ANNUAL REPORT
2019

L-BANK
Staatsbank für Baden-Württemberg

L-Bank in Figures

OVERVIEW 2015–2019 in EUR millions

	2015	2016	2017	2018	2019
Total assets	73,294.92	75,075.39	70,669.98	69,608.87	77,622.56
Equity	2,765.31	2,814.64	2,865.23	2,963.98	3,013.96
Net interest income[1]	365.41	368.93	323.41	331.37	302.04
Net income	50.63	49.33	50.59	50.18	49.98

	2015	2016	2017	2018	2019
'Hard' Tier I capital ratio (CET1 ratio)	16.38%	18.00%	18.67%	18.59%	20.06%
Total capital ratio	19.00%	20.29%	20.73%	20.59%	22.20%
Return on equity	10.28%	12.19%	5.44%	6.29%	4.39%
Cost-income ratio	42.82%	41.65%	52.39%	44.53%	53.45%
Leverage ratio	3.91%	4.37%	4.81%	5.12%	4.86%

2019	Moody's	Standard & Poor's
Rating	Aaa	AAA

1 Based on business operations.

A Letter to our *Business Partners*

Dear Business Partners,

A good result, important strategic decisions for the future... although 2019 was a challenging year for L-Bank, there were many positive outcomes. We were delighted by the European Parliament's positive decision, taken on 16 April 2019, to take Germany's legally independent development banks out of the European Single Supervisory Mechanism (SSM). This means that development banks now operate in a more appropriate regulatory environment. Among the important factors influencing the political decision-making process, our objection to banking supervision by the ECB undoubtedly played a part. On the one hand, the European Court of Justice had unfortunately perpetuated what we considered to be an erroneous judgement by the European Court of First Instance.

On the other, in making our objection, we took what has proved to be a correct and significant step, in that it helped European policymakers to better understand and appreciate the business model of regional development banks.

L-Bank was also able to make its mark on the capital market. In November 2018, we were the first European development bank to issue a floating-rate bond with an interest rate linked to the SOFR. In April 2019, we continued this pioneering role by issuing a second, similar bond. Also last year, L-Bank was the world's first institution to issue a bond linked to the new ESTR reference rate. Thus we have made our future direction clear at an early stage: Despite all attempts at reform, Interbank Offered Rates (IBORs) such as EURIBOR and LIBOR do not appear to have good long-term prospects. The future belongs to risk-free rates recently created for overnight money, such as ESTR, SOFR and SONIA, from which interest rates for typical EURIBOR maturities can also be derived.

With the implementation of our online application system for parental allowances, we have opened a new chapter in our service provision. The digitisation of applications simplifies and accelerates the whole application process, both for our clients and for ourselves. This has clearly resulted in a huge gain in efficiency, with more than 50,000 applications approved to date. We also attained an important housing development objective, by consolidating the turnaround in the provision of social accommodation for rent in Baden-Württemberg. In 2019, we once again exceeded the bare minimum threshold of 1,500 residential units per year by a substantial margin, providing development finance for a total of 2,600 residential units (of which around 2,100 were new builds). In the process, more residential units were created than ceased to be eligible for regulated tenancies.

For Baden-Württemberg's business community, last year was economically challenging. This situation is unlikely to change in the near future: A combination of political and economic risks are making investments and capital expenditure less attractive. Despite pervasively low interest rates, it is likely that these lacklustre business conditions will continue into 2020.

How can we counteract this trend? Innovation is the antidote. Baden-Württemberg is well positioned for the next generation of innovative projects. No other federal state can boast as many market leaders or such broad and deep industrial expertise, not to mention a research community that combines world-leading scientific activity with a focus on practical applications. As we face the future, we will continue to trust in our business community's ability to innovate. Our funding figures are an early indication that this trust is wellfounded. More than 4,300 businesses have taken advantage of our Digitisation Premium and Innovation Finance programmes. The excellent, wide-ranging outcomes of these programmes show that firms are working intensively on solutions for the future. But as a development bank, we too must continue to evolve. We must anticipate the ongoing decline of interest rates by preparing to issue development loans at negative interest rates.

Innovation needs more than just suitable funding programmes, however. As they say in the football world: Money alone doesn't score goals! The important thing is to ensure that the whole team is well prepared and to invest in good support structures. The same thing applies to business. While attractive financing options provide a vital incentive, contacts, stimuli and networks are at least as important for generating and implementing ideas. Innovations are the result of positive interactions between many players inside and outside a company – interactions that help the business to identify a customer need and create the right product to satisfy it.

Our technology parks, deliberately situated close to universities and major research institutions, provide firms with an environment that makes it easier to identify promising advances and transform them into real-world solutions. We commissioned Prognos AG, working with ZEW, to evaluate our existing technology parks (TPK, STEP, TTR) while pinpointing the factors that have made them so successful, and to identify other potential locations for technology parks in Baden-Württemberg. Our technology parks have chalked up some impressive achievements. In this annual report, we summarise the findings of the Prognos/ZEW study and use them to extrapolate how best to build upon these successes in the future. This study is the next in a series of studies systematically evaluating our development services and establishing a solid basis for evolutionary refinement.

Over the last few years, we have successfully resolved the many challenges we have faced. For this, I offer my heartfelt thanks to all our members of staff – just as I thank you all for your confidence in me.

Dr. Axel Nawrath
Chief Executive Officer, L-Bank

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Greetings from the *State Premier*

Today, Baden-Württemberg is one of the world's leading innovation and technology hubs. At the same time, we are facing unprecedented challenges to our economic strength. Digitisation and artificial intelligence, along with advanced technologies such as quantum computing, are transforming our society and economy. The automotive industry – one of the key sectors in the federal state's economy and guarantor of huge numbers of jobs – is facing the single most disruptive structural transformation since the invention of the automobile.

For Baden-Württemberg to emerge from this period of transformation as an even stronger and more capable global competitor, we need innovative entrepreneurs as well as creative business founders with the courage and determination to turn their visions into reality. Baden-Württemberg thrives because is nurtures clever minds with good ideas. This is, and always has been, one of the keys to our success.

It is just as important, however, that the surrounding conditions should be right. Businesses and start-ups need an environment that is conducive to innovation and cutting-edge technology. This is why the state government has drawn up its latest budget based on high-priority, long-term criteria for encouraging innovation. Thus, among other initiatives, EUR 100 million has been made available for funding projects associated with the federal government's AI strategy. This includes developing Tübingen's Cyber Valley, which has already become Europe's leading research centre for artificial intelligence. Another EUR 40 million has been set aside for establishing a Centre of Excellence in quantum computing in Baden-Württemberg. And a further EUR 50 million has been budgeted for projects under the aegis of the Baden-Württemberg Healthcare Forum ('Forum Gesundheitsstandort').

In all these activities, L-Bank acts as one of the state government's most supportive and powerful partners. It provides companies from first-time start-ups through to well-established SMEs with turnkey development funding programmes. L-Bank's very satisfactory development, which continued throughout 2019, provides impressive proof of the institution's engagement. The federal state's L-Bank-sponsored technology parks make an important contribution to creating appropriate conditions for innovation. They provide an environment that makes it easier for corporate tenants to concentrate on their business objectives. Because the technology parks are located so close to universities, they also support technology transfer from academia to industry.

I would like to thank L-Bank and all the Bank's employees for their enormous commitment and, once again, wish them every success in fiscal year 2020 – so that Baden-Württemberg can continue to maintain its leading position as a technology and innovation hub.

Winfried Kretschmann MSP
State Premier of the State of Baden-Württemberg

Hothouse for the future

Modern buildings, a good infrastructure and extensive services, situated close to universities, research facilities and educational institutions: Thanks to L-Bank's business zone development, next-generation businesses are burgeoning in ideal conditions provided by state-of-the-art technology parks.

Business Zone Development

Technology parks feel just like campuses.

An evaluation of L-Bank's technology parks[1]

Compared to competitors in Germany and internationally, Baden-Württemberg is one of the world's leading business and innovation hubs. L-Bank's technology parks have made a significant contribution to this position. In partnership with ZEW, Prognos AG was commissioned to evaluate and strategically develop the Bank's technology parks. Prior to this, Prognos AG and ZEW had already carried out a systematic review of the regional innovation systems in all twelve of Baden-Württemberg's regions on behalf of the federal state's Ministry of Economic Affairs, Labour and Housing.[2]

The first stage of the technology park evaluation exercise involved analysing findings on the success-focused environment of L-Bank's existing technology parks. The next stage involved narrowing down and prioritising potential locations for new technology parks in Baden-Württemberg, according to their suitability for hosting an L-Bank-style technology park. High-level interviews with CEOs and individual tenants in existing technology parks, including the Stuttgart Engineering Park (STEP), Karlsruhe Technology Park (TPK) and Tübingen-Reutlingen Technology Park (TTR), as well as further interviews with representatives of municipal umbrella organisations (town, district and municipal council associations) served to narrow down success-related and geographical factors.

Technology parks: evolution and current status

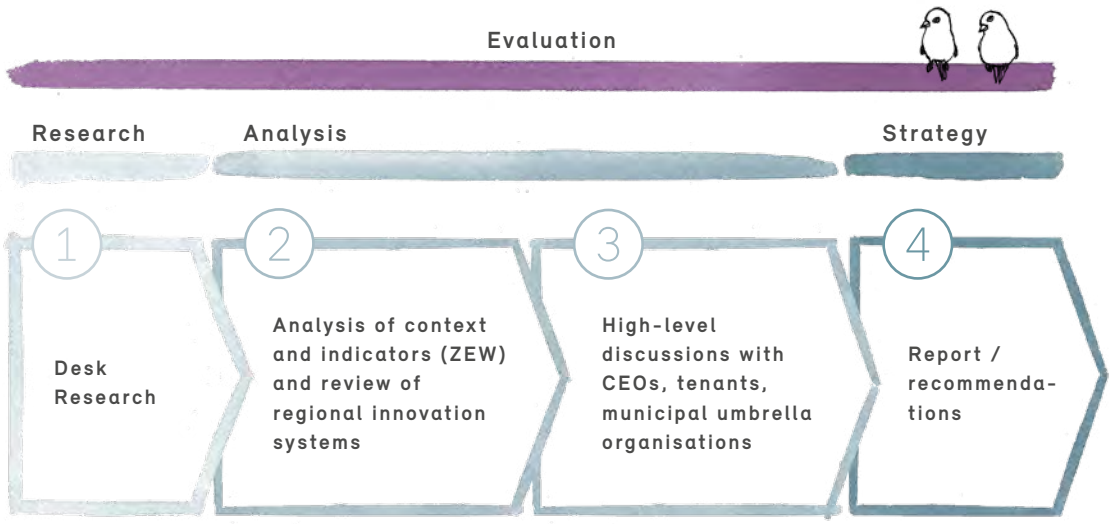
L-Bank's technology parks are real-estate investments by L-Bank that aim to support the development of technology companies and thereby strengthen Baden-Württemberg's position as a business hub. L-Bank's STEP (Stuttgart), TPK (Karlsruhe) and TTR (Tübingen-Reutlingen) technology parks are home to around 250 corporate tenants in four locations, providing over 11,000 jobs in cutting-edge technology sectors such as ICT, engineering and the life sciences. Flexible office and laboratory units are rented to technology-focused young companies just exiting the start-up phase, located on customised, campus-style sites in university towns.

The highly successful development of the three cited technology parks (STEP, TPK and TTR) contrasts with the Bank's experience of less successful development projects such as the now liquidated Gottmadingen and Stauferpark Göppingen parks. Both of the latter were refurbished brownfield sites. This distinction makes it clear that to develop and successfully operate a technology park, it must be established in a central market location with stable, long-term commercial and infrastructural

1 Extract from the Prognos/ZEW study (2019): Evaluation of L-Bank's business zone development pillar, Stuttgart/Mannheim.
2 Prognos/ZEW (2018): Regional innovation systems in Baden-Württemberg – review and conclusions, Stuttgart/Mannheim.

Figure 1

Procedure and analytical priorities



Source: Prognos presentation.

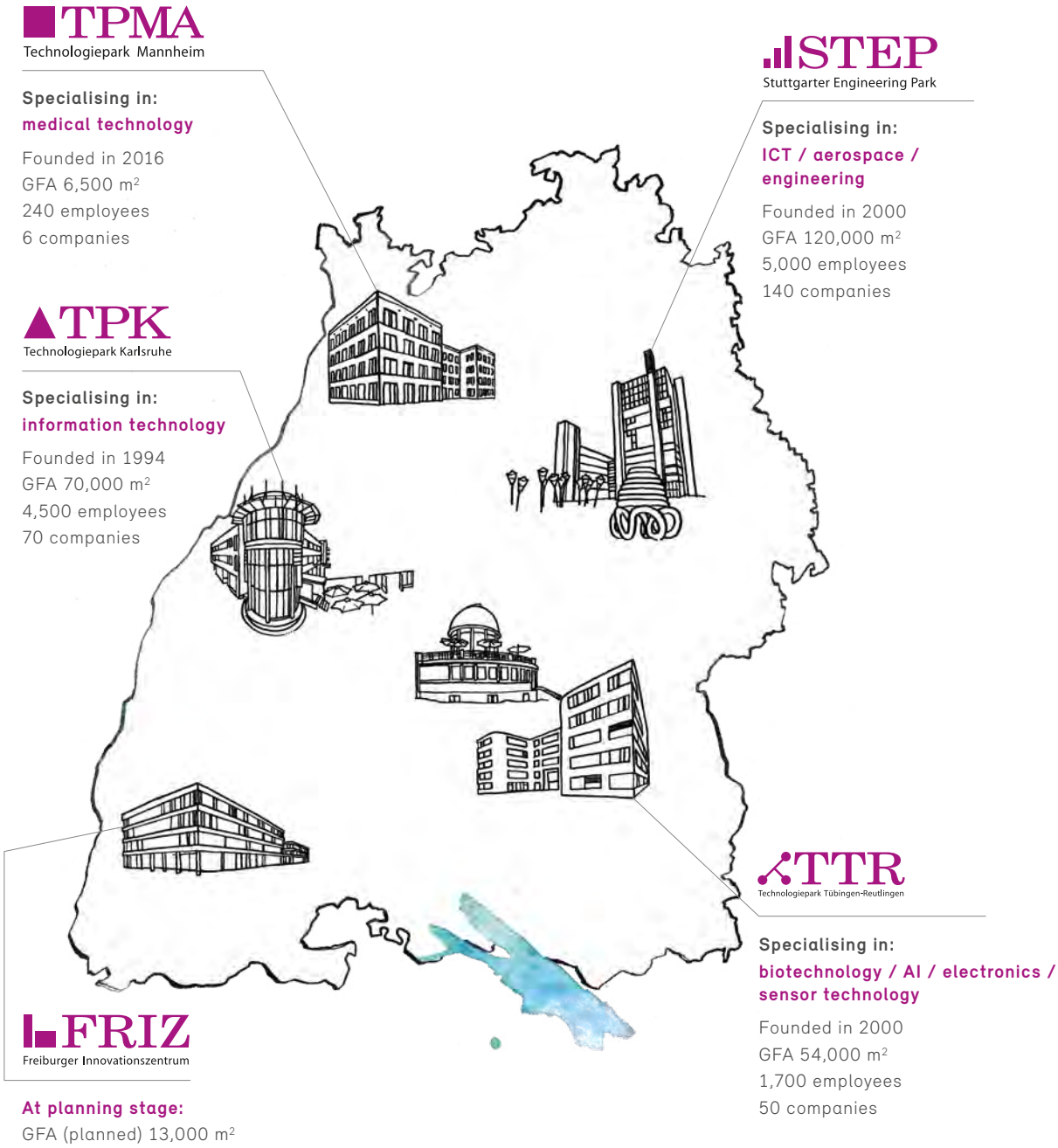
conditions if it is not to jeopardise L-Bank's revenue and risk structures. In 2016, L-Bank took the decision to set up the TPMA Technology Park in Mannheim. In 2019, the Bank then decided to set up another park in Freiburg. Both of these technology parks, currently at the planning and construction stages, have smaller rental premises and are more directly embedded in local infrastructures than the TPK, STEP and TTR technology parks.

For the most part, the Bank's planned (TPMA, FRIZ) and existing (TPK, STEP, TTR) parks already cover and provide access to the major and leading research or higher-education centres in Baden-Württemberg. Finding new locations for technology parks with the right combination of academic and commercial conditions is thus more of a challenge, meaning that potential locations must be subjected to in-depth scrutiny. Figure 2 shows the locations of the TPK, STEP and TTR technology parks in Baden-Württemberg, including the new TPMA and FRIZ technology parks.

When renting space, we were immediately able to contemplate the next stage in our growth.

Figure 2

Overview – key figures and locations of L-Bank technology parks in BW



Source: Prognos presentation based on L-Bank data (mapping: GfK Regiograph).

Technology parks: concept and criteria

L-Bank's technology parks are designed as a long-term business park concept with a series of consecutive expansion phases; they differ from private or municipal real-estate offerings in terms of price levels, target-market parameters, and flexibility of premises and service provision. Unlike traditional incubators, L-Bank technology parks operate according to free-market principles. The development finance aspect does not take the form of subsidised rents, but of real-estate developments for which L-Bank pays in advance. The aim is to attract young and innovative technology companies to the area – businesses that already run as commercial operations and no longer require (ongoing) financial support. L-Bank's technology parks also differ from incubators in their focus on this particular target market; they are best regarded as a kind of 'bridging model'.

L-Bank's technology-park concept differs from offerings by private investors primarily in its long-term approach and laser focus on innovation and technology; the other principle behind L-Bank's technology parks is the implementation of sustainable concepts and strategies with, in some cases, extended payback periods. For example, when setting up STEP, the Bank planned for and implemented very high standards of building and energy efficiency; the resulting geographical and quality advantages boost tenants' growth prospects and sustain their loyalty over the long term.

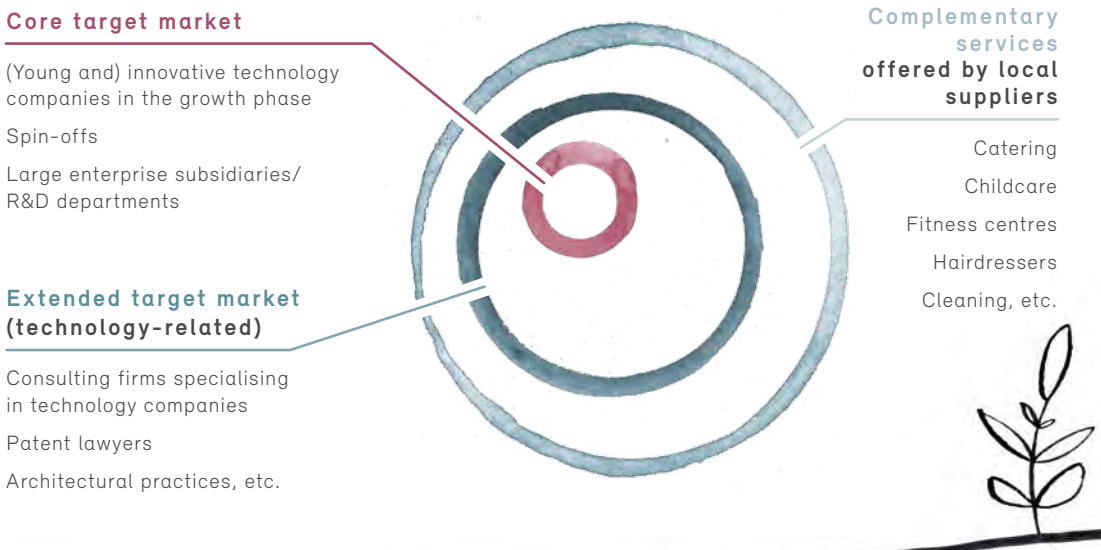
The key target market comprises young technology companies that have started to grow; in practice, the Bank is also very open to other target segments and very flexible with respect to the tenant mix, especially in terms of development over time. To ensure that the rental space is as close to fully occupied as possible, tenants also include companies in technology-related segments (such as consulting firms specialising in technology companies, patent lawyers, architectural and engineering practices). The tenant profile is rounded off by local service providers (offering services such as catering, childcare, hairdressing, dry cleaning, etc.).

Unleashing the full potential

What our technology parks have in common is that they relieve companies and employees of a great deal of work so they can concentrate on their core business without disruption. Examples include the service-minded park management teams, attractive catering and sports facilities, and of course childcare.

Figure 3

Target markets for technology parks

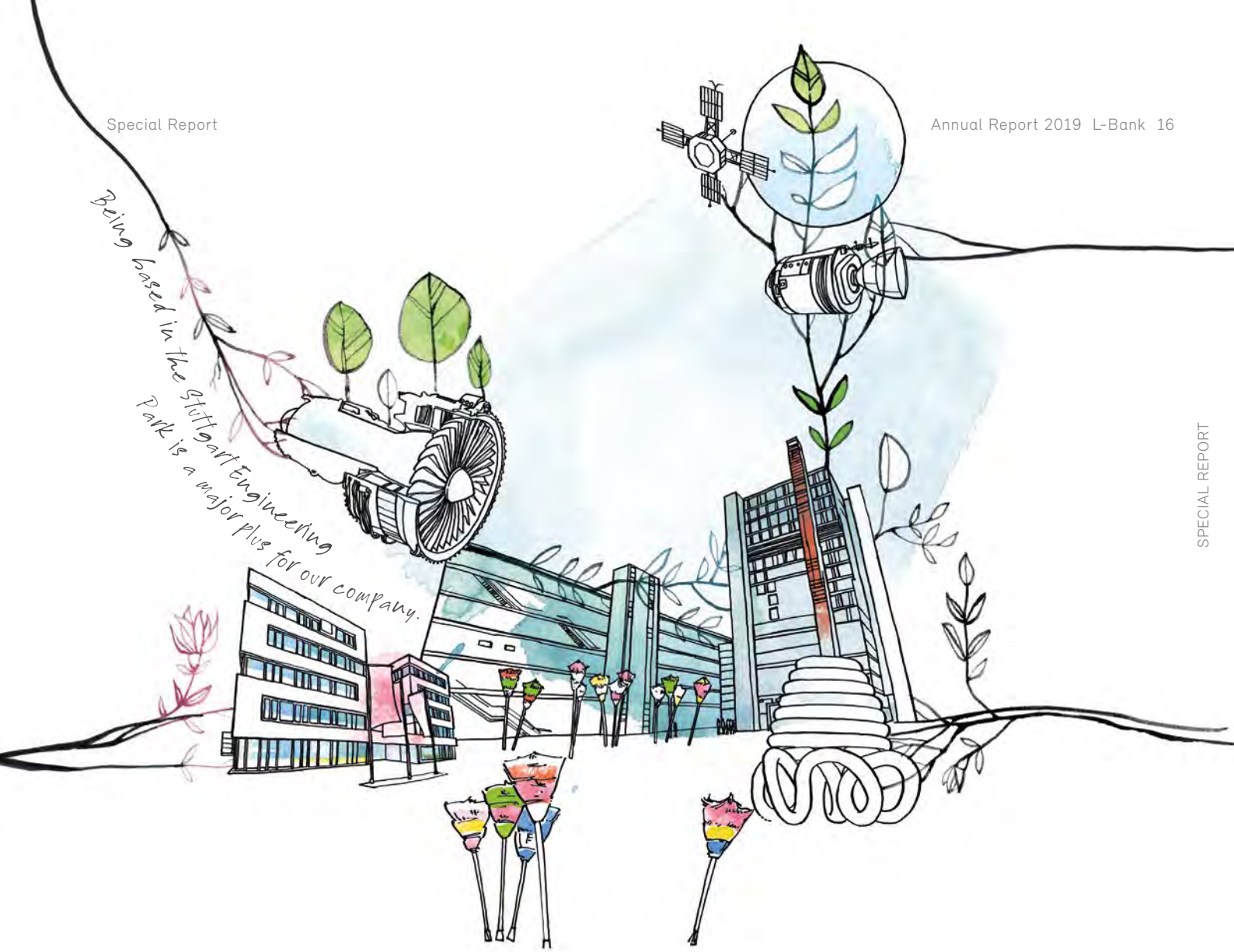


Source: Prognos presentation.

