & Burkhardt AG

Wilhelm Freiherr von Haller
Chairman of the Board of Management,
Sal.Oppenheim jr. & Cie.

Other state government deputies

Walter Leibold
Assistant Secretary
Head of Financial Policy and
Investments, Ministry of Finance and
Economic Affairs

Joachim Hauck
Assistant Secretary
Head of the Department of Agriculture,
Ministry of Rural Affairs and Consumer
Protection

Volker Jochimsen
Assistant Secretary
Head of Constitutional, Municipal,
Savings Bank and Legal Affairs
Ministry of the Interior

Johann-Christoph Kleinschmidt
Undersecretary
Head of the Central Office,
Ministry of Labour and Social Affairs,
Family, Women and Senior Citizens

Jutta Lück
Assistant Secretary
Head of Administration,
Ministry of the Environment,
Climate and Energy

Dr. Georg Walch
Undersecretary
Head of Budgetary and Tax Policy,
Tax Assessment, Real Estate and
Investments Ministry of State

PROPOSAL BY THE BOARD OF MANAGEMENT FOR THE DISTRIBUTION OF NET INCOME

The Board of Management hereby proposes to the Supervisory Board of L-Bank that out of the net income for fiscal year 2012 totalling EUR 148,294,239.82, an amount of EUR 148.0 million should be allocated to other retained earnings and the remaining amount of EUR 294,239.82 should be carried forward to the current fiscal year.

Karlsruhe, 26 February 2013

L-Bank

Christian Brand Prof. Dr. Manfred Schmitz-Kaiser Dr. Karl Epple

DECLARATION OF THE BOARD OF MANAGEMENT REGARDING THE FINANCIAL STATEMENTS OF LANDESKREDITBANK BADEN-WÜRTTEMBERG – FÖRDERBANK AS AT 31.12.2012

To the best of our knowledge, and in accordance with the applicable accounting and reporting principles, we confirm that the annual financial statements give a true and fair view of the Bank's assets, liabilities, financial position and profit or loss, and that the Management Report includes a true and fair review of the development and performance of the business and the position of the Bank, together with a description of the principal opportunities and risks associated with the Bank's expected development.

Karlsruhe, 26 February 2013

Christian Brand Prof. Dr. Manfred Schmitz-Kaiser Dr. Karl Epple

AUDITOR'S REPORT

We have certified the financial statements and Management Report as follows:

We have audited the financial statements – comprising the balance sheet, income statement, notes, cash flow statement and statement of changes in equity – as well as the accounting methods and Management Report of Landeskreditbank Baden-Württemberg – Förderbank, Karlsruhe, for the fiscal year from 1 January 2012 to 31 December 2012. The accounting and the preparation of financial statements and Management Report in accordance with German commercial law are the responsibility of the corporation's management. Our responsibility is to express an opinion on the financial statements, including the accounting methods and Management Report, on the basis of our audit.

We conducted our audit of the financial statements in accordance with Art. 317 HGB (German Commercial Code) and German generally accepted standards for the audit of financial statements promulgated by the IDW (Institute of Public Auditors in Germany). Those standards require that we plan and perform the audit such that misstatements, errors and irregularities materially affecting the presentation of the assets, liabilities, financial position and results of operations both in the financial statements, as per generally accepted accounting principles, and in the Management Report, are detected with reasonable assurance.

In determining the audit procedures, knowledge of the business activities and the economic and legal environment of the corporation, as well as expectations relating to possible misstatements, are taken into account. Within the scope of the audit, the effectiveness of the accounting-related internal control systems and the evidence supporting the details in the books of account, financial statements and Management Report are examined predominantly on the basis of sampling. The audit includes an assessment of the accounting principles used and material estimates made by the corporation's management, as well as an appraisal of the overall presentation of the financial statements and the Management Report. We believe that our audit provides a sufficiently reliable basis for our opinion.

Our audit did not give rise to any reservations.

In our opinion, based on the findings of our audit, the financial statements comply with the statutory legal requirements and give a true view of the institution's assets, financial position and results of operations in accordance with the generally accepted accounting principles. The Management Report is consistent with the financial statements and, as a whole, provides a suitable view of the corporation's position and accurately portrays the opportunities and risks of future development.

Stuttgart, 26 February 2013

Ernst & Young GmbH
Wirtschaftsprüfungsgesellschaft

Prof. Dr. Caduff
Auditor

Frey
Auditor

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