Technology parks: key success factors

In many respects, the successful operation of an L-Bank technology park depends on local conditions at the macro and micro level. The key criteria were established by reference to the existing TPK, STEP and TTR technology parks. Technology parks are set up in towns or cities which, as 'macro' locations, offer the best conditions in terms of existing entrepreneurial and academic/scientific potential.

As the name 'technology park' suggests, the success of an L-Bank technology park is very much dependent on the presence of significant resources focused on technology and innovation. The entrepreneurial technology scene in the macro location (town/city) and its commercial success are an essential foundation for the successful development and operation of an L-Bank technology park. The successful examples (TPK, STEP and TTR) clearly show that where the number and density of innovative, technology-focused, successful companies is high, parks benefit from high rent and occupancy levels. Technology-park tenants are very often technology leaders in their market segments (with high innovation potential) and play an important role in the innovative performance of Baden-Württemberg's economy. The presence of companies with large R&D departments also helps technology parks to succeed. This is because spin-offs from large companies, with their own development priorities and corresponding scope for research and product development, are ideal tenants for L-Bank technology parks.



STEP – Stuttgart Engineering Park

Optimal conditions for technology-focused companies in an ideal environment with direct fibre-optic links to the University of Stuttgart and Baden-Württemberg's research network. Supplemented by fully equipped conference centres, a well-developed service infrastructure, direct access to motorways and a dedicated suburban rail station.

Corporate tenants' technological and innovative strengths are nourished by various sources in a diversified academic/scientific environment – university STEM faculties (with plenty of students and high standards of excellence) are both a vital foundation and a prerequisite. Non-university research institutions are also an important source of inspiration. Research institutions and universities generate new knowledge and play an important role in attracting or training much-needed research specialists and knowledge-workers. Research institutions with close links to industry in the immediate vicinity of the park further enhance the latter's profile, attracting national and international experts as well as companies in the technology sector.

In terms of staff recruitment and optimal networking opportunities, ensuring that a technology park is exceptionally accessible plays a vital role in making a location attractive. The existing technology parks clearly show that good connections to public transport (preferably rail) and easy access by road are essential for long-term success.

In addition to location-related success factors, the evaluation of the existing TPK, STEP and TTR technology parks also identified success criteria associated with the underlying concept. First and foremost is the flexible, modular real-estate concept, tailored to the needs of technology companies. This means that the majority of premises can be equipped and used as offices, laboratories or other types of workspace (e.g. computer centres, server rooms, etc.) with minimal conversion overheads. Furthermore, services customised to users' needs (building services, etc.) allow technology companies to concentrate on their core activities, adding significant value for high-tech firms settled in the park.

In the case of the TPK, STEP and TTR technology parks, their homogeneous appearance and high levels of integration and networking – so much so that they could effectively be classified as 'urban districts' – have successfully established the parks and their locations as a unified brand. The advantage of this is that by leveraging the combined image and branding, companies can benefit from a halo effect which also facilitates staff recruitment.

TTR – Tübingen-Reutlingen Technology Park

Based on the concept of multifunctional space, the technology park supports every conceivable type of workspace, from offices to electronic engineering workshops to advanced biotech laboratories. Both park locations are situated in the immediate vicinity of renowned research institutions and are currently home to around 50 companies, most of which are very research-focused.

Obstacles to success

Obvious obstacles with significant potential to hinder a technology park's success include an insufficient number and density of local technology companies with the kind of growth potential that would qualify them as park tenants. If local firms are not sufficiently technology-focused or commercially successful, this will impact on a prospective technology park's rent levels and target market (such as urban subsidiaries), resulting in vacant premises and underutilisation.

In addition to the number of technology companies, the market situation in the local office-property segment is also a key criterion for selecting a suitable location; if it is not attractive enough, it may limit a technology park's success. Locations where the rental prices for higher-end office or laboratory premises are not sufficiently accessible to local businesses are only suitable for hosting a successful, smoothly operating L-Bank technology park to a limited extent. The areas around the TPK, STEP and TTR technology parks are also characterised by a strong presence of superregional and institutional investors. In smaller, less attractive (office) property markets, the opportunities for third-party commercialisation – not to mention commercial flexibility – are comparatively limited.

Furthermore, certain local contexts and interactions between players (e.g. local decision-making) may also create conditions that hinder success. In the past, for example, park developments that were motivated by external (political) demands, but failed to meet the criteria for geographical location, transport connections, strong research/technology base, rent levels and readily available skilled workforce, were not successful. While the Gottmadingen and Göppingen developments (both conversion projects) received plenty of political support, the poor quality of the local conditions meant that they failed to exert the same business and technology-boosting effect as the TPK, STEP and TTR projects.

Another fundamental prerequisite for the success of a technology-park development project is the interest and active cooperation of municipal actors. Not only do they play a key role in providing a suitable site; they are especially important for ensuring a technology park is fully integrated into regional clusters. The willingness of towns and municipalities to collaborate in the siting of an L-Bank technology park is generally regarded as a given.[3] However, especially in very attractive cities where space is at a premium and the housing market is overburdened, technology-park developments may encounter some resistance from municipal representatives.

3 Source: High-level interviews with representatives of town, district and municipal council associations in October 2019.

While the rents aren't cheap, you get more for your money.

Looking to the future: further development options for the technology-park concept and services

Interviews with tenants and CEOs at existing technology parks produced a range of preliminary ideas and suggestions for ways to expand and further develop the technology-park concept, as well as the various services on offer.

In view of the growing mobility and flexibility of (international) skilled workers, overnight accommodation (e.g. in the form of extended-stay hotels) would add further value for technology companies with multinational connections. This applies in particular to technology parks without hotels or other overnight accommodation either nearby or easily accessible by public transport. A lack of overnight accommodation could represent a bottleneck, especially for employees visiting from other sites, and potentially also for customers and business partners.

In view of transformative business trends, adding supplementary premises for coaching or continuing professional development (CPD) purposes could be another value-adding contribution. The need for employee training and continuing education is likely to grow, especially in the automotive sector and ancillary segments. With bundled competencies in a variety of technology-related fields, technology parks could play a key role in the delivery of technology-focused professional or vocational training courses by providing suitable venues.

Adapting premises and facilities to meet trends such as co-working, Cloud-working or New Work/Workplace 4.0 could also reinforce the parks' ability to attract and retain technology companies in the future. The flexible design of technology-park buildings already provides excellent conditions for co-working and could be further developed in terms of digital infrastructure.

As a matter of course, any proposal for future technology-park development should also include the possibility of extending parks physically onto other sites. In particular, an effective strategy should ensure that the concept is sustainably aligned with local geographical and environmental conditions, and that the park's ongoing development is tailored to local strengths. This may involve, for example, adapting the concept to focus on specific industries, size of site, integration into existing research and campus networks, and other factors. To date, this has proven to be an effective strategy.

New workplace concepts

Today, technology parks are already giving us a fairly accurate picture of how we will be working tomorrow. The most future-proof solutions are those with flexible premises and services that can easily be adapted to user needs.

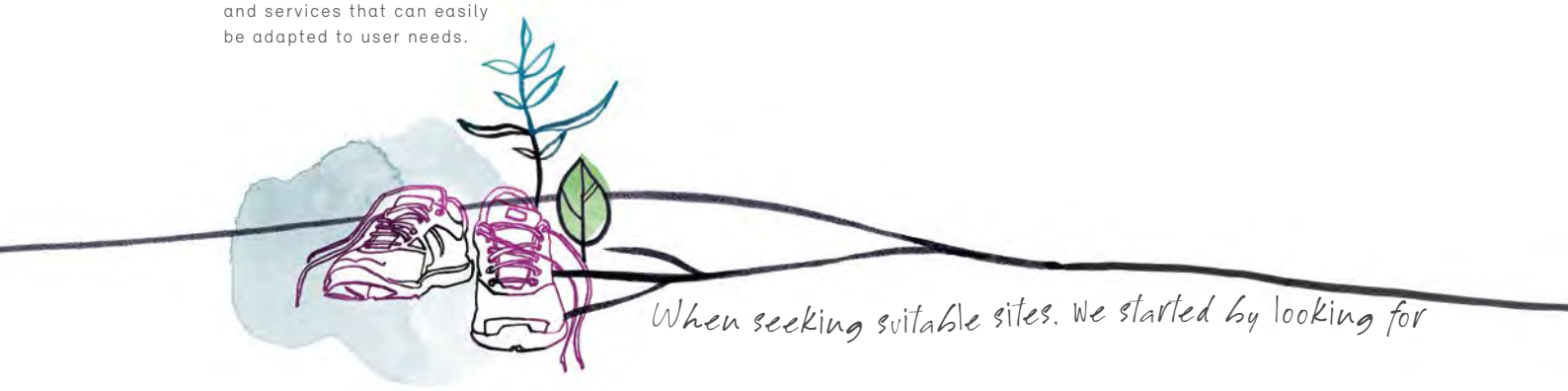
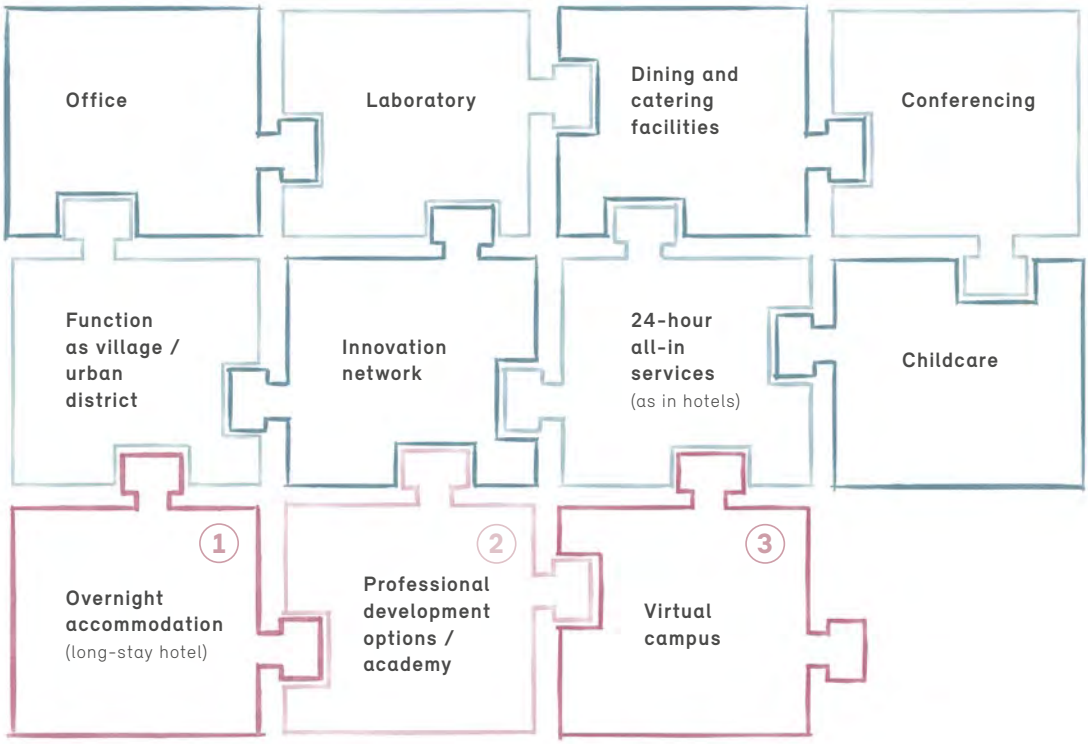


Figure 4

Mix of functions at L-Bank technology parks with options for further development

Bundling of functions at an L-Bank technology park



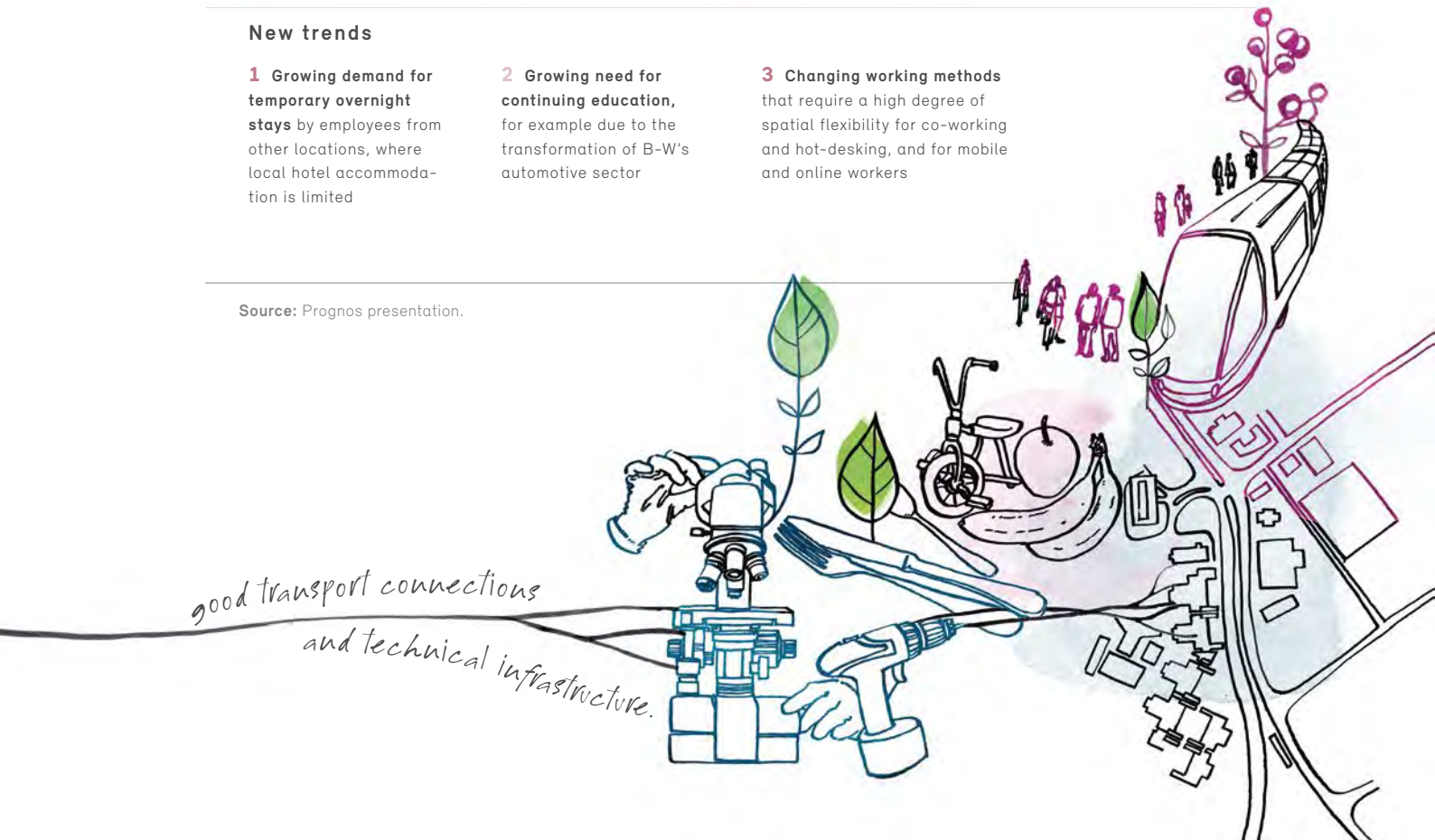
New trends

1 Growing demand for temporary overnight stays by employees from other locations, where local hotel accommodation is limited

2 Growing need for continuing education, for example due to the transformation of B-W's automotive sector

3 Changing working methods that require a high degree of spatial flexibility for co-working and hot-desking, and for mobile and online workers

Source: Prognos presentation.



TPMA –
Mannheim Technology Park

As a new centre of medical technology, the technology park provides ideal conditions for generating synergies between companies, hospitals, universities and researchers. And at 6,500 square metres, there is plenty of space for ground breaking ideas.

Pre-screening of potential sites and sites under investigation

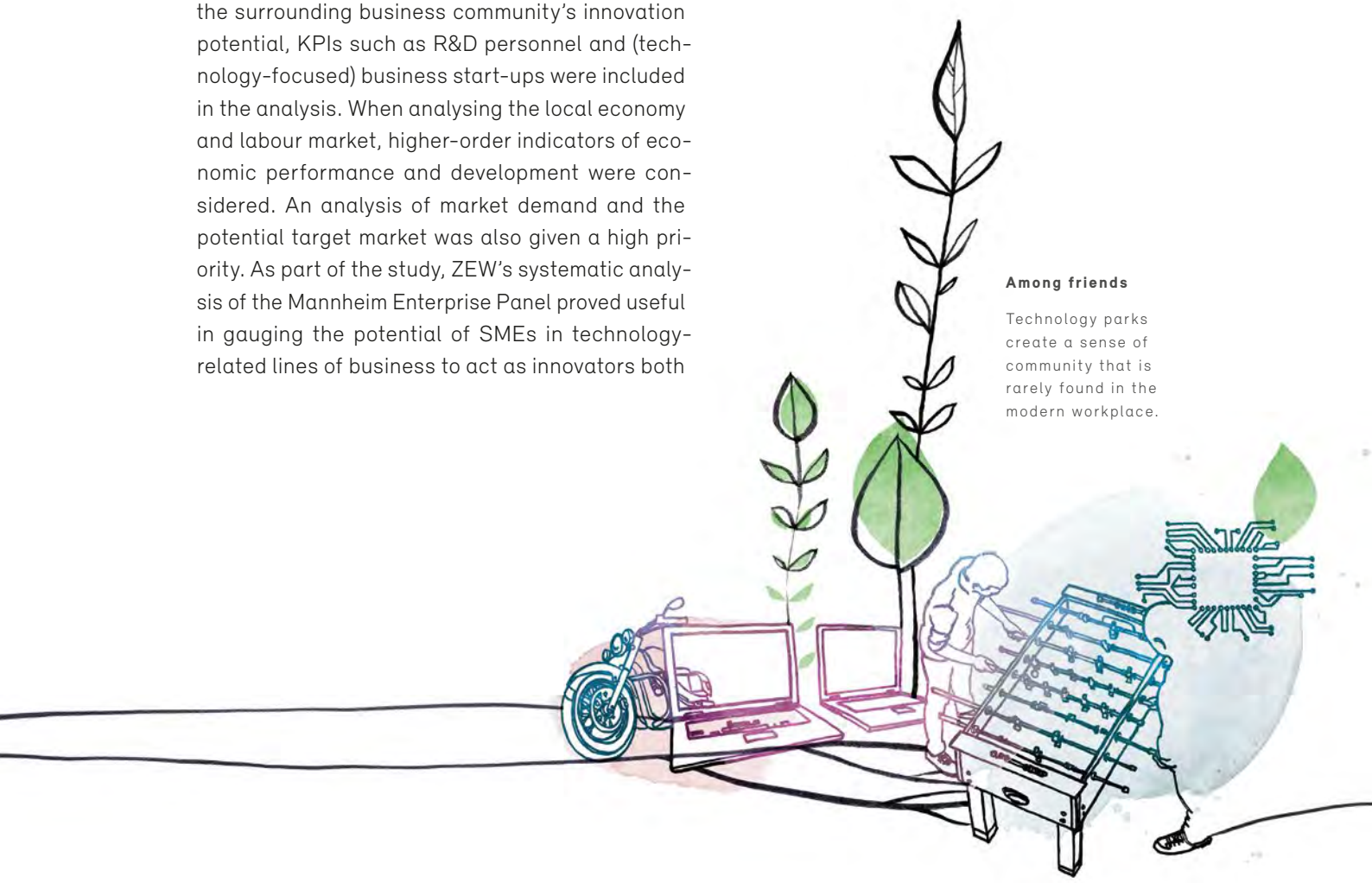
To narrow down potential locations for new technology parks, university and technical college locations were selected for further investigation as potentially suitable sites. Based on the experience of the existing technology parks, university towns are a good starting point. In each case, nearby universities and related institutions have contributed to the parks' success, acting as central hubs of research activity. Consequently, other university towns in Baden-Württemberg were also included in

For us, personnel development is a bottleneck.

the shortlist of locations for further investigation. These included Heidelberg (in the Rhine-Neckar region), Ulm, Constance and Friedrichshafen (home to Zeppelin University, a private institution).

But the investigation was not limited to university towns. In view of the strengths of universities of applied sciences in terms of applied research and partnerships with business, the team also selected towns and cities hosting technical universities for closer examination, to check their suitability as potential sites for L-Bank technology parks. In total, five universities of applied sciences were included in the next stage of the analysis (Heilbronn, Aalen, Pforzheim, Villingen-Schwenningen and Ravensburg-Weingarten).

Comparative analysis of nine potential sites was initially carried out using clearly defined indicators of research and innovation potential. To rank the institutions by research excellence, the team used key potential indicators (KPIs) such as student numbers and STEM focus. To gauge the surrounding business community's innovation potential, KPIs such as R&D personnel and (technology-focused) business start-ups were included in the analysis. When analysing the local economy and labour market, higher-order indicators of economic performance and development were considered. An analysis of market demand and the potential target market was also given a high priority. As part of the study, ZEW's systematic analysis of the Mannheim Enterprise Panel proved useful in gauging the potential of SMEs in technology-related lines of business to act as innovators both in Baden-Württemberg and in the specific locations under investigation. Finally, certain aspects of the local real-estate and rental markets were included in the analysis. This was based on a simplified breakdown of office rents that focused on rental prices in the higher-value market segment in which L-Bank's technology parks naturally belong. The following table provides an overview of the relevant KPIs in the four areas of analysis used in this comparative study of potential locations. This combination of areas of analysis and KPIs is useful for illustrating and evaluating the key conditions required for technology-park sites, and for establishing the relevant success criteria.



Among friends

Technology parks create a sense of community that is rarely found in the modern workplace.

Table

Overview of key potential indicators broken down by area of analysis

Subject matter	Area of analysis	Indicators
Research excellence	**Research and innovation potential**	Student density
		Proportion of STEM students
		R&D personnel in business
		Start-up activity
Economic strength	**Economy and labour market**	Employee development
		Proportion of highly qualified employees
		Job density
		Employees in potential technology-focused sectors and as a proportion of all employees
Technology focus	**Market demand and potential target markets**	Number of companies with high focus on technology/innovation/as a proportion of SMEs (separate ZEW analysis of Mannheim Enterprise Panel)
		Employees in companies with high focus on technology/innovation/as a proportion of all employees in SMEs (separate ZEW analysis of Mannheim Enterprise Panel)
Infrastructure status	**Real-estate and rental market**	Office-space rents, segment, good location

Source: Prognos presentation.

We could have found alternatives, but they wouldn't have been modern enough for us.

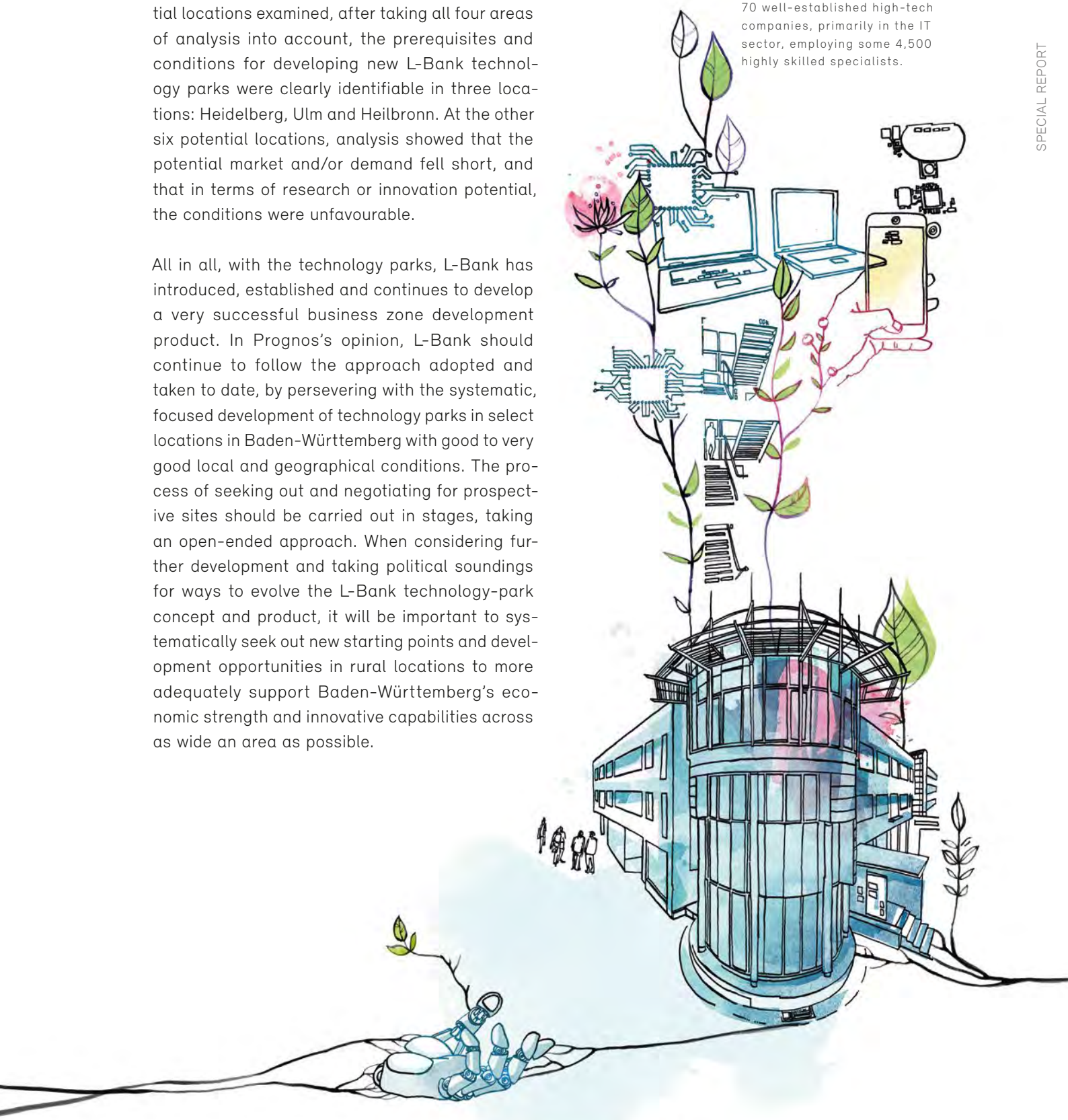
Overall assessment and proposed locations

In the final overall assessment of the nine potential locations examined, after taking all four areas of analysis into account, the prerequisites and conditions for developing new L-Bank technology parks were clearly identifiable in three locations: Heidelberg, Ulm and Heilbronn. At the other six potential locations, analysis showed that the potential market and/or demand fell short, and that in terms of research or innovation potential, the conditions were unfavourable.

All in all, with the technology parks, L-Bank has introduced, established and continues to develop a very successful business zone development product. In Prognos's opinion, L-Bank should continue to follow the approach adopted and taken to date, by persevering with the systematic, focused development of technology parks in select locations in Baden-Württemberg with good to very good local and geographical conditions. The process of seeking out and negotiating for prospective sites should be carried out in stages, taking an open-ended approach. When considering further development and taking political soundings for ways to evolve the L-Bank technology-park concept and product, it will be important to systematically seek out new starting points and development opportunities in rural locations to more adequately support Baden-Württemberg's economic strength and innovative capabilities across as wide an area as possible.

TPK – Karlsruhe Technology Park

The first L-Bank-financed technology park was opened in 1996. Today, the ten-hectare site is home to around 70 well-established high-tech companies, primarily in the IT sector, employing some 4,500 highly skilled specialists.



Interview with Tobias Koch

'Support for innovation should not stop at funding.'

Innovation thrives in Baden-Württemberg. According to the latest analysis by the State Statistical Office, Baden-Württemberg ranks first out of 86 regions in the European Union. Attractive financing options for start-ups and SMEs are a major reason for this ranking. But other factors should also be kept in mind. On behalf of L-Bank, **Tobias Koch, Maike Fliessbach-Schendzielorz** and **Melanie Reisch** from the **economic research institute Prognos** evaluated the Bank's technology parks.

Mr Koch, what's your view of Baden-Württemberg from an 'innovation' perspective?

Tobias Koch: Baden-Württemberg is one of the leading business and innovation hubs in Germany and Europe. This is due to the presence of large enterprises in the state, but also to its well-established, broad-based 'Mittelstand' in the form of small and medium-sized 'hidden champions'. In recent years, however, innovation by SMEs in Germany and Baden-Württemberg has been declining, whereas expenditure on innovation by large companies has shown above-average growth over the same period. What's more, SMEs are having to cope with growing uncertainty in the form of structural, market-related and technological change, and the challenges associated with disruptive transformation. Typical drivers of change include developments in mobility technology, new drive technologies, digitisation, and all the uncertainties resulting with the slowdown in global trade, not to mention new trade barriers caused by, for example, Brexit. The problem is, compared to large companies with in-house R&D departments, SMEs have significantly fewer human and financial resources to devote to innovation.

Where do you see a need for action?

Tobias Koch: In view of the particular challenges facing SMEs, the increasing complexity of innovation processes, and the growing pressure both to innovate and also control costs in view of international competition, the importance of smooth, coordinated collaboration between research institutions and the business community – as well as between companies – is greater than ever.

What role could L-Bank technology parks play here?

Tobias Koch: For more than 20 years, L-Bank has been extending its 'business zone development' offering by selectively leasing building and laboratory space to young companies in the Bank's own technology parks. In terms of local context, target market and building structures, each technology park is geared to different target markets and demand profiles so they can better support the development and consolidation of regional strengths as well as specific areas of competence. They're deliberately located in knowledge-focused university towns. And the Bank's approach has been successful in both quantitative and qualitative terms: The parks are working at full capacity, and in many areas the companies there are highly innovative and play a central role in developing the federal state's leading growth industries.

How would you rate the technology parks' prospects?

Tobias Koch: L-Bank's technology parks are a building block for strengthening Baden-Württemberg's competitiveness as a business hub. And they've only just started to fulfil their potential. There are plenty of exciting development opportunities for the existing parks, and plenty of highly promising potential new sites.

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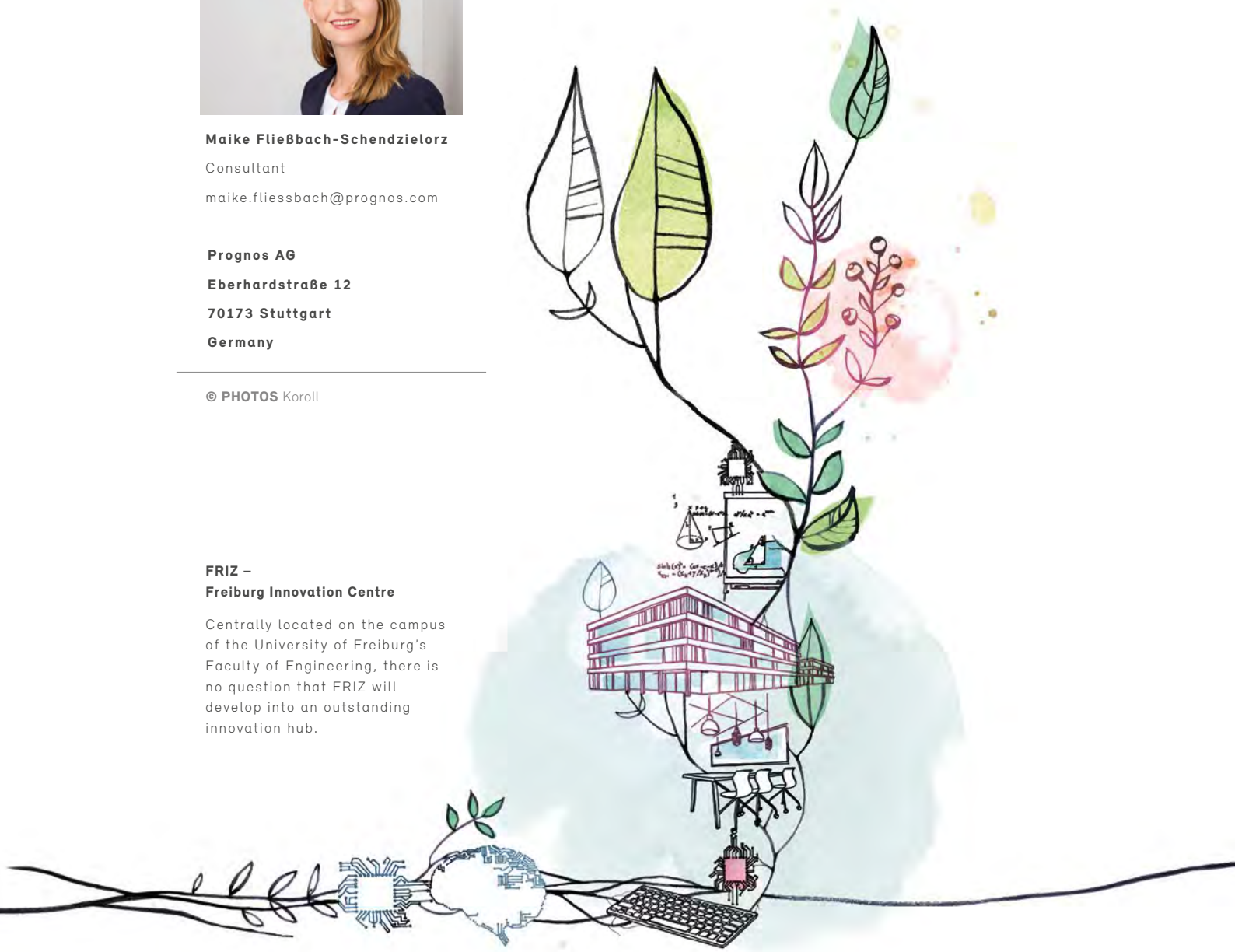


FRIZ –
Freiburg Innovation Centre

Centrally located on the campus of the University of Freiburg's Faculty of Engineering, there is no question that FRIZ will develop into an outstanding innovation hub.

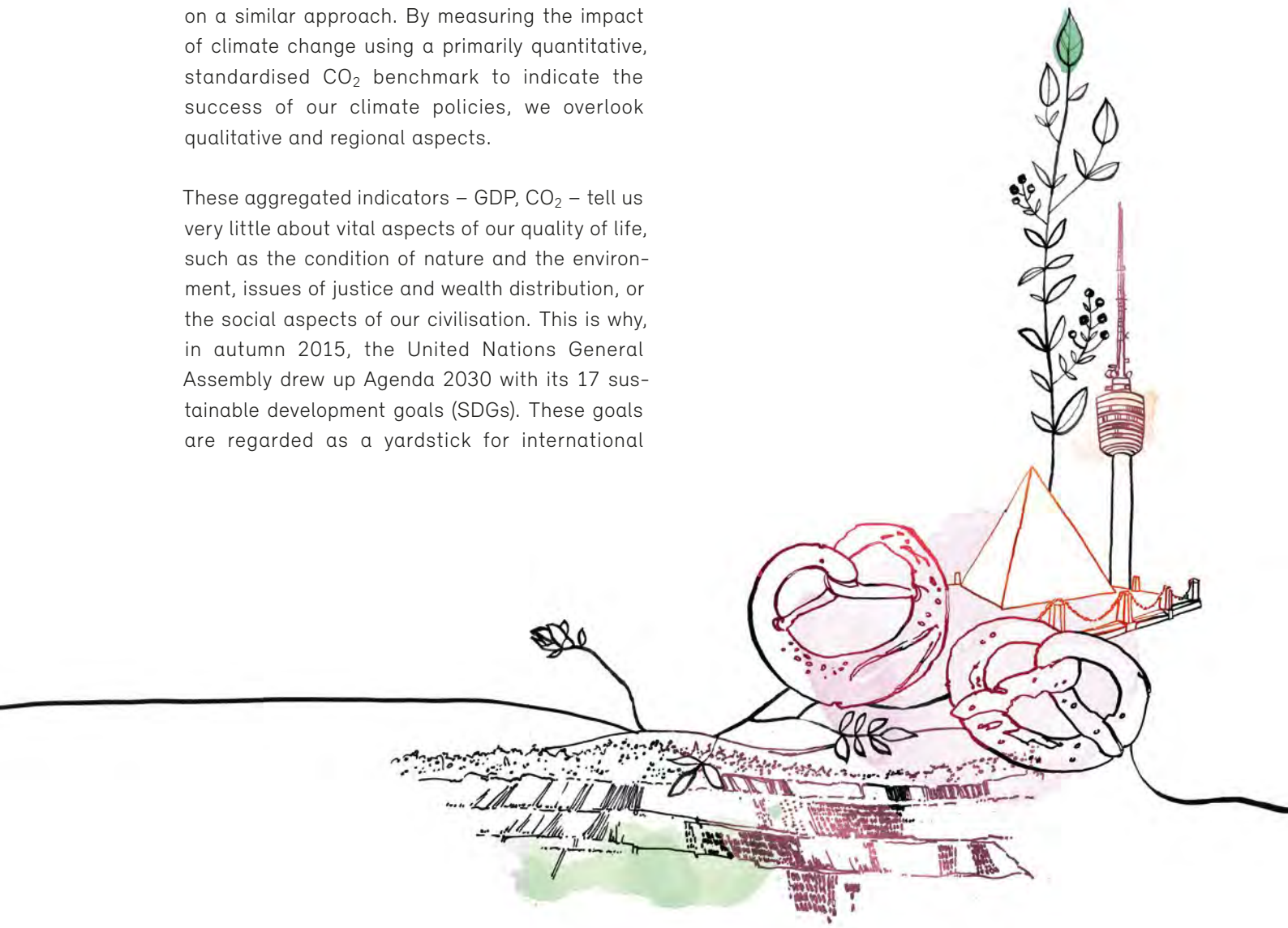
A development bank dedicated to Baden-Württemberg's welfare*

*Prosperity

Strong, stable economic development is the foundation of our prosperity – hence also L-Bank's primary development priority. Welfare, however, means more than the continuous growth of gross domestic product (GDP). The introduction of GDP as a measure of economic performance was groundbreaking. It represents the total value of all products and services produced or provided within the boundaries of a given economy in the course of a year. However, it only records transactions that have a market price, so does not take account of, for example, the cost of exploiting natural resources. On the contrary, any expenditure required to alleviate environmental damage actually increases GDP. Thus by basing our prosperity benchmark on a figure reflecting the sum total of an exclusively economic calculation, we simplify the complexity of the world around us – but in doing so, overlook certain vital aspects. Climate policy is based on a similar approach. By measuring the impact of climate change using a primarily quantitative, standardised CO_2 benchmark to indicate the success of our climate policies, we overlook qualitative and regional aspects.

These aggregated indicators – GDP, CO_2 – tell us very little about vital aspects of our quality of life, such as the condition of nature and the environment, issues of justice and wealth distribution, or the social aspects of our civilisation. This is why, in autumn 2015, the United Nations General Assembly drew up Agenda 2030 with its 17 sustainable development goals (SDGs). These goals are regarded as a yardstick for international policymaking. At the same time, the importance attached to these goals and the urgency with which they are being implemented vary from one country to another.

According to Section 3 (1) of the L-Bank Act, L-Bank's development finance activities should be entirely focused on providing broad support for the State of Baden-Württemberg as the latter fulfils its public duties, especially in terms of structural, economic and social policy. This means that the Bank's development activities were expected to meet a broad range of objectives from the outset. It would be just as inappropriate to focus the Bank's development instruments exclusively on quantitative economic growth as it would be to focus solely on a specific target for reducing carbon emissions.

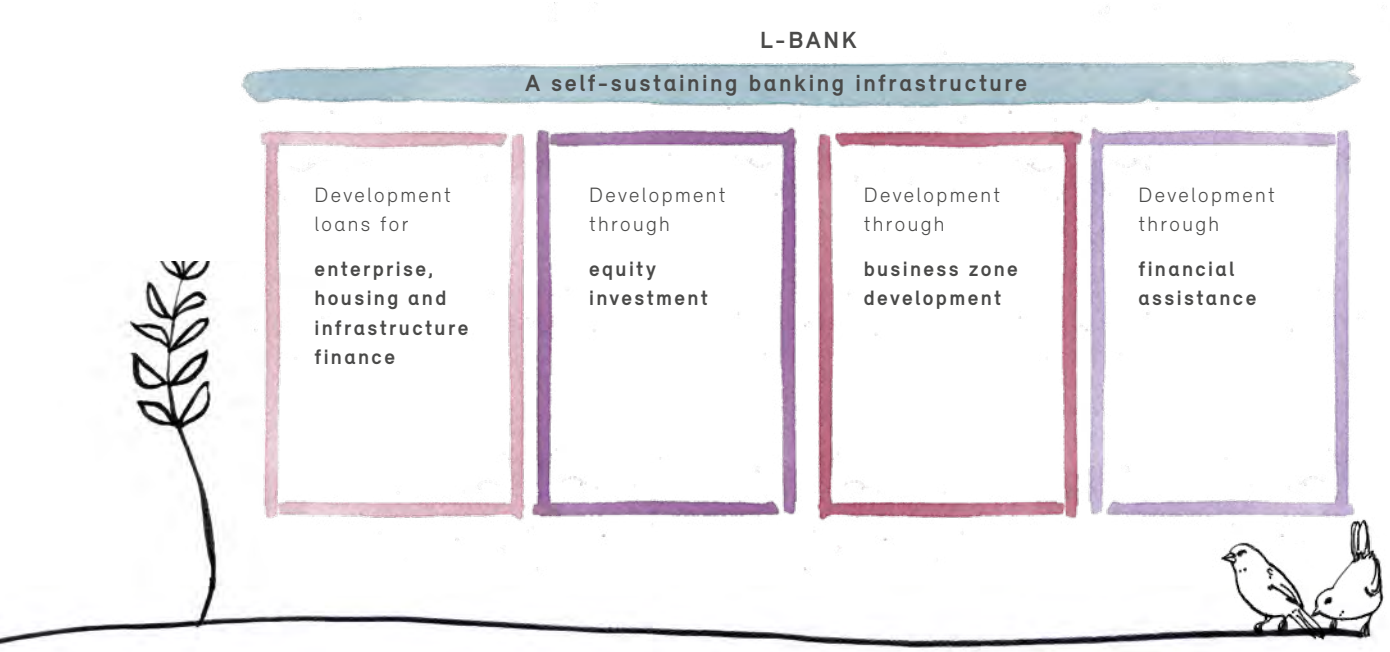


Broadly diversified, well positioned: L-Bank's development finance instruments

Our development activities are based on our 4-pillar model. We help the state government to shape Baden-Württemberg's future by providing development loans for financing business, housing and infrastructure projects, by funding enterprise development through equity investment, by developing business zones and by providing support in the form of financial assistance. Year after year, we use these instruments to provide more than 160,000 clients in Baden-Württemberg with the development services they need. The development loan remains the most important and – as an economic stimulus – most potent instrument in our toolbox. But the services we provide to ministries by managing grants and subsidy programmes are also an important part of our development portfolio.

L-Bank's 4-pillar model

Thanks to our banking infrastructure, we are a key partner to the State of Baden-Württemberg.



With a wide variety of instruments at our disposal, we are able to adapt our actions to current circumstances. The range of options available to us is broad, extending from development projects with long-term objectives through to emergency aid. Of course it is also important to decide which deficits to eliminate or which stimuli to apply. Where it makes sense to put pressure on costs, development loans or grants are the best way to provide efficient support. Where there is a need to boost capital availability or accessibility, we can help by providing guarantees or equity capital. This is also where our technology parks play a role – by providing access to networks and research facilities, and by providing ancillary services that allow firms to concentrate on their core business.

Development finance works – but only if it takes account of changing circumstances.

From paying out family allowances to supporting enterprise development, L-Bank's services are broadly diversified. The Bank has spent EUR 8.26 billion for Baden-Württemberg through a variety of very different projects.

Which factors influence the selection, weighting and design of the individual projects? Among them are political requirements such as the prioritisation of individual funding objectives, macroeconomic developments and the implementation of specific operational requirements and structures.

The urgency of climate-policy action is largely undisputed. At the political level, the issue of climate change has become even more compelling since the Paris Convention in December 2015, when 195 countries signed up to a broad-based, legally binding, global climate-protection agreement and action plan to limit global warming to well below 2 °C. We support the state government's initiatives through our environmental-protection programmes, which, like our Resource Efficiency Finance programme, are demonstrating the effectiveness of a multisectoral approach across different lines of business.

The current economic slowdown is the result of a combination of cyclical and structural factors. The cyclical dip has coincided with structural challenges that are further impeding growth. Overcoming ongoing disruptive changes driven by all-embracing digitisation and the transformation of our entire system of mobility – involving, among other things, a complete rethink of vehicle technology – is vitally important for the long-term prospects of Baden-Württemberg's economy. This is why we must focus on further structural development rather than economic stimuli. With our Digitisation Premium and Innovation Finance programmes, we are addressing this issue by creating stronger incentives for companies to break new ground. Market interest rate levels represent an important benchmark for the cost-conscious design of our development programmes. Today's low interest rates are obliging us to rethink our approach – especially since we are highly unlikely to see any increase in interest rates in the immediate future. Indeed, with the economy expected to weaken further in 2020, the ECB may take further steps towards negative interest rates in order to boost macroeconomic demand. Such a negative rate would result in even longer maturities and affect more areas of activity than before. In addition to interbank business and public-sector lending, it could also have a growing impact on enterprise development and housing construction loans.

Taking negative interest rates into account in our development finance programmes represents an enormous technical and legal challenge. As a result, we are maintaining an intensive dialogue with KfW and other state development institutions. L-Bank has launched an in-depth study into how development loans could provide adequate subsidy incentives even in the event of persistently low or negative interest rates. We can see various possible ways of doing this, with negative interest rates on development loans as just one possible option. For example, L-Bank has been working for some years now with repayment subsidies or rebates linked to development loans. At the moment, this means we can offer development instruments on attractive terms even without negative interest rates.

Development loans

Traditional development loans – the core instrument in L-Bank's development activities – are used to boost investments in business, housing and infrastructure. To arrange the loans, we rely primarily on the 'borrower's bank' approach, although we do grant direct loans in areas such as housing construction and for special clusters such as our MikroCrowd development programme.

Allocation of development loans

Total volume: EUR 4,914 million

Focusing on the client

The borrower's bank approach enables us to provide comprehensive advice and support, and enables clients throughout Baden-Württemberg to access our development loans. Our funding partners' well-established client relationships, based on trust between bank and end-borrower, allows us to distribute development loans without having our own branch network. In 2017, we set up an expert portal to provide our partners with digital support; around 700 experts are now active on the portal. The platform provides our partners with daily updates on programme modifications and conditions, as well as comprehensive answers to questions about our development funding options. To make it easier for specific user groups to navigate the portal, we have created separate information channels for the Bank's various target markets – financing partners, financing intermediaries, state housing development agencies and multipliers. Even so, personal contact is and remains important to us. In our on-site training courses, we tell our financing partners all about the latest developments and clarify the various ways in which our programmes can be used. In the regions, we also organise 'bank breakfasts' every six months, at which we – together with Bürgschaftsbank/ Mittelständische Beteiligungsgesellschaft and RKW Baden-Württemberg – present new development finance concepts. In 2019, we reached out to some 600 of our funding partners' corporate client advisers, department managers and board members at these events.

To ensure that end-clients are well prepared before they talk to their own banks, we have been organising financing advisory days for many years, in close cooperation with local Chambers of Commerce. Over the last two years, to meet the needs of all those who are already well prepared and want more detailed funding information as quickly as possible, we have set up a supplementary video advisory service in conjunction with a large number of Chambers of Commerce, using a videoconferencing system to link up experts from Bürgschaftsbank and L-Bank. We held 29 videoconferences in 2019, during which we were able to provide immediate answers to questions concerning business start-ups, self-employment and corporate finance.

We are also testing ways of providing a digital advisory service for our home ownership programmes. In a pilot project with the state housing development agency in Heilbronn, agency staff can directly involve L-Bank experts in their online advisory sessions with clients. While the project is still at the pilot stage, we are only providing this facility for online discussions of private home ownership programmes. If it becomes clear that digital advisory sessions are accepted by users and generally suitable for social home ownership support, we plan to extend the service to state housing development agencies in other regions.

In the rental accommodation segment, personal, on-site advice is especially important. In addition to making regular visits to regional building societies, we organise training sessions for housing associations and municipal decision makers. Supplementary roadshows organised by the Bank familiarise clients with the full range of development options available for rental housing.

Equity

The financing ecosystem established by Baden-Württemberg's public sector around the Ministry of Economic Affairs, L-Bank and Mittelständische Beteiligungsgesellschaft (MBG) specifically addresses the needs of start-ups, business founders and corporate successors, supporting SMEs at different stages in their development. The transition from loans to equity capital is fluid. The high proportion of guarantees linked, for example, to development loans under our Start Finance 80 programme, acts as a kind of 'venture credit' in the low-volume segment.

New commitments associated with L-Bank's SME and venture capital activities are made via the LEA Mittelstandspartner fund (assets: EUR 200 million) launched in spring 2016 or the LEA Venturepartner fund launched the following year (assets: EUR 60 million).

Managed by experts

The funds are managed by LEA Partners which, as an entrepreneurial equity partner, helps the start-up and management teams of innovative companies to grow and achieve leading market positions. Since 2002, LEA Partners has managed investments in more than 40 companies, totalling over EUR 300 million.

Technology parks

Our traditional technology-park sites have established themselves in the marketplace. The first building in our Mannheim Technology Park (TPMA) was ready for occupation in August 2019 and is already fully tenanted. Similarly, our other parks have no further vacancies and are fully occupied. By the end of 2019, some 250 companies employing more than 11,000 people were established in L-Bank's technology parks. Most companies in the parks experience growth, demonstrating their ability to transform technological ideas into entrepreneurial success.

Technology parks set a sophisticated benchmark.

L-Bank operates this line of business without subsidies, at the Bank's own construction and operational risk, applying free-market principles in a financially limited, revolving system. The maximum investment volume is EUR 180 million. Flexible office and laboratory units in university towns are rented to technology-focused (fledgling) companies that have just emerged from the start-up phase. The Bank's technology parks are designed as a long-term business-park concept with successive development stages, differing from private

or municipal real-estate providers in terms of price levels, their focus on specific target markets, and flexible space and service offerings. The sale of the properties is considered from the outset, as are any commercialisation opportunities for local third parties. This applies in particular to the local real-estate market. The presence of superregional investors (funds, pension companies, asset managers) and institutional investors is an important criterion when identifying potential sites for technology parks.

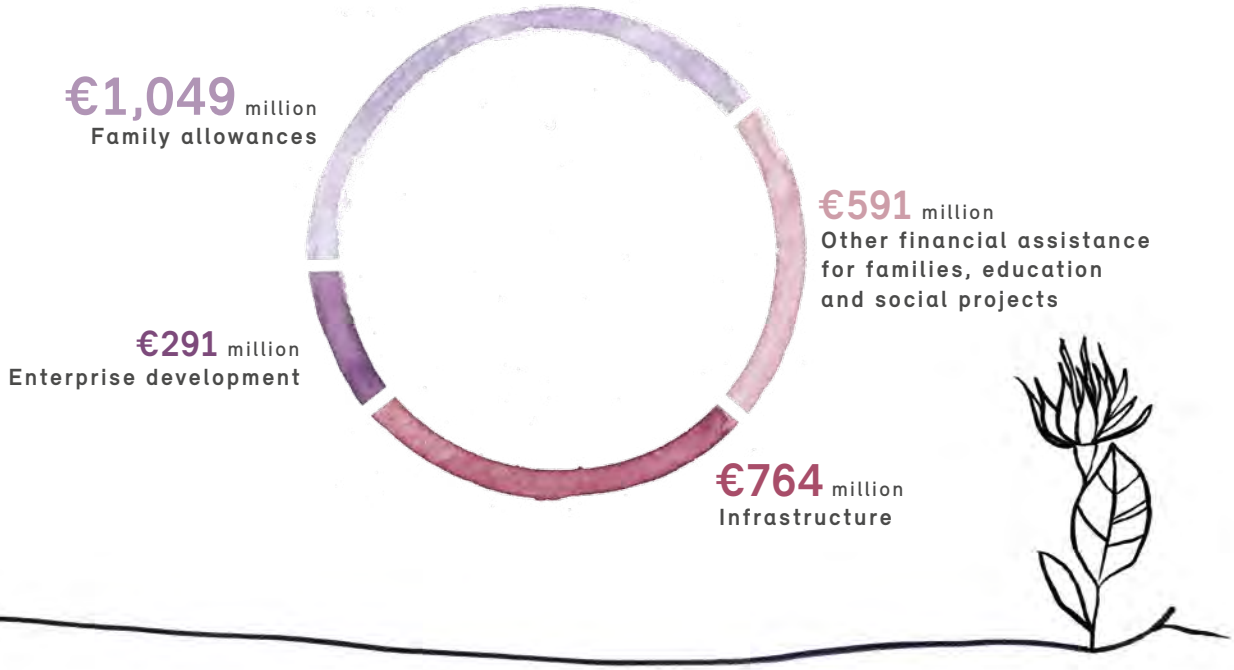
Financial assistance

L-Bank is a key player in a large number of development programmes involving the distribution of financial assistance. We act as a development services provider, allocating state, federal and EU funds through a total of more than 100 financial assistance programmes. The growth of our financial assistance activities shows how attractive our service is.

Funding objectives range from family-policy incentives through to environmental protection initiatives. They include such diverse areas as family allowances; funding for static, grid-connected battery storage systems linked to newly installed photovoltaic panels (ideal for reducing the load on power distribution grids and increasing the efficiency of the electricity supply chain); subsidies for purchases of electric cargo bikes to support the transition to eco-friendly modes of transport; and language teaching for kindergarten children in need of extra assistance to learn German.

Distribution of financial assistance

Volume of financial assistance in 2019: EUR 2,696 million – 2018: EUR 2,718 million



service-bw.de integrated into funding infrastructure

A common feature of all programmes is that L-Bank's grant funding is provided by the federal state, or by third parties under the terms of a specific engagement. By agreement with the funding body, L-Bank – using its institutional development finance infrastructure – takes over partial or complete implementation of the funding process in return for a cost-covering contribution to administrative expenses. From advising on, reviewing and approving applications, right through to disbursing funds, we act in accordance with the federal state's wishes. Wherever possible, we work closely with the state's own administrative resources, thereby ensuring that funds are disbursed with the lowest possible administrative overheads.

The digital transformation of the federal state's administrative mechanisms is an essential starting point for the effective provision of financial assistance. E-files and e-government are key elements in the modernisation of public-sector administration. Setting up the service-bw.de joint service portal for all state agencies and municipalities is an important milestone in this respect. This portal is intended to provide seamless access to as many administrative services as possible, thereby establishing a central interface between citizens and administration. For L-Bank, implementing the online application process for family allowances acted as a useful pilot project for working with this administrative portal. By integrating the service-bw.de portal into our service provision, we are supporting the state's digitisation efforts and leveraging our joint IT synergies.

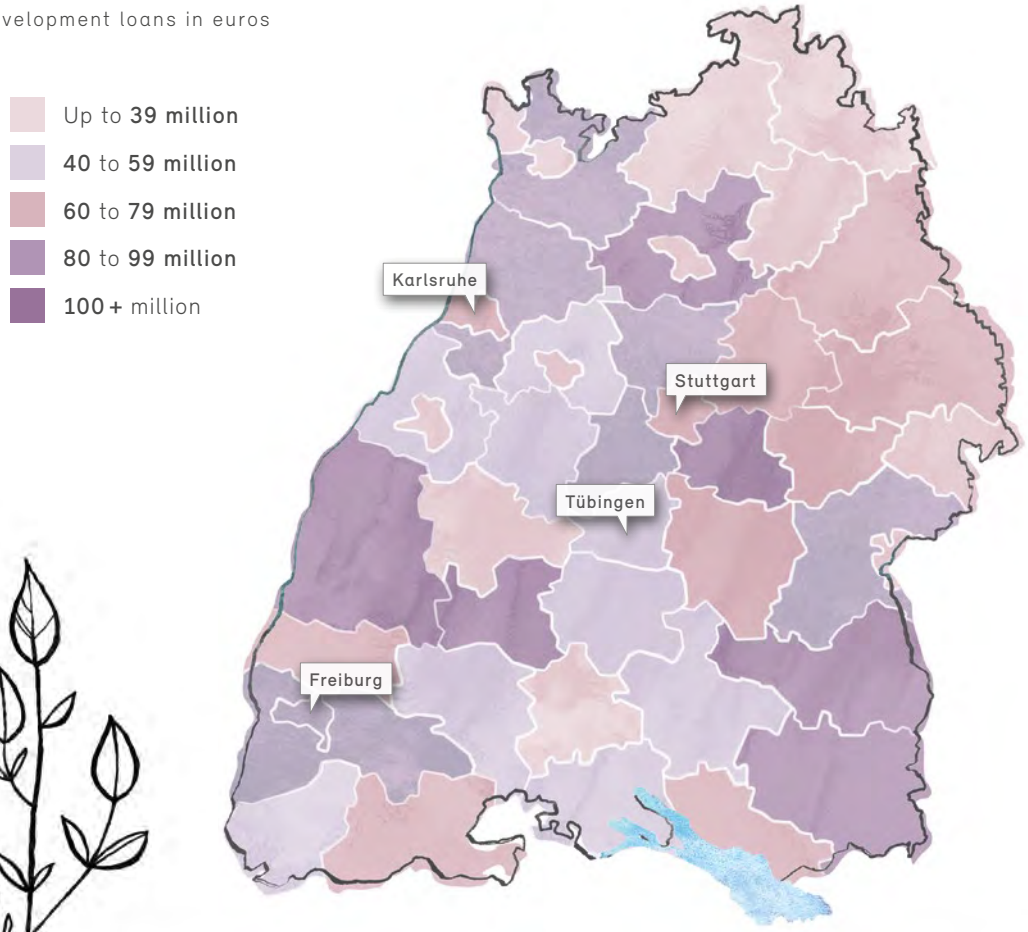
Support for business

The current forecasts for global economic development suggest that any growth in 2020 will be moderate. Growth rates of less than one per cent are also expected for Baden-Württemberg. Cyclical slowdowns in certain areas of activity are exacerbated by an economy in transition. For the necessary structural transformation processes to succeed, the economy must regain its dynamism and initiative. Fresh ideas are required, along with the courage to take new approaches. It is important to assist businesses to make structural changes, but also to generate new stimuli by encouraging start-ups.

L-Bank's enterprise development takes all these requirements into account. Over the last five years, we have contributed more than EUR 16 billion to the development of companies in Baden-Württemberg. To ensure the stability and continuity of long-term business development, we have made appropriate adjustments to our development programmes.

Regional distribution of enterprise development finance

Development loans in euros

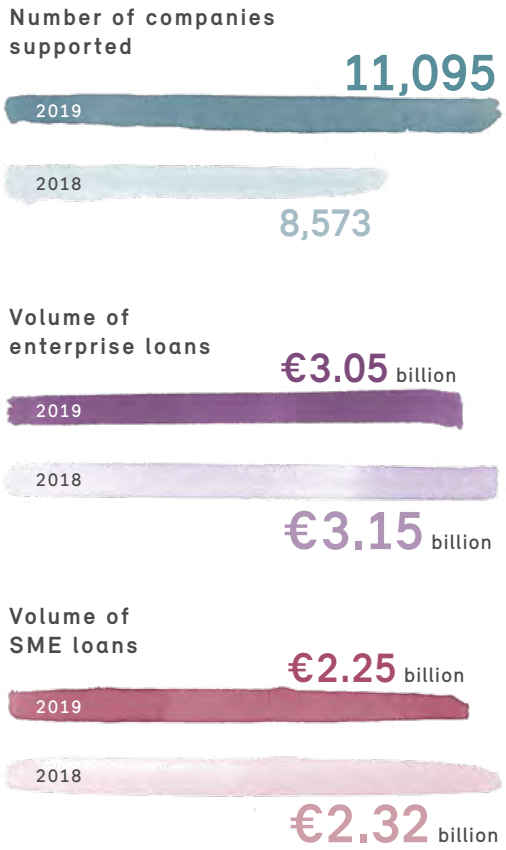


Development loans are a cost-effective financing method

By offering development programmes that help companies to increase their commercial leverage, we can achieve a much broader economic impact. We encourage companies to embrace structural change by offering targeted transformation incentives, for example through our Resource Efficiency Finance programme, Digitisation Premium and Innovation Finance programme. Our start-up development finance also aims, on the one hand, to improve the general conditions for launching start-ups and corporate successions, while on the other hand, specifically attempting to support the implementation of new ideas.

Scope of enterprise development

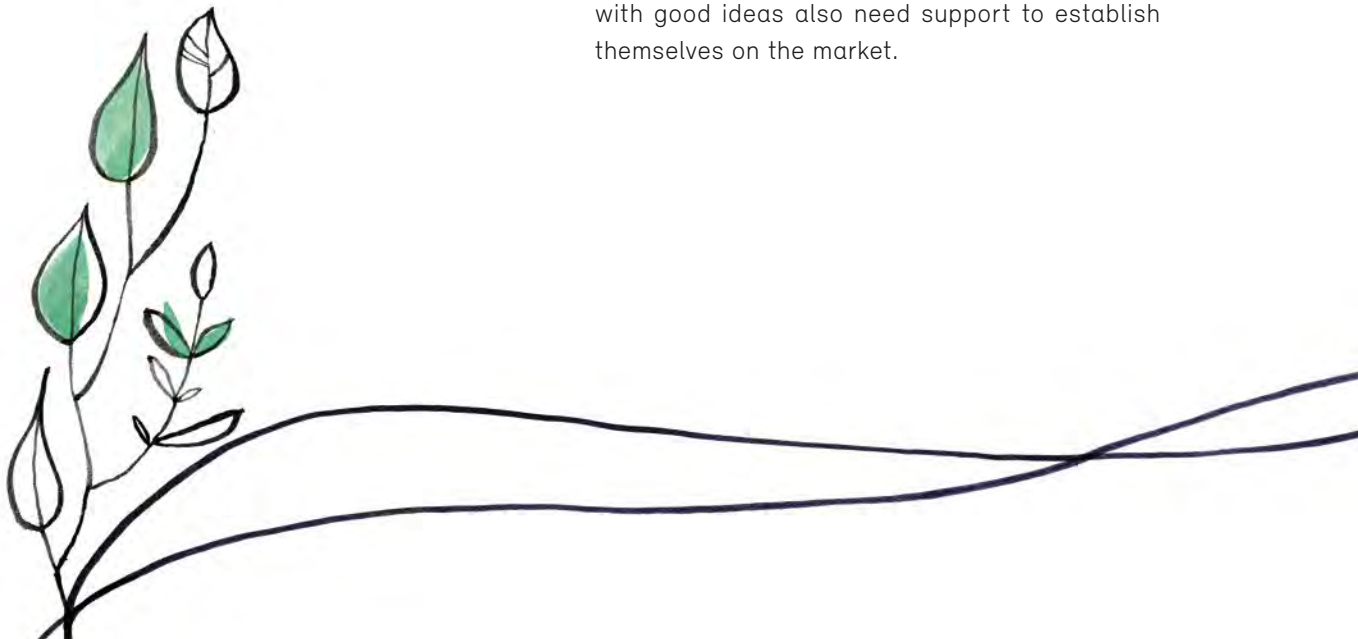
Compared to the previous year in each case



Innovation is our future

The strength of Germany's south-west lies in the breadth of innovation and synergies between all those involved. We are well positioned: The innovation index calculated by the State Statistical Office identifies Baden-Württemberg as the region with the highest innovative capability in the European Union by a wide margin. For this to remain the case, we must ensure that development is balanced. The Digitisation Premium and Innovation Finance programme in particular have an enormously broad impact. The Digitisation Premium aims to help small and medium-sized enterprises (SMEs with up to 100 employees) in all sectors to cope with the digital transformation. Funding is available for projects that introduce new digital solutions or improve IT security in SMEs. The digitisation of the economy in particular represents a huge opportunity for SMEs in Baden-Württemberg, by helping them to streamline processes, introduce new products and services, and implement innovative business models. And with our Innovation Finance 4.0 programme, L-Bank supports projects of particular significance for the future viability and competitiveness of companies in Baden-Württemberg.

When implementing new ideas, it is often helpful to have a solid capital foundation and a well-established network – both of which many SMEs already have. If the corporate structures are right, exciting opportunities for launching innovative projects can arise. But SMEs are not the only corporate partners who can count on us: Start-ups with good ideas also need support to establish themselves on the market.



Volume:
Digitisation Premium

Compared to the previous year

Volume:
Innovation Finance

Compared to the previous year

And sometimes it takes the best of both worlds: the highest possible degree of freedom for new ideas, embedded in a resilient commercial network – ideally, the kind of thing successors can expect when taking charge of an existing company.

Corporate successors – an underestimated innovation driver

It is precisely this pillar of innovation that will demand our undivided attention over the next few years. Succession often provides the vital stimulus required to implement fresh ideas in established companies, encouraging them to develop further within established structures while rethinking their strategies where necessary. However, this pillar of our innovation system is shaky because corporate succession in SMEs has lost some of its appeal. Not only does this hamper the pace of innovation, it also jeopardises the substance of the business itself, the networks it has developed, and the customer and supplier relationships that are so important to the flexibility of Baden-Württemberg's economy.

This is why the opportunities associated with corporate succession must be brought even more sharply into focus: Succession in SMEs offers exciting prospects. The new management can count on an experienced team, a good market position and a solid customer base. Operating procedures are already in place, and there is plenty of scope for building on existing orders, meaning that start-up risks can often be minimised. One hurdle, however, is the initial capital required.

Even smaller SMEs with just 25 employees are often valued at over one million euros. As a rule of thumb, and depending on the industry, business valuations are based on sales multiples of between 0.7 and 1.3. So it is important to ease the entry barriers for successors by offering attractive financing options. Not least because, as a rule, they will not only need funding to engage with their new remit, but also because their fresh ideas are often predicated on an ambitious strategic rethink that requires additional investment.

Volume of business start-up finance

Compared to the previous year

Our business start-up finance is also open to corporate successors – who are among the most active in taking it up: More than one third of our loans are used to finance successions.

Access to venture capital

In many cases, development loans are a cost-attractive way of financing new projects. But they are not always the first choice. Finance for growth or for high-tech projects, where product development needs very long lead times before it starts to generate revenues, is associated with risks that make it impossible to rely exclusively on loan finance. Such long-term projects are dependent on equity capital. In recent years, we have reorganised L-Bank's equity finance offerings so that we can make a more substantial contribution to such projects. New commitments associated with L-Bank's SME and venture capital activities are made via the LEA Mittelstandspartner fund launched in spring 2016 and the LEA Venturepartner fund launched the following year.

L-Bank deliberately became a minority shareholder in both funds from the outset. In both cases, L-Bank acts as the anchor investor. Further capital was raised from the private sector, with the aim of leveraging the Bank's own funds. The LEA Mittelstandspartner fund has made seven investments to date, with the result that almost three quarters of the available funding of EUR 200 million has already been drawn down.

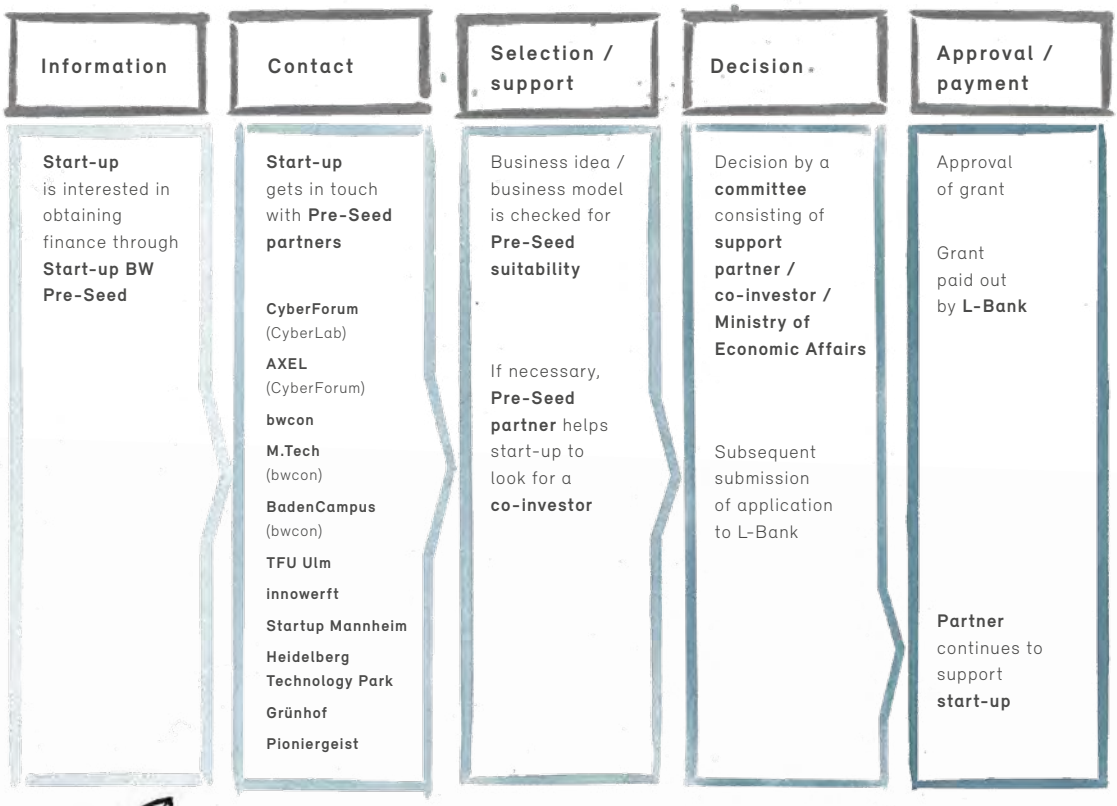
The LEA Venturepartner fund's closing subscription reached EUR 60 million. The acquisition of understand.ai by the German technology group dSpace was the fund's first successful exit.

Our Start-up BW Pre-Seed programme kicks in at an even earlier stage. Many innovative business ideas fail in the earliest stages of implementation due to a lack of funding. Institutional investors are reluctant to act during this early phase because of the higher risks involved and uncertainties surrounding the project's prospects of success. The Start-up BW Pre-Seed programme aims to support such projects on their way to financing maturity. To supplement the financial support provided by the State of Baden-Württemberg, Pre-Seed partners (regional incubators) help pre-seed start-ups to develop their business models and build up their companies. Pre-Seed partners also help them to find the right co-investors.

Since we launched Start-up BW Pre-Seed in December 2018, 62 start-up projects have already passed through the selection process and received funding commitments totalling around EUR 13.2 million.

Start-up BW Pre-Seed

Start-up BW Pre-Seed: steps on the way to development funding

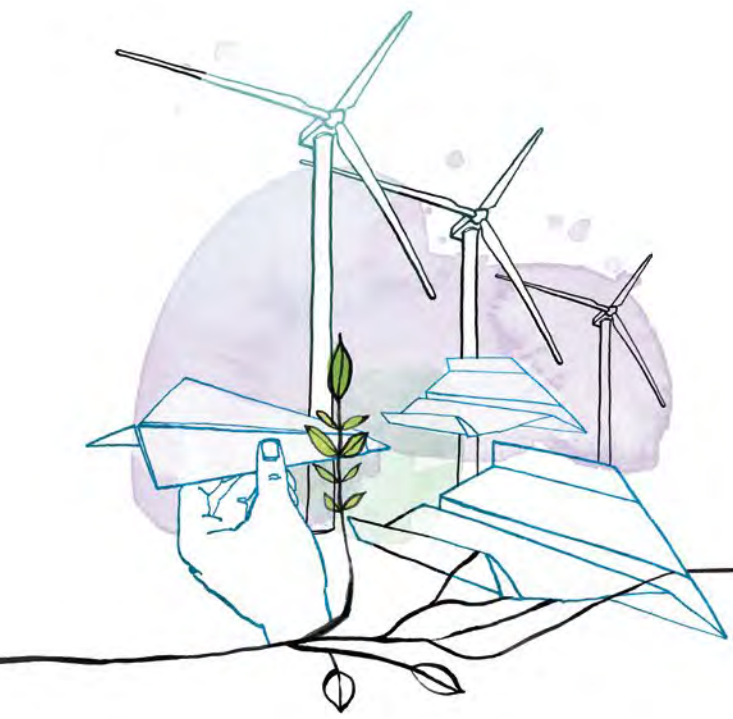


Source: Baden-Württemberg Ministry of Economic Affairs, Labour and Housing.

Technology parks are the entry ticket to innovation networks.

Our technology parks are owned by L-Bank's real-estate subsidiaries. They manage the technology parks according to commercial and economic criteria. Karlsruhe Technology Park (TPK), Stuttgart Engineering Park (STEP), Tübingen-Reutlingen Technology Park (TTR) and Mannheim Technology Park (TPMA) make a range of buildings available to technology-focused companies specialising in various areas. For example, the outstanding USP of TPMA, which was set up in the previous year, is the geographical concentration of companies, hospitals and research institutions specialising in medical technology, all located within walking distance of each other. This means that medical products can be developed faster and more efficiently here than elsewhere.

Our latest project, the Freiburg Innovation Centre (FRIZ), is also making progress. The land is available; the building application has been submitted. This will add another member to our growing family of technology parks. But there is plenty of development work on our existing sites: Further construction projects are being planned in Reutlingen and Karlsruhe.



No two ways about it: Financial aid has a direct impact.

Grants are often the first choice for funding narrowly defined objectives.

Financial assistance for business

Compared to the previous year

In the right, precisely defined circumstances, it is possible to engineer systematic changes in behaviour – using, for example, the BW e-voucher (BW-e-Gutschein). Businesses that make deliveries can use the e-voucher to claim up to EUR 5,000 back on the costs of e-vehicle maintenance and charging infrastructure. This represents an additional e-mobility incentive. Between the programme launch in December 2018 and the end of 2019, we approved 1,322 applications.

Support for housing

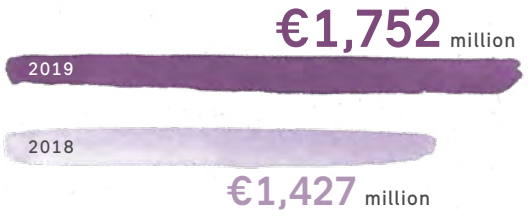
The lack of affordable housing is not merely an urban problem – it has also spread into rural areas. In technical terms, this means that rents and incomes have become decoupled.

The current shortage of affordable housing has its origins in misjudgements of the housing market situation back in the 1980s and 1990s. At the time, it was assumed that declining population figures would cause demand on the housing market to drop. As a result, both publicly subsidised and private housing construction efforts were stepped down. The forecasts failed to adequately anticipate the growing trend towards single-person households and the accelerating rural exodus in certain parts of the federal state. The results are reflected in the current housing deficits: According to the Prognos study proposed by the Baden-Württemberg Housing Alliance in 2017 and subsequently commissioned by L-Bank, housing demand rose by 4.6 per cent (215,000 residential units) between 2011 and 2015, whereas the housing supply increased by just 2.5 per cent (128,000 residential units). The result is a cumulative housebuilding shortfall amounting to 88,000 'missing' residential units. Subsequent demographic shifts have underscored the need for action: Since then, Baden-Württemberg's population has grown again, exceeding the figure of 11 million for the first time – with no signs of slackening. This means that between 410,000 and 485,000 residential units must be built in Baden-Württemberg by 2025.

The Baden-Württemberg Housing Alliance commissioned L-Bank to organise a new study to analyse the current specifics of the federal state's local housing markets. The F+B research institute in Hamburg presented the preliminary results of the study at a top-level meeting of the Housing Alliance on 14 October. The principal aim of the study was to identify those housing markets in the federal state's various regions which are under particular strain. Based on five indicators, 88 municipalities were identified as particularly affected.

Volume of lending in the housing development sector

Compared to the previous year



Home ownership assistance

Owner-occupied housing is a cornerstone of the housing market. A comparison of the European Union's member states reveals clear differences in home ownership profiles: Germany is at the bottom of the league in this respect. If we include the non-EU countries in Europe, only Switzerland has a lower home ownership ratio. Although Baden-Württemberg is at the forefront of Germany's federal states, residents do not take sufficient advantage of the opportunities for individual wealth creation and old-age provision offered by

home ownership. Home ownership also stabilises existing housing structures and, especially in rural areas, represents a commitment to the region. Investments in housing stock thus have a positive impact on infrastructure in cities, towns and villages throughout the state.

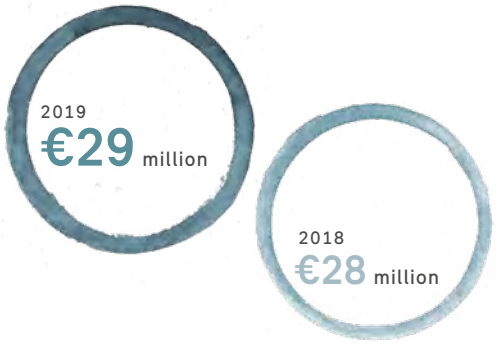
Volume of state housing assistance for home ownership

Compared to the previous year

L-Bank's home ownership development programme – especially important for families with children – provides successful incentives for the purchase of owner-occupied residential property. To support the growing financing needs of families in the state and encourage the construction of affordable housing, L-Bank's housing development programme has been supplemented by the 'Combined Home Loan' programme. The new development programme, designed as a top-up supplement for the Bank's 'Living with Children', 'Energy-efficient Construction' and 'Energy-efficient Renovation' programmes, closes the funding gap that can arise as a result of the funding ceilings in the above-mentioned programmes, further strengthening L-Bank's home ownership efforts. This year, the state housing development programme has continued the successful development arc observed in past years, attaining the same high levels of demand and funding as in the preceding year. In addition to the sharp drop in interest rates in the summer, excess demand on the real-estate market also caused a slight decline in the number of applications received.

Volume of homeowners' association funding

Compared to the previous year



Volume of state housing assistance for rental housing construction

Compared to the previous year

Homeowners' associations

Support for homeowners' associations is an integral part of L-Bank's housing development activities. The Bank's aim is to modernise the energy efficiency of residential building stock in Baden-Württemberg and improve the age-appropriate utilisation of residential properties. Last year, demand for the programme was as stable as in the previous year.

Rental accommodation finance

Support for rental housing makes a substantial contribution to providing low-income households with affordable housing. It complements offerings available on the free housing market.

We are continuing to see a turnaround in rental accommodation funding for social purposes in Baden-Württemberg. In 2019, development applications were submitted for around 2,600 residential units, nearly 2,100 of which related to new-build projects. In 2019, we once again exceeded – by a substantial margin – the barely acceptable minimum threshold of 1,500 residential units per year identified as the breakeven point in the Prognos report. Thus the state housing development programme is successfully counteracting any further decline in the social housing stock.

The provision of protected social housing is supplemented by initiatives at various levels. In addition to social housing development programmes at state level, these include – among other things – support for individuals through instruments such as housing benefits and legal provisions governing residential tenancy rights.

Support for families, education and social projects

Issues associated with families, education and social affairs are multifaceted – as are our programmes. For example, we support on-the-job training of nursery school teachers by paying out lump-sum training allowances; our Hummingbird and Sparrow language support programmes help kindergarten children with their language development, and our Homework, Language and Learning aids help to integrate children into the German school and education system by teaching them German language skills. But we also support municipalities with integration officers and provide development funding for building schools.

Volume of financial assistance for families, education and social affairs

Compared to the previous year

The distribution of family allowances remains by far the largest single item. When family allowances were introduced in 2007, Baden-Württemberg's state government decided that the programme would be administered centrally by L-Bank. At the same time, suitable conditions were put in place for the ongoing development of the existing standalone administrative processes which the Bank was already using to distribute federal and state education allowances.

Since then, L-Bank, as the federal state's central provider of development finance services, has been helping to optimise the use of family allowances through its service centre and accompanying information services, and by ensuring that decision-making and settlement processes are fast and efficient. More than 290,000 telephone consultations conducted by our Family Support Service Centre underscore the breadth of our support for parents in Baden-Württemberg. And our administrative processes also work well: Despite the increasingly complex work involved in assisting with and processing applications, and the growing number of applications due to the higher birth rate, the average processing time (approx. 30 days to first decision) is unusually short compared to the federal average.

To achieve this, we have optimised online applications. For at least two years previously, the application process in Baden-Württemberg was supported by a form-filling wizard. After answering a series of questions, applicants could print out and sign the application form and send it to L-Bank together with the necessary supporting documentation. Around one-third of applicants used this hybrid approach to make their applications. Now L-Bank has taken another significant step towards optimising digital interactions with clients. Working closely with the Ministry of Social Affairs and in partnership with the Ministry of the Interior, we have implemented a full online application system for family allowances. The new system is connected to L-Bank's existing processes, which are efficient and cutting edge. The key to further development of the already partially automated process was the integration of service-bw.de's service account into the application procedure. The ongoing digital development of the family allowance system complies with the provisions of Section 1 of the law for improving online access to administrative services (Online Access Act – OZG), which obliges both federal and state governments to provide their administrative services via administrative portals by the end of 2022. The service-bw.de portal is Baden-Württemberg's technology platform for online services, benefiting citizens, companies and state government agencies alike.

The new online family allowance application system has been available to users since April 2019. Applicants are guided through the online application process step by step. They can interrupt the process at any time, in which case their data is temporarily stored. As soon as they have finished entering all the information, applicants are given their own service-bw.de service account, where they will find their personalised application documents plus a list of supporting documentation to be submitted with the application.

This simplifies the process for applicants, but also benefits Baden-Württemberg's online service. Because there are so many applicants, the family allowance is effectively acting as a catalyst for the state's administrative portal – it is so user-friendly, young parents find the platform equally attractive for dealing with other administrative services (lock-in effect).

In 2019, L-Bank approved more than 152,000 family allowance applications on behalf of the state: three per cent more than in the previous year. Acceptance of electronic applications via the service-bw.de administration portal – and the leveraging of this opportunity to rationalise the process – is making excellent progress: After just nine months, almost 45 per cent of applications are now submitted online.

Volume of family allowances

Compared to the previous year

DEVELOPMENT FINANCE BY BUSINESS SEGMENT: 1 JANUARY TO 31 DECEMBER 2019

DEVELOPMENT FINANCE ACROSS ALL LINES OF BUSINESS	VOLUME OF COMMITMENTS	COMMITMENTS	
	4,913,975,897.94	**23,290**	
	VOLUME OF COMMITMENTS	COMMITMENTS	RESIDENTIAL UNITS*
HOUSING DEVELOPMENT	**1,751,561,543.46**	**11,083**	**16,149**
Home ownership assistance	**934,120,760.17**	**10,012**	**7,333**
Home Ownership Finance – BW including finance for growing families – Structured loans (state housing development)	305,336,597.17	2,002	1,454
Top-up and miscellaneous loans	119,985,600.00	940	
Living with Children	314,681,000.00	5,574	5,574
Living for the Future	6,890,163.00	215	275
Combined Home Loan	185,408,700.00	1,255	
Other programmes	1,818,700.00	26	30
Rental accommodation assistance	**788,069,441.28**	**810**	**5,488**
Rental Accommodation Finance – BW – New builds – MW15/MW25 (state housing development)	332,438,300.00	136	2,083
Rental Accommodation Finance – BW – Approval of regulated tenancies (state housing development)	18,032,900.00	323	513
Rental Accommodation Finance – BW – Modernisation (state housing development)	37,286,228.00	55	798
Rental Accommodation Finance – L-Bank – New builds	105,161,600.00	78	648
Rental Accommodation Finance – L-Bank – Modernisation	58,236,289.38	61	1,446
Top-up loans (new builds/modernisation)	236,914,123.90	157	
Support for homeowners' associations (state housing development)	**29,371,342.01**	**261**	**3,328**

* The total includes multiple counting, as the various home ownership finance programmes may be combined in certain cases.

	VOLUME OF COMMITMENTS	COMMITMENTS
INFRASTRUCTURE DEVELOPMENT	**115,509,880.00**	**175**
Municipal investment loan, direct	72,224,250.00	96
New Energy – Community wind farms	13,285,630.00	76
Other financial instruments	30,000,000.00	3

	VOLUME OF COMMITMENTS	COMMITMENTS	COMPANIES
ENTERPRISE DEVELOPMENT	**3,046,904,474.48**	**12,032**	**11,095**
Business start-up finance	**643,684,311.20**	**2,779**	**2,518**
Start Finance 80	56,248,604.00	835	823
Start-Up Finance	574,795,707.20	1,885	1,636
Pre-Seed Finance Grant	12,640,000.00	59	59
SME finance	**2,246,613,163.97**	**8,654**	**8,033**
Growth Finance	614,906,915.26	1,973	1,788
Local Transit Finance	16,708,500.00	404	169
Tourism Finance	4,100,000.00	4	4
Liquidity loans	42,696,850.00	231	225
Investment Finance	323,953,106.32	399	291
Rural Area Development programme	65,853,680.93	361	351
Resource Efficiency Finance	654,197,774.49	425	396
Direct loans and syndicated finance	77,000,000.00	12	8
Surety and guarantee programme/ Sureties for refinancing loans	16,765,614.00	12	10
Loans to associated companies	30,000,000.00	2	2
Refinancing of associated companies	1,550,000.00	7	6
Innovation Finance	277,446,450.80	476	443
CPD Finance	4,344,000.00	21	21
Digitisation Premium	116,970,272.17	4,314	4,306
Microfinance	120,000.00	13	13
Agricultural development finance	**156,606,999.31**	**599**	**544**
Agricultural Liquidity Assurance BW	475,000.00	4	4
Agricultural Growth	64,965,087.31	397	363
Loans for environmental and consumer protection, sustainability, new forms of energy	56,827,952.00	165	148
Working capital loans – Growth in the agri-food industry	34,338,960.00	33	29

Corporate Governance Report 2019

L-Bank, in its capacity as the State of Baden-Württemberg's development bank, has a statutory remit to support the federal state in the performance of its public duties and, in doing so, to implement and manage various development initiatives. A sound and responsible approach to corporate governance is a natural component of the Bank's approach to these non-commercial activities. L-Bank has incorporated the Public Corporate Governance Code of the State of Baden-Württemberg into the Bank's standard operating procedures by resolutions of both the Board of Management and Supervisory Board, and observes all the prescriptions of the latest valid version of the Code. This Corporate Governance Report covers fiscal year 2019; the following declaration applies in full as at the reporting date, 31 December 2019.

Declaration of compliance

The Board of Management and Supervisory Board of L-Bank declare that:

We have observed, and continue to observe, the recommendations of the Public Corporate Governance Code of the State of Baden-Württemberg (PCGK BW) to the extent that such recommendations apply to L-Bank in its capacity as a public-law institution, with the exception of the following recommendation.

Audit of annual financial statements: entrusting audit procedures to persons previously involved in the audit (margin note 107 PCGK BW)
As part of the framework agreement for the 2019–2022 annual audits concluded once again between L-Bank and PricewaterhouseCoopers GmbH in the course of the fiscal year, an audit team will be set up in which persons already involved in the audits will continue to be entrusted with audit engagements in the future. The fact that audit team members are replaced after five years of team membership nevertheless ensures that professional independence and audit quality are maintained, thereby complying with the fundamental intention of the regulation.

Proportion of women on the Board of Management and Supervisory Board, and in executive management positions

As at 31 December 2019, one woman was represented on the four-strong Board of Management. As at the reporting date, five of the 18 members of the Supervisory Board (27.8%) and 74 of the 221 employees in executive management positions (33.5%) were women.

Remuneration paid to members of the Board of Management and Supervisory Board

REMUNERATION PAID TO MEMBERS OF THE BOARD OF MANAGEMENT FOR 2019 in EURk

Name	Membership period	Fixed remuneration	Other non-cash benefits	Payments from third parties in relation to Board of Management activities	Total
Dr. Axel Nawrath Chair	01.01.–31.12.	682	25	8	714
Dr. Ulrich Theileis Vice-Chair	01.01.–31.12.	525	27	25	577
Dr. Iris Reinelt	01.01.–31.12.	425	29	9	464
Johannes Heinloth	01.01.–31.12.	425	25	5	455
Total		**2,057**	**107**	**47**	**2,211**

An occupational pension scheme is in place for members of the Board of Management based on the rules applicable to L-Bank employees.

REMUNERATION PAID TO MEMBERS OF THE SUPERVISORY BOARD FOR 2019 in EURk

Name	Membership period	Membership of Supervisory Board	Membership of committees	Attendance fees	Total
Edith Sitzmann[1)] Chair	01.01.–31.12.	9.0	14.0	2.1	25.1
Dr. Nicole Hoffmeister-Kraut[1), 2)] 1st Vice-Chair	01.01.–31.12.	7.5	5.3	1.1	13.9
Franz Untersteller[1), 3)] 2nd Vice-Chair	01.01.–31.12.	6.7	2.4	0.6	9.7
Dr. Jürgen Bufka	01.01.–31.12.	6.0	–	0.6	6.6
Dr. Maximilian Dietzsch-Doertenbach	01.01.–31.12.	6.0	12.9	2.0	20.9
Martin Gross	01.01.–31.12.	6.0	2.6	0.9	9.5
Manuel Hagel	09.07.–31.12.	2.9	–	0.2	3.0
Roger Kehle	01.01.–31.12.	6.0	–	0.5	6.5
Gabriele Kellermann	01.01.–31.12.	6.0	8.1	1.4	15.5
Andrea Lindlohr	01.01.–31.12.	6.0	–	0.6	6.6
Rainer Reichhold	01.01.–31.12.	6.0	–	0.6	6.6
Professor Dr. Wolfgang Reinhart	01.01.–31.12.	6.0	–	0.3	6.3
Dr. Florian Stegmann[1)]	01.01.–31.12.	6.0	5.8	0.8	12.5
Thomas Strobl[1)]	01.01.–04.07.	3.8	4.8	0.9	9.5
Harald Unkelbach	01.01.–31.12.	6.0	2.4	0.8	9.2
Joachim Walter	01.01.–31.12.	6.0	–	0.5	6.5
Clemens Meister	01.01.–31.12.	6.0	–	0.8	6.8
Barbara Bender-Wieland	01.01.–31.12.	6.0	–	0.8	6.8
Thomas Dörflinger	01.01.–31.12.	6.0	–	0.6	6.6
Total		**113.9**	**58.3**	**15.6**	**187.8**

1) Subject to a duty of surrender to the State of Baden-Württemberg.
2) Appointed as first Vice-Chair with effect from 09.07.2019.
3) Appointed as second Vice-Chair with effect from 09.07.2019.

The Board of Management The Supervisory Board

Management Report – Report of the Board of Management of L-Bank for fiscal year 2019

Background

Landeskreditbank Baden-Württemberg – Förderbank (L-Bank) is the development bank of the German federal state of Baden-Württemberg. The Bank has its head office in Karlsruhe, with a branch office in Stuttgart. L-Bank is wholly owned by the State of Baden-Württemberg and, as a public-law institution, is subject to the supervision of the federal state government. With effect from 27 June 2019, L-Bank withdrew from the Single Supervisory Mechanism (SSM) and thus from direct supervision by the European Central Bank (ECB) as the result of a corresponding amendment to the Capital Requirements Directive (CRD). It has since been supervised by the Federal Financial Supervisory Authority (BaFin) in cooperation with Deutsche Bundesbank. As expected, this has not resulted in any material change to the applicable substantive banking supervisory legislation.

The Bank's business activities are governed by its statutory remit, namely to support the state government of Baden-Württemberg in the fulfilment of its public duties, especially in terms of structural, economic and social policy, by implementing development programmes that comply with European Union (EU) regulations governing state aid. L-Bank's development goals and operational targets – such as the Bank's target clients and development priorities – are determined by the Bank's owner in accordance with the provisions of the L-Bank Act, relevant political priorities and, with respect to activities relating to development programmes, the specific terms of each individual programme. Consequently, L-Bank's main business activities are largely influenced by external factors and can therefore only be controlled by the Bank to a limited extent.

Economic Report

Basic parameters

For the time being, Germany's sustained economic upswing has come to an end. Although 2019 saw the country's economy grow for the tenth time in succession, real gross domestic product (GDP) only increased by 0.6% (2018: 1.5%). The economy's momentum slowed considerably in the course of the year. After growing strongly in the first quarter, up by 0.5% on the previous quarter, the German economy only narrowly avoided a technical recession in the two subsequent quarters, with growth rates of –0.2% and +0.2%, respectively. Even in the final quarter of 2019, the economy failed to build any new momentum (growth rate: 0.0%). The current downturn is primarily affecting the industrial sector, which, as sales and orders decline, is now in a recession brought about by developments in global economic policy and far-reaching structural changes.

This contrasts with Germany's domestic economy, which is still robust. The construction industry continues to act as a growth driver and the development of the service sector is still comparatively stable. This is due mainly to the very good situation on the labour market and the latter's positive influence on private consumption. Thus the average unemployment rate in Germany in 2019 was 5.0% (2018: 5.2%) – the lowest level since reunification. In addition, the positive trend in real wages has continued, thanks to wage increases and fiscal stimuli. This was further enhanced by the direction of the rate of inflation, which at 1.4% fell significantly below the ECB's 2% target due to declining energy prices.

Baden-Württemberg's true strengths – local industry's high contribution to value added, the state's export-oriented economic structure and strong automotive and mechanical engineering sectors – are currently metamorphosing into weaknesses as a result of current political and structural uncertainties. Global political developments such as the UK's withdrawal from the European Union and trade disputes between the USA, China and the EU, have brought about a significant increase in economic uncertainty over the last few years. As a result of these conditions, the dynamism of Baden-Württemberg's export and overseas business has been considerably impaired. Back in 2017, exports were still showing a growth rate of 5%; over the last two years, however, growth rates have fallen below 2%. Furthermore, structural factors such as demographic and technological trends, coupled with political measures to combat climate change, are becoming increasingly important. Over the past year, the heavy impact of all these factors on Baden-Württemberg resulted in significantly below-average economic growth compared to the rest of Germany. According to preliminary figures, Baden-Württemberg's gross domestic product in 2019 did not exceed the previous year's level (GDP growth rate: 0.0%). Towards the end of the year, the economic slowdown also began to have an (albeit minimal) impact on Baden-Württemberg's labour market; the unemployment rate in December was 3.2%, slightly higher than the previous year's figure (3.0%).

Business performance

In 2019, L-Bank's business operations were affected by the low market interest rates. High levels of development funding reflect – on the whole, robust – investment activity by small and medium-sized enterprises (SMEs) in Baden-Württemberg, as well as a consistently high demand for real-estate finance due to the strong construction sector. From the middle of the year onwards, there was a discernible upward trend in demand for development finance.

In enterprise and housing development, the focus of L-Bank's development funding activities remained unchanged. The volume of new business in enterprise development remained high, albeit slightly down on the previous year. Housing development saw a significant increase in new business during the year under review.

Enterprise development

To strengthen Baden-Württemberg's position as a business hub, and to secure local jobs, L-Bank works closely with commercial banks on funding for investment projects by start-ups and established SMEs; the Bank also supports initiatives in rural areas, issuing low-interest loans and subsidies and deliberately assuming risks.

The economic slowdown and geopolitical risks in the year under review also had an inevitable if still minor impact on the level of new business in the enterprise

development sector. Companies showed a declining willingness to invest, as reflected in the lower take-up of individual development programmes. Even so, L-Bank still achieved a high volume of new business in this business segment at EUR 3,338.1 million (2018: EUR 3,568.0 million) – in line with expectations for 2019.

The volume of new start-up financing business rose to EUR 643.7 million (2018: EUR 623.6 million). In particular, L-Bank supported start-ups and fledgling companies with the 'Start-up Finance' programme, which helps them to achieve commercial autonomy, but also to expand and acquire existing companies.

In 2019, established SMEs in Baden-Württemberg received development funding totalling EUR 2,246.6 million through a wide variety of programmes (2018: EUR 2,324.1 million). The 'Resource Efficiency Finance' programme, which provides targeted support for initiatives that encourage the responsible use of resources, continued to be the most popular development programme. The total volume of commitments came to EUR 654.2 million (2018: EUR 628.8 million). The volume of new business in the 'Growth Finance' programme, under which the Bank issues long-term loans for typical SME investment projects on favourable terms, also showed very positive development, increasing significantly to EUR 614.9 million (2018: EUR 361.8 million). In contrast, the demand for funding under the 'Investment Finance' programme showed an appreciable decline. The volume of new business in this programme, which supports business investments in rural areas, fell to EUR 324.0 million (2018: EUR 628.4 million). New business figures for the 'Innovation Finance' programme, which was resumed at the start of 2019, also saw a decline; the total volume of commitments was EUR 277.4 million (2018: EUR 352.1 million). The 'Innovation Finance' programme supports companies that want to introduce innovative business models or finance innovative investment projects. Demand for the 'Digitisation Premium' programme, on the other hand, was extraordinarily high – the funding volume more than tripled to EUR 117.0 million (2018: EUR 28.5 million). The 'Digitisation Premium' programme helps SMEs to finance the digitisation of their processes, products and services. This development shows that companies in Baden-Württemberg are actively addressing the ongoing digital transformation.

In the agricultural development segment, the volume of new business declined to EUR 156.6 million (2018: EUR 204.6 million). In line with the development of the economy as a whole, the increasing reluctance of farmers and agricultural firms to invest made itself felt. On the one hand, demand for the Bank's 'Agriculture – Growth' programme – which supports investments, reduces production costs or helps to improve production and working conditions – once again improved over the previous year, with the result that the lending volume rose from EUR 50.8 million to EUR 64.9 million. On the other hand, this increase could not offset the significant decline of funding volumes under the 'Agri-Food Industry – Environmental and Consumer Protection' programme in particular, from EUR 134.1 million to EUR 56.8 million. The programme supports the reduction of energy consumption and emissions, the processing and marketing of organic products, and improvements in consumer protection.

Housing development

L-Bank uses low-interest loans and subsidies to fund the creation and acquisition of rental and owner-occupied accommodation. By financing modernisation and repair projects, the Bank also facilitates the energy-efficient refurbishment of, and physical access to, existing properties. The volume of new business increased significantly, rising 22.8% to EUR 1,751.6 million (2018: EUR 1,426.7 million) and confounding last year's forecast of a relatively modest increase in new business figures. The high demand for development funding in the year under review is due mainly to the state housing development programme, as well as the 'Living with Children' and 'Combined Home Loan' development programmes. In addition, borrowers' average financing requirements increased due to price trends in the residential real-estate market, which also resulted in higher demand for top-up loans.

The Bank's various programmes in support of rental accommodation help to fund the construction and refurbishment of rental housing in Baden-Württemberg. As expected, this segment once again saw a very high volume of new business. Total financing commitments again rose significantly to EUR 788.1 million (2018: EUR 726.9 million). The positive trend from the previous year continued, especially under the state housing development programme. The volume of loans issued rose by 28.5% to EUR 387.8 million (2018: EUR 301.7 million). This was due in particular to the strong demand for new-build funding. In 2018, the Bank optimised the programme's funding conditions and made them more flexible. The eligibility ceiling for costs was raised, and land costs and construction costs may now be financed separately. The number of subsidised social housing units increased appreciably to 2,598 (2018: 2,219). This enabled L-Bank not just to counteract the decline in the construction of socially contracted housing (formerly approx. 1,500 p.a.), but actually increase the housing stock. In the Bank's own supplementary development programmes for new-build and refurbishment projects, demand showed a slight decline, with total funding commitments of EUR 400.3 million (2018: EUR 425.2 million). As expected, there was positive movement in funding for homeowners' associations for the purposes of energy-efficient renovation or conversion of residential buildings to make them suitable for the elderly. Here, the volume of commitments rose to EUR 29.4 million (2018: EUR 27.7 million).

At EUR 934.1 million, financing commitments under home ownership development programmes were significantly up on the previous year (EUR 672.1 million). The 'Living with Children' programme helps families with children to buy or build their own homes. The volume of new business in this programme rose by 35.9% to EUR 314.7 million (2018: EUR 231.6 million), well in excess of the predicted mild increase in new business. This is due, first, to the new maximum loan ceiling of EUR 100,000 (previously: EUR 50,000) and, second, to the fact that it can be combined with the 'Combined Home Loan' programme, which was launched in mid-2019. This 'Combined Home Loan' programme supplements existing development programmes by covering the additional funding needed to build, buy or renovate owner-occupied housing. Loans totalling EUR 185.4 million were issued in the year under review. Contrary to expectations, the volume of approvals under the state housing development programme fell slightly to EUR 305.3 million (2018: EUR 322.9 million). The ongoing decline in market interest rate levels meant that there was less demand for this programme, whereas the opposite trend in residential property prices drove the demand for top-up finance. Lending commitments increased by 15.8% to EUR 120.0 million (2018: EUR 103.6 million).

Other developments

To strengthen Baden-Württemberg's position as a business centre, L-Bank provides solutions for funding municipal and social infrastructure projects. The Bank also helps the public sector to implement infrastructure projects by providing loans or other forms of finance. In response to increased public-sector demand, the Bank issued a total volume of EUR 1,529.8 million (2018: EUR 1,128.7 million) in funding during the year under review.

Working on behalf of the State of Baden-Württemberg, L-Bank is responsible for distributing and managing a wide variety of financial-assistance services funded from state, federal and EU budgets. In 2019, the Bank processed a total of 15,128 new approvals (2018: 11,068) amounting to a total volume of EUR 1,646.8 million (2018: EUR 1,723.1 million). The highest-volume programmes continued to be school funding (EUR 506.4 million; 2018: EUR 462.4 million) and hospital funding (EUR 434.5 million; 2018: EUR 660.7 million). Financial commitments to water, wastewater, flood protection, decontamination and hydropower projects amounted to EUR 165.7 million (2018: EUR 115.5 million). Approved funding for technology and enterprise development purposes came to a total of EUR 109.6 million (2018: EUR 106.5 million). Urban development finance reached a volume of EUR 104.1 million (2018: EUR 83.3 million). In addition, L-Bank supported families on behalf of the federal and state governments, in particular by distributing family allowances. At EUR 1,049.4 million, the volume of funding approved for family allowances was up on the previous year (EUR 993.5 million) due to rising birth rates and general wage increases.

The bulk of L-Bank's investment portfolio consists of strategic and credit-equivalent shareholdings in companies based in Baden-Württemberg, as well as shareholdings in subsidiaries involved in the regional development of Baden-Württemberg. The book value of the entire portfolio was EUR 238.5 million as at the balance sheet date (2018: EUR 231.2 million).

The book value of strategic investments held by L-Bank on behalf of the State of Baden-Württemberg totalled EUR 180.1 million at year-end 2019 (2018: EUR 178.0 million).

L-Bank participates as a co-investor in SMEs based in Baden-Württemberg. LEA Mittelstandspartner, an external SME fund with EUR 200.0 million in assets (L-Bank stake: EUR 50.0 million) helps established companies, in particular, to overcome the challenges associated with the ongoing digitisation of products and value chains ('Industry 4.0'). The external venture-capital fund LEA Venturepartner (assets: EUR 60.0 million; L-Bank stake: EUR 29.4 million), set up in cooperation with the State of Baden-Württemberg, provides venture capital to technologically strong companies with growth potential. As expected, the volume of investment in external funds increased in the year under review, while the remaining investments in L-Bank's venture-capital portfolio were further reduced as planned. The total book value of the Bank's credit-equivalent shareholdings as at the balance sheet date was EUR 49.5 million (2018: EUR 35.3 million).

Through subsidiaries, L-Bank operates technology and business parks in Karlsruhe, Stuttgart, Tübingen, Reutlingen and Mannheim. Because they are located near universities and research institutions, they assist companies to transfer technology from academia to business by providing conveniently located real estate. These parks differ from other commercial rental premises by the way they are managed and the additional services on offer, which include conference and training facilities as well as nursery and primary schools. As at 31 December 2019, L-Bank provided companies involved in business zone development

with a total of EUR 58.9 million in funding (2018: EUR 75.7 million).

Assets, financial performance and financial position

Financial performance

The following breakdown of operating income helps to clarify L-Bank's financial performance. Transfers to the development fund, which under commercial law should be treated as interest expenses, commission expenses or other operating expenses, are shown here as payments to the State of Baden-Württemberg, hence as an appropriation of profits. Net interest income, which continues to be L-Bank's most important source of income, declined as expected to EUR 302.0 million (2018: EUR 331.4 million). This was due mainly to the ECB's expansive monetary policy and the associated low interest rates.

Once again, net commission income, at EUR 44.7 million (2018: EUR 41.4 million), was comprised primarily of payments by the State of Baden-Württemberg for services provided by L-Bank. These included, in particular, the distribution of family benefits (especially family allowances) and the granting of financial aid (EU structural funds and other instruments).

The net result from other operating income and expenses was negative at EUR 1.4 million (2018: positive net income of EUR 16.1 million). This anticipated decline was due to one-off income in the previous year from the sale of a building not used for banking operations. The operating result before risk provisioning/valuations fell to EUR 165.3 million (2018: EUR 221.0 million).

Administrative expenses, which include depreciation on tangible assets as well as personnel and general expenses, increased by 7.2% year-on-year to EUR 180.0 million (2018: EUR 167.9 million), in line with expectations. General expenses were dominated by costs and expenses for building work incurred in the course of modernising the Bank's IT systems. The increase in personnel expenses was due primarily to actuarial valuation adjustments for company pension plans and collective wage increases.

As expected, gains and losses from asset revaluation improved slightly (2019: EUR –35.1 million; 2018: EUR –39.9 million). This brought the operating result to EUR 130.2 million (2018: EUR 181.1 million). The Bank's distributable income totalled EUR 130.0 million (2018: EUR 180.2 million).

Due to the development fund system, L-Bank's current development contributions had no impact on earnings in 2019. Of the total development fund (provision) of EUR 86.6 million set up for the year under review, EUR 77.4 million was utilised. The development fund available for financing development services in 2020 amounts to EUR 89.2 million. Out of the Bank's earnings for 2019, an amount of EUR 80.0 million was transferred to the development fund for 2021's development contributions.

Net income for the year totalled EUR 50.0 million (2018: EUR 50.2 million). So taking account of the profit carried forward from the previous year, net profit amounted to EUR 51.0 million. The Board is planning to transfer EUR 50.0 million of this income to other retained earnings in order to increase the Bank's Tier I capital ratio, and to carry forward the remaining EUR 1.0 million.

BREAKDOWN OF OPERATING INCOME in EUR millions

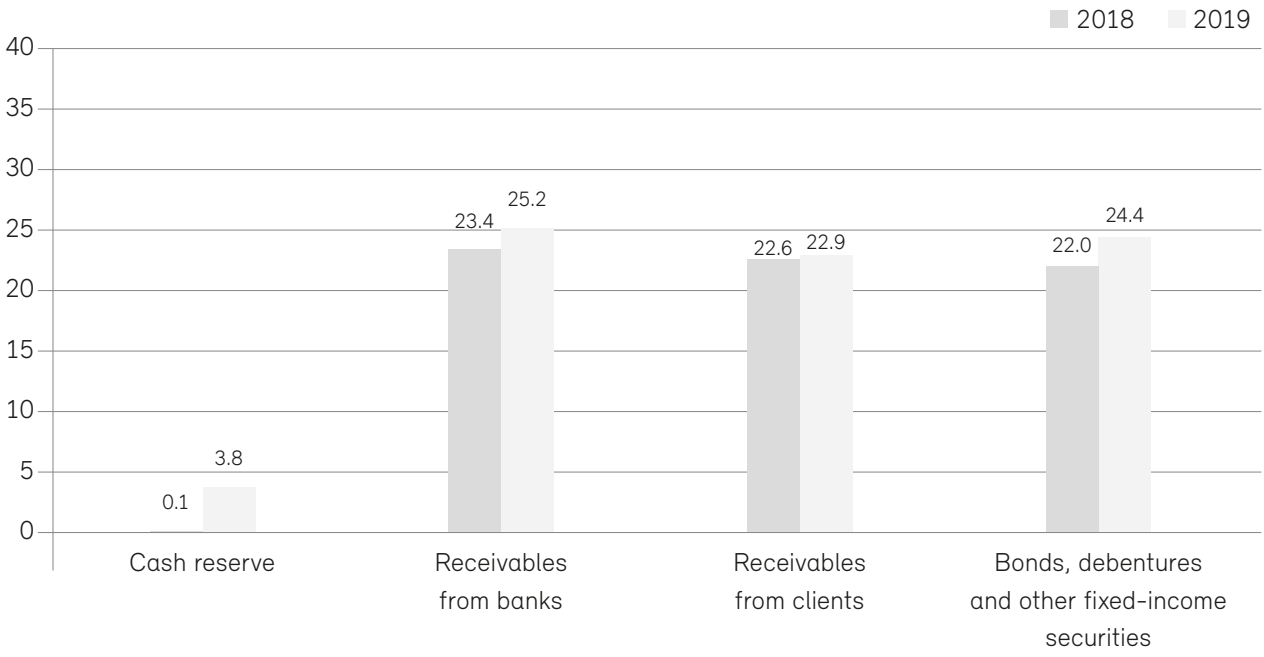
	01.01.2019 to 31.12.2019	01.01.2018 to 31.12.2018	Change	Change in %
Net interest income	302.0	331.4	–29.4	–8.9
Net commission income	44.7	41.4	3.3	8.0
Net result from other income/expenses	–1.4	16.1	–17.5	>–100.0
Administrative expenses	180.0	167.9	12.1	7.2
Operating result before risk provisioning/valuations	**165.3**	**221.0**	**–55.7**	**–25.2**
Net income from asset revaluation	–35.1	–39.9	4.8	–12.0
Operating result	**130.2**	**181.1**	**–50.9**	**–28.1**
Taxes on income	0.2	0.9	–0.7	–77.8
Distributable income	**130.0**	**180.2**	**–50.2**	**–27.9**
Addition to development funds (provision)	80.0	80.0	0.0	0.0
Addition to fund for general banking risks	–	50.0	–50.0	–100.0
Net income	**50.0**	**50.2**	**–0.2**	**–0.4**

Assets and liabilities

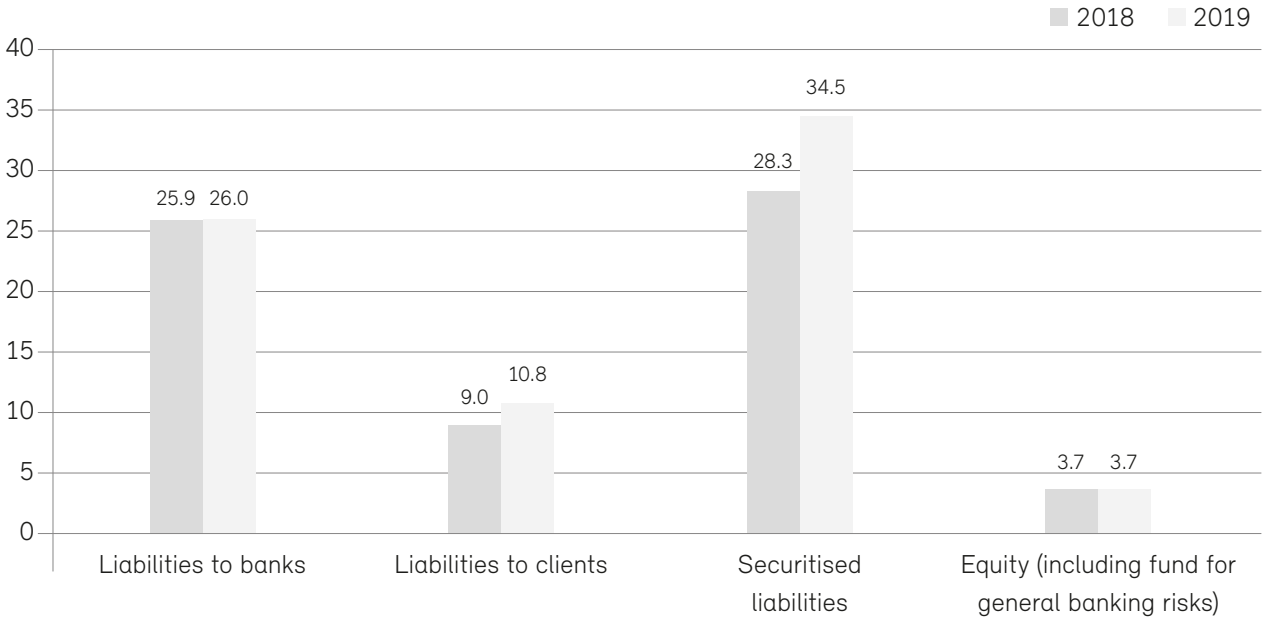
L-Bank's total assets showed significant growth, due mainly to short-term portfolio growth, amounting to a total of EUR 77,622.6 million as at the balance-sheet date (2018: EUR 69,608.9 million). The assets side saw increases in the cash reserve, receivables from banks and securities receivables. On the liabilities side, this was offset by higher securitised liabilities and liabilities to clients.

The business volume, which also encompasses contingent liabilities and irrevocable lending commitments, rose by 9.2% to EUR 81,397.0 million as at the balance sheet date (2018: EUR 74,512.6 million).

SELECTED ITEMS UNDER ASSETS in EUR billions



SELECTED ITEMS UNDER LIABILITIES in EUR billions



Financial position

As the State Bank of Baden-Württemberg, L-Bank benefits from the federal state's maintenance and public (statutory) guarantee obligation, as well as an explicit state guarantee. The latter means that L-Bank's de facto credit rating is identical to that of the State of Baden-Württemberg. Consequently, credit-rating agencies Moody's Investors Service, Standard & Poor's and, since January 2020, Scope, continue to give L-Bank their top ratings of Aaa and AAA. In addition, banks can count L-Bank bonds towards their short-term liquidity coverage ratios (LCR) as assets with the highest liquidity standing.

During the year under review, L-Bank was once again able to make flexible use of the refinancing options on offer to meet its objectives in terms of funding volumes, maturity profiles and structure. The Bank focused on maturities in the two-year to five-year range. The principal instrument used here is the Bank's Debt Issuance Programme, with a funding limit of EUR 30,000.0 million, of which EUR 17,193.8 million was utilised as at 31 December 2019 (2018: EUR 14,581.6 million). The total volume of medium and long-term refinancing through borrowings on the capital markets amounted to EUR 5,711.7 million (2018: EUR 3,558.9 million). As at year-end, utilisation of the Commercial Paper Programme, which is used for short-term refinancing and has an upper funding limit of EUR 20,000.0 million, amounted to EUR 14,050.7 million (2018: EUR 10,178.1 million).

For certain development programmes, L-Bank also made use of refinancing products available from other development institutions such as KfW and Landwirtschaftliche Rentenbank, to the extent that such products were compatible with the Bank's own programmes.

During the past fiscal year, the Bank's liquidity was assured, and the Bank complied with all regulatory requirements at all times.

Capital adequacy is calculated in accordance with the requirements of the Capital Requirements Regulation (CRR). The following table provides a breakdown of the Bank's equity as at 31 December 2019, prior to approval of the annual financial statements by L-Bank's Supervisory Board.

EQUITY in EUR millions	
'Hard' Tier I capital after deductions	3,659.0
Additional Tier I capital after deductions	0.0
Supplementary capital after deductions	390.0
Total equity	4,049.0

Summary of the Bank's business development and position

L-Bank's business development and its financial performance, net assets and financial position were satisfactory in the year under review.

Personnel

As at the balance sheet date, the number of active staff employed by L-Bank totalled 1,307 (2018: 1,277). With a staff turnover rate of 3.68% (2018: 3.49%), L-Bank has a stable headcount. Meanwhile a macro-trend is becoming evident: Younger employees, in particular, change employers more frequently than preceding generations did.

As in previous years, L-Bank pursues a strategy of filling vacant positions from internal resources wherever possible. In-house professional development initiatives help to underpin this strategy. Even so, highly specialised knowledge workers in particular – specialising in IT, for example – must be recruited on the external labour market.

In-house training of junior staff represents another cornerstone of L-Bank's strategy for recruiting new employees. As at the balance sheet date, a total of 52 people were involved in training programmes. With a broad range of educational options for trainees, employees on work-study programmes, working students and volunteers, L-Bank not only ensures that in-house knowledge is passed on, but also helps to create diversified professional development opportunities in society.

In a constantly evolving digital environment, personnel development is especially important. L-Bank offers a wide range of staff development programmes. As part of the Bank's in-house staff dialogue, employees regularly meet and exchange ideas with their line managers, and jointly define suitable programmes for further developing their skills. Furthermore, L-Bank enables junior staff to develop their professional skills above and beyond their specialist areas through a talent management programme based on personalised development modules.

Since 2018, L-Bank has provided employees with the opportunity to tailor their transition to retirement according to their own preferences by enabling them to opt for phased retirement. Given that the average employee age remains unchanged at 46.6, this approach enables L-Bank to plan for long-term recruitment as positions become vacant for demographic reasons.

When filling executive positions, L-Bank strives to achieve an appropriate gender balance while always taking suitability, skills and professional performance into consideration. As a rule, this means that male and female candidates are considered in equal proportions. As at the balance sheet date, 33.5% of all executive managers were women (2018: 35.1%). Overall, L-Bank employs more women than men: female employees accounted for 56.4% (2018: 57.2%) of the workforce. With the ascension of Edith Weymayr to the office of Chair of the Board of Management on 1 January 2020, the membership of L-Bank's Board of Management is now composed equally of women and men.

Finding a good work-life balance is a top priority in the Bank's personnel strategy. L-Bank supports families by enabling individuals to work on part-time employment contracts adjusted to their personal circumstances. As at the balance sheet date, a total of 354 employees (2018: 344) were working part-time. If there are any bottlenecks in childcare, L-Bank makes specially equipped parent-child offices available. Furthermore, the Bank pays employees a childcare allowance for children who are not yet required to attend school.

Sustainability Report

As a development bank, sustainability is a core component of L-Bank's DNA and the vision guiding the Bank's business activities. In collaboration with the state government, L-Bank uses development funding as both an incentive and a lever for the sustainable development of Baden-Württemberg's economy and society. L-Bank introduced a sustainability management system in 2013, and since then has steadily continued to develop it. By integrating sustainability issues into the Bank's business strategy, L-Bank ensures that it is fully committed to resolving them.

The accompanying reports illustrate the material economic, ecological and social impacts of L-Bank's activities. L-Bank continues to document the discharge of its social responsibilities in detail by issuing regular reports in compliance with the Eco-Management and Audit Scheme (EMAS), publishing detailed sustainability reports every three years, and by preparing annual reports on selected sustainability aspects in accordance with the WIN Charter framework.

We fulfil our statutory reporting obligations under the CSR Implementation Directive by issuing a non-financial report as a separate part of our annual report, complete with references to the management report. The annual report is published on L-Bank's home page (www.l-bank.info).

Outlook

The current economic downturn in Germany is characterised by a discrepancy between the state's export-intensive industrial and other, more domestically oriented, sectors of the economy. The decisive factor in future developments will be whether and, if so, to what extent the labour market and domestic demand can escape the pull of the current industrial recession in the long term. A positive factor militating in favour of the labour market's continuing stability is the fact that many companies are complaining about a shortage of skilled workers, meaning that they may avoid staff cuts even if the economy continues to perform poorly. A rapid rise in unemployment is therefore unlikely. Private consumption should continue to make a significant contribution to growth, reducing the risk of a full-scale German recession in the coming year. The ECB continues to pursue a very expansionary monetary policy, and fiscal policy is also expected to deliver suitable stimuli. Furthermore, the risks associated with global trade conflicts and Brexit appear to have diminished at least temporarily prior to year-end. However, the coronavirus outbreak in China represents a new risk factor for economic development, the extent of which is very hard to gauge. Assuming that the COVID-19 wave does not have a major impact on the global economy, we can expect to see a gradual recovery in Germany's industrial sector. Overall, however, economic expansion is likely to remain weak in 2020, with production output falling short of its potential. As a result of the slightly higher number of working days in 2020, L-Bank forecasts a slightly higher year-on-year growth rate for the Germany economy of between 0.8% and 1.1%. Forecasts suggest that the inflation rate will fall even further as energy prices continue to decline. Thus Deutsche Bundesbank expects the rate of inflation to weaken from 1.4% to 1.3% in 2020.

Generally speaking, the factors impacting Germany's economy as a whole, as described above, also apply to Baden-Württemberg's economy. The situation is made more difficult by the fact that a disproportionately high number of companies in the federal state are also having to cope with wide-ranging transformation. The automotive industry is facing particular challenges. In addition to a worldwide decline in demand, due in part to the Chinese economic slowdown, the industry is facing the enormous technical challenge of transitioning to vehicles with unconventional drive systems. Having suffered a double-digit percentage drop in orders last year, mechanical engineering companies in Baden-Württemberg are also heavily affected by this structural shift, even as the global economy cools. Despite all these risks and challenges, business confidence indicators, as well as order and export trends towards the end of last year, suggest that the manufacturing industry's lean period may be coming to an end. If there is no new escalation of global trade conflicts and no serious deterioration of the economy as a result of the coronavirus, the contribution of exports to growth is likely to stabilise again, which is especially important for Baden-Württemberg's economy.

In addition, the service sector, the booming construction industry and the trend towards increased government spending continue to make a stabilising contribution to Germany's economy. Taking account of all these factors, Baden-Württemberg's growth rate is once again likely to fall slightly below the national average, given the greater impact of current challenges on the state. L-Bank therefore expects to see growth in Baden-Württemberg range from 0.5% to 0.8%. In line with federal predictions, the average rate of unemployment is expected to show a minimal rise from 3.2% in 2019 to 3.3% in 2020.

L-Bank's business activities in 2020 will continue to focus on support for housing development and ongoing enterprise development programmes for Baden-Württemberg's SMEs in particular. Essentially, the Bank plans to continue its development finance activities through existing programmes. In light of the economic forecasts described above, L-Bank expects to see a moderate improvement in overall demand.

In view of the somewhat subdued economic outlook, the Bank expects the overall volume of new start-up and SME financing to decline slightly. The 'Digitisation Premium' development programme, which was suspended at the end of 2019, is to be redesigned and relaunched in 2020. The programme is being harmonised with relevant development finance services offered at federal level by KfW. As before, the Digitisation Premium, a repayment subsidy for L-Bank development loans, is intended to assist SMEs with the implementation of specific projects for introducing new digital solutions or improving their IT security. The Premium is L-Bank's contribution to Baden-Württemberg's ongoing structural development as a major centre of technology. The Bank also intends to further expand its business-zone development activities, in particular by adding new technology-park sites. The sale of properties in the technology parks remains part of the Bank's overall strategy.

In the housing development segment, the volume of new business in 2020 is expected to surpass 2019 levels. The main reason for this is most likely to be a higher volume of funding under the 'Living with Children' and 'Combined Home Loan' programmes. The new loan ceiling of EUR 100,000 for the 'Living with Children' programme, introduced in the year under review, together with the 'Combined Home Loan' programme's first full fiscal year, should contribute to this development. L-Bank is not expecting any significant changes on the home ownership side of the state housing development programme. Development programmes supporting rental accommodation will continue at the high level achieved in 2019. Housing demand will remain high, especially in cities and built-up areas. In addition, municipalities still need to commission new building projects to comply with social housing quotas, and the federal state continues to offer high subsidies for such projects.

In 2020, L-Bank is predicting a somewhat lower operating result before risk provisioning/valuations. On the one hand, this is due to the fact that net interest income will again decline slightly. On the other hand, slightly higher costs are expected, especially for IT projects. The Bank is expecting income from asset revaluation to exceed the level achieved in the reporting year. Total assets in 2020 are likely to be comparable to 2019 levels.

With respect to refinancing, L-Bank expects to be able to continue to raise funds on the capital market without any problems, thanks to its very good rating. The Bank is well positioned on the national and international money and capital markets, with good, diversified sources of funding.

Overall, L-Bank is forecasting a slight decline in the volume of new business in 2020 compared to 2019. No significant changes in the Bank's financial performance, financial position or net assets are anticipated.

Opportunities and risk report

The aim of the Bank's risk management model is to ensure that, even in the event of unexpected losses, the Bank's survival should be sustainably assured without the support of the State of Baden-Württemberg. To manage the risks associated with L-Bank's business activities, the Bank has installed a risk management system with the aim of enabling it to:

- ensure the Bank's risk-bearing capacity and solvency at all times,
- assess the Bank's overall risk exposure at any time,
- identify, assess, communicate and manage material individual and concentration risks at an early stage, and
- identify risk-related developments, combined with alternative courses of action.

By devising development programmes, the State of Baden-Württemberg defines the specific market segments in need of financial support, as well as the regional focus of the Bank's business activities. In return, the State of Baden-Württemberg explicitly and unconditionally guarantees the Bank's liabilities through a public (statutory) guarantee and maintenance obligation.

L-Bank was specifically excluded from the scope of the CRD with effect from 27 June 2019. Consequently, L-Bank is no longer subject to the provisions of the CRR, SSM-V, BRRD or SRM-V, each of which is intended for the same circle of institutions as the CRD. However, as CRR regulations apply to all German lending institutions pursuant to Section 1a of the German Banking Act (KWG), L-Bank must continue to comply with these regulations.

Because L-Bank, as a major institution, was directly supervised by the ECB until June 2019, the Bank implemented the ECB's Internal Capital Adequacy Assessment Process (ICAAP) and Internal Liquidity Adequacy Assessment Process (ILAAP) guidelines for in-house processes by the required deadline of 1 January 2019. The guidelines' requirements do not always correspond to the MaRisk provisions laid down by the German supervisory authorities, or with the supplementary regulations published in the 'Regulatory Assessment of Internal Bank Risk-bearing Capacity Concepts and their Integration into the Overall Bank Management Process ('ICAAP') Realignment, November 2018'. The Bank also implemented the EBA guidelines on the stress testing of banking institutions (EBA/GL/2018/04) by the specified deadline of 1 January 2019, as required by the ECB.

How risk management is organised

The core elements of the Bank's risk management approach are defined by the Board of Management in the form of internal guidelines (operational directives). In particular, the Board of Management regulates the implementation of risk inventories, methods for determining the materiality of risks, risk quantification methods, validation methods, the performance of internal stress tests, procedures for reviewing risk-bearing capacity, the capital planning process, the definition of risk tolerances, risk reporting, and the processes and powers for controlling and monitoring risks. The Board of Management has delegated the implementation of internal guidelines to various risk managers, as well as to the Risk Controlling function, the Compliance function, the head of the Internal Audit unit and the Security Office. Within the L-Bank hierarchy, these functions report directly to the Board of Management. To assist them in fulfilling their remits, they have set up a Stress-testing Committee, a Regulatory Compliance Committee and a Risk Management Working Group.

With respect to the Bank's lending and trading business, the front-office and back-office areas at L-Bank are strictly separated at all levels, up to and including Board of Management level. Divisions I and IV are front-office areas, and divisions II and III are back-office areas. Thus the organisational separation of powers is also consistently guaranteed in the event of deputising.

The Head of Division II is the Chief Financial Officer, who is responsible for the back office (second vote). The CFO's deputy is head of Division III (the Chief Risk Officer), who bears bank-wide responsibility for assessing and monitoring all counterparty default, market price, liquidity and operational risks. As head of the Risk Controlling function, she reports exclusively on the above-mentioned risks.

The Board of Management regularly briefs the Supervisory Board on the risk situation, risk management, risk controlling and any other risk-related issues, and – where necessary – reports on specific incidents. The Supervisory Board has set up various committees to deal with specific areas of activity, as follows:

At meetings of the Risk Committee, the Board of Management reports on counterparty default, market price, liquidity and operational risks. The Risk Committee is also briefed on the Bank's risk strategies and on any matters which, in view of the associated risks, are especially significant. For its part, the committee advises the Board of Management on questions relating to the Bank's overall risk appetite and risk strategies.

The Audit Committee is primarily responsible for discussing the audit report with the auditor, and for preparing the Supervisory Board's adoption of the annual financial statements and the Board of Management's proposal for the appropriation of profits. It also discusses the Internal Audit unit's reports, as well as the Compliance function's annual report.

The Personnel Committee is primarily responsible for preparing Supervisory Board resolutions relating to appointments to the Board of Management; it adopts resolutions setting out contractual and other formal matters relating to Board of Management members, with the exception of remuneration.

The Remuneration Control Committee is primarily responsible for preparing Supervisory Board resolutions relating to the remuneration of Board of Management members.

In consultation with the Risk Committee/Supervisory Board, the Board of Management determines the Bank's overall risk appetite and sets appropriate control limits for the individual risk types:

- Thus the Board of Management defines, for example, an interest rate-risk and currency-risk profile for the investment book; the Treasury department is responsible for implementing this profile. The Treasury department is also responsible for managing liquidity risk while observing the control parameters specified by the Board of Management.
- Counterparty default risk is managed by various methods, including the setting of limits approved by the Board of Management; these may be set by the Bank's individual lending departments according to a system of competencies.
- 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.

The Controlling department is responsible for the quantitative and qualitative assessment and communication of risks, in accordance with the Board of Management's instructions. The department's staff perform the duties of the Risk Controlling function.

Their assessments are based on a company-wide database containing standardised records detailing all the Bank's transactions and business partners. The analyses produced as part of the risk management process are regularly compared to balance sheet-based analyses and data used for reporting purposes. 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 Board of Management has set up a Stress-testing Committee which, taking existing risk concentrations into account, designs stress scenarios across multiple risk types and proposes suitable settings for model parameters to the Board of Management. In addition, the Stress-testing Committee proposes sensitivity analyses at the level of individual risk types.

The Credit Analysis department assesses the credit standing of individual borrowers and specific portfolios, and proposes appropriate borrower-based lending limits to the Board of Management, as well as lending limits for portfolios and countries. The Credit Analysis department also acts as the back office and casts the back-office vote on business decisions involving risk.

Taking a risk-focused, process-independent approach, the Internal Audit unit 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 material activities and processes, on behalf of the Board of Management. The unit reports directly to the Board of Management. The Internal Audit unit carries out its duties independently and impartially, and is not required to accept instructions regarding the evaluation or reporting of audit results.

The Compliance unit is responsible for regulatory compliance, money-laundering and fraud prevention, as well as securities compliance. The Data Protection Officer, who is part of the Legal Affairs Division, is responsible for ensuring compliance with data protection regulations.

The Security Office assists the Board of Management with all security policy issues. In addition to ensuring that Bank buildings are secure, the Security Office is also responsible for information security policy, coordinating information security and all associated measures, monitoring the effectiveness of security measures, ensuring the continuous improvement and further development of the security process, and regularly reporting on information security.

Business and risk strategies

In the Bank's business strategy, the Board of Management sets a target for, among other things, the Bank's Tier I capital ratio, and decides which products should be used to meet the Bank's public-service mandate through development programmes and other development business. The Bank's statutory public-service mandate results in concentrations of counterparty default risks (cluster risks) in particular industries, types of collateral and regions. To achieve a balanced aggregate risk profile, the Board of Management defines quality requirements for the portfolio structure as a whole in the Bank's business strategy. These include policies defining 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 its business strategy. In its 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 risk.

As part of a quantitative assessment of the Bank's risk-bearing capacity, the Board of Management defines the Bank's risk appetite in the risk strategy by specifying the scope of risk coverage capital that should be set aside as cover for losses.

With respect to managing credit risk, the risk strategy includes policies specifying borrowers' minimum credit ratings and risk margins, and obliges business units to secure loans against collateral that is deemed to be recoverable. In addition, the maximum lending volumes for the next four years are defined for each business unit. 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 are based primarily on levels of demand from the commercial banks with which L-Bank cooperates. Lending business associated with development aid business is primarily determined by the refinancing options available. Any investments made for this purpose must meet exceptionally high standards of creditworthiness. In conformance with the Bank's risk-bearing capacity, the risk strategy duly shows – after making proper 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 projected interest rate movements to generate predictable levels of income with acceptable levels of risk, primarily within maturity bands of up to 24 months. The underlying projections of interest rate movements are derived from capital market parameters. Due to the current volatility, these transactions are intensively monitored on a daily basis, with ongoing reviews being conducted at least weekly by the Board of Management. Due to the long-term investment of equity capital, a market price risk is shown for maturity bands of more than 24 months. The Bank makes use of the national and international capital markets to obtain refinancing on optimised structural and cost terms. 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 refinancing risks due solely to a substantial downgrade of the federal state's credit rating are permanently classified as negligible.

With regard to operational risk, L-Bank pursues an avoidance strategy while adhering to the principle of profitability. This means that – regardless of 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

Risk-bearing capacity represents the highest and most comprehensive level at which the Bank's risk exposure is analysed. It is the basis for the operational implementation of the Bank's risk strategy, because when the risk strategy is formulated, risk tolerances are explicitly specified in the form of limits for risk-weighted assets (RWA limits) for counterparty default risk, and value-at-risk (VaR) limits for all material risks. As part of establishing these limits, a conscious decision is made regarding the scope of potential future risks. And because planned new business activities can only be implemented if the resulting risks are covered by the Bank's risk coverage capital, the analysis of risk-bearing capacity effectively determines the maximum scope of potential new business (especially development aid business), providing a timely indication of any capital increase that may be required. The review of the Bank's risk-bearing capacity is supplemented by analyses of the expected shortfall, by stress tests across all risk types, by sensitivity analyses and by an inverse stress test.

The risk-bearing capacity review process essentially consists of the following subcomponents:

- risk inventory, including determination of risk materiality,
- determination of risk exposures and comparison with existing risk coverage capabilities from economic and normative perspectives, using normal scenarios and various adverse scenarios across multiple risk types, and including equity and risk exposure projections,
- validation of risk measurement methods, and
- sensitivity and stress-test analyses.

Risk inventory

The starting point for reviewing risk-bearing capacity is a risk inventory, carried out at regular intervals. During the risk inventory, of the generally conceivable risks that could impact the Bank's net assets, financial position, financial performance or liquidity, those risks are first selected that present not just a theoretical threat, but also an actual threat. These risks are described as 'relevant' risks. The materiality of these relevant risks is assessed from normative and economic perspectives. If, when considering the Bank's net assets, financial performance, financial position or liquidity from either of these two perspectives, a relevant risk exceeds at least one of the defined thresholds, that risk is material. The risk inventory is used to check whether the risk management system takes account of all material risks (risk coverage). Then follows a critical analysis to determine whether risk assessment, risk management and risk reporting permit an appropriate evaluation of all risks identified by L-Bank.

Risk management takes account of all relevant risks either by means of risk quantification or by applying other risk management policies: during reviews of the Bank's risk-bearing capacity, potential losses are calculated and management limits specified for all material risks as a matter of course. Where these potential losses cannot be meaningfully assessed against the value at risk (VaR), the risks are limited using other management instruments. The ECB specified the instruments to use for liquidity risk in the Internal Liquidity Adequacy Assessment Process (ILAAP). If it is not economically feasible to carry out a value-at-risk assessment in view of the risk profile, the potential losses are evaluated using a simplified procedure. The suitability of the simplified procedure(s), as well as the assumptions made and calculation methods used, are reviewed as required, but at the very least as part of the regular risk inventory. The 2019 risk inventory confirmed that material risks include: counterparty default risk, market price risk, liquidity risk and operational risk, as well as associated risk concentrations. The risk inventory did not identify any new relevant risks. ESG risks ('Environmental, Social and Governance' risks) were identified as risk drivers with an impact on counterparty default risk and reputational risk in particular.

Potential risks and risk coverage capability

The Bank's risk-bearing capacity is monitored from a normative and an economic perspective. The results are reported to the Board of Management on a monthly basis. The Risk Committee and the competent supervisory body are informed of the Bank's risk-bearing capacity in the quarterly risk report.

Scenarios

The Bank implemented three normal scenarios. In the baseline scenario, net interest income and risk provisioning expenses in particular are projected on the basis of parameters derived from the parameters existing on the balance sheet date (e.g. forward rates for interest, multi-year default rates calculated from current transition matrices). In the baseline assumption used for the second scenario, the empirical economic forecast model, the overall state of the economy at the end of the scenario period is predicted on the basis of the current economic situation, taking account of current political and economic circumstances. This forecast also takes account of international trade relations (global political aspect), the ECB's monetary policy (European monetary aspect) and any structural shifts or changes in Baden-Württemberg's economy (local economic aspect). Finally, the economic plan scenario is a combination of the baseline scenario and the empirical economic forecast model, whereby certain risk factors in the base scenario are adjusted by applying conservative aspects of the empirical economic forecast model.

Due to L-Bank's business model, the implementation of a macroeconomic satellite model is not appropriate for modelling adverse scenarios. For this reason, relevant risk parameters are derived from the current economic cycle and then stressed in various adverse scenarios. Each scenario's specific risk parameters are derived from empirical observations, and each scenario targets a different geographical 'event space': a severe global economic downturn, stagflation in the eurozone, the impact on Germany of a liability union, a structural crisis in Baden-Württemberg and an adverse empirical economic forecast model.

In these various adverse scenarios, only implausible events are capable of generating significant stress effects on the Bank's capital ratios due to the Bank's business model. So the Bank also produces a suitably adverse stress scenario by deriving the negative effects on the annual result from value-at-risk calculations. To round off the assessment of the Bank's future risk-bearing capacity, a regulatory stress scenario is also applied, based on sudden changes in CRR regulations which would disadvantage the Bank.

Normative perspective

In the normative perspective, the Bank's risk-bearing capacity is deemed to be adequate if the Bank continuously complies with all regulatory and supervisory capital requirements and constraints for at least 36 months from the reporting date under observation. For this purpose, the Bank projects the total capital ratio, Tier I capital ratio and leverage ratio on a quarterly basis.

In the normative perspective, the Bank's risk coverage capability corresponds to the total or Tier I capital calculated in accordance with the CRR. In the normative perspective, the CRR requires that counterparty default risk, market price risks in the trading book, FX risks in the investment book, operational risk and CVA risk should all be assessed. The Bank uses the following procedures to quantify the risks under consideration:

- Counterparty default risk: calculation of risk-weighted exposure levels to credit and counterparty default risk (CCR) using the standardised approach to credit risk set down in Articles 111–141 CRR or the market valuation method specified in Article 274 CRR.
- Market price risk: The Bank has no trading books. For the investment book, the total risk exposure to foreign exchange, settlement and commodity risk is calculated in accordance with Articles 325–383 CRR.

- Operational risk: The Bank's total risk exposure to operational risk is calculated using the baseline indicator approach described in Articles 315–316 CRR.
- CVA risk: The Bank's total risk exposure to the risk of adjusted credit valuations of OTC derivatives is calculated using the standard method set out in Article 384 CRR.

When projecting future capital adequacy, scenario-dependent assumptions are made regarding the future development of net interest income (taking possible interest rate movements into account), plus, in particular, personnel expenses, general expenses and risk provisioning expenses (in each case taking planned new business and interest rate adjustment transactions into account). In the case of risk provisioning expenses, the Bank distinguishes between specific and non-specific risk provisions. Specific risk provision for the unsecured part of a non-performing exposure (NPE) is calculated using a standardised expected-loss model; for the secured part of an NPE, it is calculated in accordance with the ECB's Guidance to Banks on Non-Performing Loans. Non-specific risk provisions are calculated for performing exposures (PE) using the methodology applied in standard accounting practice.

In the normative perspective, normal scenarios must adhere to ICAAP minimum capital ratios. These comprise the trigger for the maximum distributable amount (MDA trigger: Total SREP Capital Requirement – TSCR, Combined Buffer Requirements – CBR, Pillar 2 Guidance – P2G) plus a management buffer defined by the Board of Management. This management buffer makes it possible to take appropriate management steps as soon as capital bottlenecks become apparent.

The Bank prepares projections of future capital adequacy and capital requirements at the end of each quarter. The following table shows the development of the Bank's equity, Tier I capital, total risk exposure and resulting capital ratios.

FISCAL YEAR 2019	31.03.2019	30.06.2019	30.09.2019	31.12.2019
Total risk exposure in EUR millions	18,511.5	18,580.7	18,669.5	18,241.2
Tier I capital in EUR millions	3,555.6	3,659.3	3,659.1	3,659.0
Equity in EUR millions	3,927.1	4,075.1	4,062.2	4,049.0
Tier I capital ratio in %	19.21	19.69	19.60	20.06
Total capital ratio in %	21.21	21.93	21.76	22.20
Leverage ratio in %	4.74	4.89	4.78	4.86

The normal scenarios performed as at 31 December 2019 confirm the Bank's risk-bearing capacity from a normative perspective. All relevant capital ratios are well above the requisite regulatory/supervisory ratios, and also well above the specified ICAAP minimum ratios.

In the adverse scenarios performed as at 31 December 2019, the earnings projections show in part significant declines in profits, but at no point in time do they show a negative result. Again, the projected capital ratios in these scenarios are higher than the required regulatory/supervisory ratios.

To ensure future compliance with the minimum capital ratios, risk-weighted assets are limited at business unit level. The RWA ceiling is distributed across the individual business segments, taking account of new business planning and the associated risk concentrations.

The following table shows the RWA limits for 2019 and 2020 and their maximum utilisation in fiscal year 2019. The maximum utilisation of RWA limits per business segment and in total is based on monthly calculations.

In EUR millions	RWA LIMIT 2019	MAXIMUM UTILISATION 2019	RWA LIMIT 2020
Total credit risk (CRSA)	25,000	18,210.6	25,000
Thereof for:			
Home ownership assistance	5,500	4,287.7	5,500
Companies	10,500	7,587.1	10,500
Financial institutions	7,000	6,433.7	7,500
Public sector	1,000	644.5	750

Economic perspective

In the economic perspective, the net present value of all existing assets and liabilities, less associated administrative expenses and anticipated risk provisioning expenses, is presented as risk coverage capability. Thus the hidden charges on fixed assets from avoiding depreciation at the lower of cost or market are also taken into account. This risk coverage capability (also known as internal capital) is compared with all identified material risks that could cause an economic loss and a reduction of internal capital, irrespective of any capital adequacy requirements set out in the CRR regulations. All risks are calculated with a confidence level of 99.90% (2018: 99.98%).

As at the balance sheet date, the business portfolio's net present value is calculated as EUR 6,167.7 million. This is offset by NPV administrative expenses totalling EUR 325.4 million, plus imputed NPV risk provisioning costs of EUR 244.7 million, resulting in an NPV-based risk coverage capability of EUR 5,597.6 million.

As at the balance sheet date, 44.74% of this was taken up by VaR values totalling EUR 2,504.4 million. Utilisation of NPV risk coverage capital in 2019 ranged between 44.74% and 58.99%. The Bank complied with the specified aggregate loss ceiling (upper limit of all value-at-risk sub-limits; ALC) of EUR 3,800.0 million (valid to 31 August 2019) or EUR 4,300.0 million (valid from 1 September 2019) on all observation dates in the last fiscal year.

Even when taking the impact of adverse scenarios on internal capital into account, the latter still exceeds the VaR of EUR 2,504.4 million in all scenarios.

For control purposes, an aggregate loss ceiling (ALC) of EUR 4,300 million has been specified for 2020. This corresponds to 78.1% of the Bank's internal capital as at the planning date (30 June 2019), totalling EUR 5,506.6 million. The increase in the ALC compared to 1 January 2019 (EUR 3,800.0 million) is due not to increased risk exposure, but to the further decline in interest rate levels, which is resulting in higher VaR regardless of exposure. In addition, unlike 31 December 2018, VaR is also calculated for longevity risk and real-estate risk.

To manage risks, the specified ALC is distributed across the individual risk types in the form of (sub) limits.

	VALUE-AT-RISK LIMIT 2020 in EUR millions
Aggregate loss ceiling	4,300.0
Thereof for:	
Credit default and migration risks	1,600.0
Credit-spread risks	1,500.0
Interest rate and FX risks (IRRBB)	200.0
Embedded options	35.0
Funding liquidity risks	700.0
Operational risks	50.0
Longevity risk	20.0
Real-estate risk	10.0

Validation of risk measurement methods and performance of sensitivity and stress-test analyses

To ensure that the value-at-risk figures are as informative as possible, the underlying risk measurement methods are validated, which also involves subjecting the parameters used to various sensitivity analyses. In addition, an inverse stress test is used to verify the useful content of the value-at-risk figures. The annual validation procedures are carried out by a unit that has no connection with, or involvement in, model development and application. The validation methods, scope of the individual validation procedures and responsibilities for these procedures, as well as the regular intervals at which they should be applied, are specifically defined for each type of risk. Standardised report templates are used for all types of risk, in which the key findings of the validation processes are summarised for the Board of Management. If the findings of these validation exercises result in adjustments to measurement procedures or their underlying assumptions, all such adjustments must first be approved by the Board of Management. The Controlling department informs the Board of Management of the results once a year. During the 2019 validation cycle, the adequacy of the methods and procedures used was confirmed.

In the economic perspective on the Bank's risk-bearing capacity, the actuarial models used to measure risk showed the limitations of their informative value at various points during the financial market crisis. In view of the fact that actuarial models cannot, by their very nature, depict all possible events, the Bank's quantitative assessments of individual risks are continuously supplemented by comprehensive sensitivity analyses. By performing these analyses, the Bank identifies risk factors that could have a particularly significant impact on the Bank's net assets, financial position and/or financial performance.

In the course of these analyses, scenarios relating to a single type of risk are developed and assessed in terms of impact. The information obtained is taken into account when modelling the adverse scenarios and stress scenarios used during reviews of risk-bearing capacity.

The analytical system described above does not preclude entirely the possibility that certain scenarios jeopardising the Bank's continued existence may never be identified. Consequently, to establish the limits of the models used to review the Bank's risk-bearing capacity, certain assumptions are made regarding loss-related exposure; these assumptions are used to retroactively determine the conditions under which such losses might occur.

This inverse stress test is performed once a year. The Controlling department informs the Board of Management of the results in a separate report. The Risk Committee/Supervisory Board is informed of the results when they receive the risk report at year-end.

The statutory liability mechanisms (maintenance obligation, public guarantee obligation and explicit guarantee of all the Bank's liabilities) mean that the State of Baden-Württemberg is obliged to take any capital and/or liquidity measures necessary to maintain the Bank's business operations. The inverse stress test findings indicate that it is highly unlikely that these liability mechanisms will need to be invoked.

The 2019 inverse stress test showed that the relevant mechanism-triggering liabilities would only be conceivable if one assumed a sudden, severe and rapidly deteriorating economic crisis. It would also mean that national or international actors had failed to make appropriate changes to economic policies. However, these assumptions are not plausible.

Risk management and risk control

In addition to identifying material risks as part of the risk inventory process, the Bank's risk management and risk control processes include the assessment, management, monitoring and communication of material risks.

Counterparty default risk

Credit default risk refers to the risk that a business partner will fail to meet its contractual obligations. These obligations may arise from a lending transaction as defined in the German Banking Act (Section 19 KWG), or from a performance obligation relating to a transaction involving settlement on completion. The reason for non-fulfilment of a contract may be specific, relating to the borrower's credit standing or particular circumstances (e.g. home country, industry sector). Migration risk is the risk of a decline in value due to borrowers' deteriorating credit ratings. Market-wide credit-spread risk is the risk of a rating-independent decline in the value of securities due to market-wide credit-spread movements. Concentration risk arises when the solvency of a large number of borrowers depends on an identical condition or event and, due to the uneven distribution of these borrowers, losses are incurred that threaten the Bank's solvency. Even a single borrower's default may have a significant impact on a financial institution's solvency if the credit volume is sufficiently high.

Assessment of counterparty default risk

The qualitative assessment of credit default and migration risk – which also includes issuer, counterparty and settlement risk – is carried out by classifying the borrower's creditworthiness and appraising the collateral provided for the loan. As part of classifying borrowers' creditworthiness, each borrower is assigned a credit rating expressed as a risk category. When assigning individual ratings, in addition to the client's ability to service their debt, the Bank also pays particular attention to industry affiliation and other risk-related characteristics (e.g. home country, exposure to ESG risks). For borrowers involved in development finance for owner-occupied housing, the homogeneity of the client group means that they are assigned a group rating based on the average probability of default. Certain collateral is taken into account in the qualitative assessment of loss exposure. Loans guaranteed by municipalities and real-estate loans secured on residential properties in Baden-Württemberg are assigned to risk category 1.

Where collateral in kind is provided in the form of residential property in Baden-Württemberg – independent of the real-estate loan, but within the relevant lending value – the borrower is assigned to risk category 4. In the case of Pfandbriefe and similar bond issues (e.g. covered bonds), the external issue rating is used.

The quantitative assessment of the credit default and migration risk for all material risk subtypes of counterparty default risk is linked to the results of the qualitative assessment. A value at risk is calculated for the entire loan portfolio with the help of a Monte Carlo simulation based on migration and default probabilities as well as recovery rates. Migration and default probabilities are allocated on the basis of the rating category to which each client is assigned during the Bank's qualitative assessment. In the case of private and corporate clients in the rental housing sector, a sufficient default history is already available, so the Bank can incorporate its own historical borrower correlations and recovery rates into the assessment. In other business segments, regulatory borrower correlations are applied.

When calculating the amount of the loss, for reasons of prudence, only security provided in the form of cash collateral and/or loans granted to end-borrowers in accordance with the 'borrower's bank' principle are taken into consideration. For the remaining unsecured portion, the regulatory (IRBA) residual debt servicing capability of 55% is applied to the 'Companies in the financial sector' segment. A residual debt servicing capability of 78% is assumed for the 'Public sector' segment, based on the results of a benchmark survey. For borrowers in the 'Other companies' segment, no representative loss history is available. Consequently, based on an expert opinion, a residual debt servicing capability of 30% is applied. For all securities eligible for bail-in, a residual debt servicing capability of 25% is assumed, as their servicing is prioritised over any subordinated risk claims (for which the regulatory residual debt servicing capability is 25%).

The following table shows the default probabilities for the individual risk categories and shows internal risk categories against the corresponding external risk categories.

RISK CATEGORIES AND CORRESPONDING DEFAULT PROBABILITIES

Risk category	1	2	3	4	5	6	7	8	9	10	11	12	13	14
Range of probability of default 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	100	100
	0.02	0.04	0.09	0.19	0.39	0.80	1.65	3.35	6.70	12.95	23.55	100		
External (S&P)		AA+		A		BBB			BB–	B	CCC+	CC	Default	Default
	AAA	AA	A+	A–	BBB+	BBB–	BB+	BB	B+	B–	CCC	C		
		AA–									CCC–			
	Investment grade						Non-investment grade							

The credit-spread risk is measured quantitatively on the basis of market-wide credit-spread fluctuations using a value at risk based on historical simulation of changes in sector-dependent, rating-dependent credit-default swap-spread curves.

The value-at-risk calculations for credit default, migration and credit-spread risk are based on a holding period of one year and a confidence level of 99.90%.

Risk concentrations arising primarily from the Bank's public-service mandate are assessed both qualitatively and quantitatively. A qualitative assessment of concentration risks associated with industries, collateral and countries is performed on the basis of the Herfindahl-Hirschman Index (HHI).

Using the parameters applied to the value-at-risk calculation (in particular rating category/probability of default, recovery rate, correlations) and the fact that a portfolio model is involved, the risks arising from concentrations on individual borrowers, industries, countries and collateral are included in the value at risk calculated for the credit-default or migration risk. The value at risk is calculated on the basis of a Monte Carlo simulation that takes account of borrower correlations, whereby individual borrower concentration risks are included in the assessment.

The quantitative assessment of individual borrower concentrations is made possible by a comparative value-at-risk assessment. For this purpose, a value at risk is calculated for all loans on the basis of the Gordy model and aggregated to produce a total value at risk. The difference between the total value at risk calculated on the basis of the Monte Carlo simulation and the total value at risk calculated on the basis of the Gordy model shows the individual borrower concentration.

To ensure that all risk factors are adequately considered in both quantitative and qualitative assessments, the Bank performs a variety of sensitivity analyses. Sensitivity analyses of specific risk types did not identify any new risk drivers in 2019.

Managing, monitoring and controlling counterparty default risk

To limit the risk of loss, comprehensive risk management policies must be observed both when granting loans and as part of ongoing loan processing.

The following table shows the minimum credit ratings that borrowers in each of the individual business segments must satisfy at the time the loan is granted.

Business segments	Risk category
Loans provided under programmes	Credit ratings required for programme-related activities are stipulated in the development programmes agreed between the State of Baden-Württemberg and L-Bank, and in the Bank's in-house directives
Other loans (including securities and financial investments)	1 to 5
Interest rate derivatives without collateral	1 to 3, but currently no new business
Interest rate derivatives with collateral	1 to 5

In the case of non-programme-related development business, exceptions to the minimum risk categories must be approved by the Board of Management.

In addition, adequate collateralisation must be assured when granting loans. The type of collateral to be provided in programme-related development business is specified in the corresponding programme guidelines. In non-programme-related development business, care must be taken to obtain sufficient and sustainable collateral, insofar as this is customary in banking and reasonable on the basis of the client's legal form or credit rating. At the same time, the value of the collateral provided must not depend on the borrower's credit rating. 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 of the loan. 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 enforced realisation, the Bank can expect to realise recovery proceeds.

Furthermore, loans may only be granted if appropriate, individual limits have been set for issuer, counterparty and borrower risks. For development aid business, appropriate limits should always be set before loans are granted, whereas for non-programme-related development business, the Bank may set limits while simultaneously granting loans. In programme-related development business, the Bank is very much subject to the 'obligation to contract', so the individual limits are very tight. The maximum loan amount that L-Bank may issue to borrowers incurring commercial risks outside the Federal Republic of Germany is restricted by appropriate limits set at country level (country limits). Issuer, counterparty, borrower and country limits are set by the Board of Management based on an internal analysis of credit quality and monitored on a daily basis by the Controlling department. If a limit is exceeded, the heads of the departments concerned are informed on the same day and appropriate risk-response measures are initiated. The Risk Committee/Supervisory Board is informed of significant limit overruns in the quarterly risk report.

To offset possible losses from counterparty default risks, risk-based margins should really be charged when granting loans. Given L-Bank's business model, however, it is not possible to set individual risk-based margins for development loans issued under the Bank's development programmes. With respect to development aid business, most transactions are conducted with capital market participants. For these borrowers, the Bank mainly trades in credit spreads on the capital market, meaning that L-Bank only has limited influence on margins. For all loans where margins are not fixed by third parties (programme loans) and where conditions are not set on the capital market, a risk margin is calculated on the basis of the probability of default and incorporated into the decision-making process.

To prevent unbalanced lending decisions, two approving votes (front office/trading and back office) are mandatory for all trading transactions and for all risk-related credit transactions prior to conclusion of the transaction.

Furthermore, the Bank has installed an early risk detection system so that it can identify early-stage deterioration of borrower creditworthiness at the level of both individual transactions and the portfolio as a whole, and subsequently gear ongoing loan processing and risk management to such changes in borrower creditworthiness.

Due to the Bank's business model, it is not really possible to limit concentration risks by applying new-business policies. However, to ensure that portfolio structures which could endanger the Bank's existence are identified at an early stage, concentration risks are analysed at portfolio level and constrained by value-at-risk limits and RWA limits for credit default, migration and credit-spread risk.

The collateral concentration risk associated with housing development is lower. Because 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. Due to the economic strength of the State of Baden-Württemberg, the Bank does not currently see any danger of significant declines in real-estate values. Guarantees are subject to another collateral-related concentration risk. Of the guarantees received (without public guarantee or maintenance obligation) worth around EUR 8,580.4 million, the State of Baden-Württemberg accounts for some EUR 7,195.9 million. Due to the credit standing of the State of Baden-Württemberg, L-Bank regards this risk as negligible.

L-Bank's business model also results in a low concentration risk for business sectors. At EUR 36,183.2 million, the highest volume of receivables is due from banks. Also included in this amount are receivables from central banks and other public bodies that are not taken into consideration when determining the degree of interdependency between an institution and the financial system pursuant to Commission Delegated Regulation (EU) 1222/2014 of 8 October 2014. However, the contagion risk to which L-Bank is exposed through receivables from banks is classed as exceptionally low. L-Bank extends loans for business development purposes via borrowers' commercial banks. The Bank's exposure to these borrowers' bank loans amounted to EUR 20,961.0 million as at 31 December 2019. These lendings to banks are secured by the assignment to L-Bank of claims on end-clients. Another EUR 129.1 million is attributable to the fact that L-Bank has underwritten the commercial banks' exposure to end-client risk. EUR 15,093.1 million of the Bank's total lending commitment relates to transactions associated with development aid business, whereby the Bank invests low-cost funds from refinancing in low-risk or risk-free issuers. Of this amount of EUR 15,093.1 million, EUR 5,513.0 million is secured by public guarantee/maintenance obligation, and EUR 47.0 million against Pfandbriefe. After deducting receivables from central banks (EUR 3,754.8 million) and multilateral development banks (EUR 1,299.8 million), the remaining unsecured volume is EUR 4,478.5 million. Roughly 94.4% of this is assigned to risk categories 1 to 4 and only around 5.6% to risk categories 5 and 6. Consequently, the concentration on the financial sector does not currently represent an increased risk of loss for the Bank.

In regional terms, the Bank's public-service mandate means that it is exposed to a high concentration risk for the region 'Germany'. A total of 89.7% of the risk portfolio is assignable to Germany, of which 70.2% relates to the State of Baden-Württemberg. Some 5.3% of the risk-relevant portfolio is located in France, the Netherlands, Austria or with international organisations (e.g. the World Bank). A total of 5% of the risk-relevant portfolio is attributable to transactions in countries outside the eurozone, which are performed for purposes of risk management or capital investment.

Ongoing and incident-related creditworthiness and collateral classifications are intended, above all, to ensure that the Bank can take early risk-response measures (e.g. by increasing the collateral requirement) at the level of individual transactions in the event that a client's credit standing should deteriorate. But the classification also enables the Bank to carry out real-time assessments of the entire portfolio's risk structure. The following table shows the loan portfolio's risk structure as at 31 December 2019.

RISK STRUCTURE OF THE LOAN PORTFOLIO in EUR millions

Risk category	Private clients	Companies and self-employed persons	Companies in the financial sector	Public sector	L-Bank total	Allocation in %
1	149.4	273.6	9,528.6	18,100.3	28,052.0	36.0
2	7.5	803.0	2,666.4	4,539.5	8,016.3	10.3
3		3,141.1	8,971.1	58.9	12,171.1	15.6
4	4.8	2,690.0	15,438.2	67.2	18,200.2	23.4
5	5,410.7	1,739.7	1,518.7	0.0	8,669.2	11.1
6	191.2	428.4	1,166.9	52.0	1,838.4	2.4
7	46.8	215.1	16.6		278.6	0.4
8		106.0	236.7		342.8	0.4
9	0.9	15.4	12.6		29.0	0.0
10	0.5	10.1		0.0	10.6	0.0
11		2.4	50.0		52.4	0.1
12	1.0	4.7	29.0		34.7	0.0
13	28.8	62.5	2.2		93.6	0.1
14	18.9	16.7	0.5		36.1	0.0
Total	**5,860.5**	**9,508.7**	**39,637.7**	**22,818.0**	**77,824.9**	**100.0**

In addition to RWA limits, which are used to safeguard the Bank's risk-bearing capacity in the normative perspective, credit risks are also limited by setting a value-at-risk limit at portfolio level. The following table provides an overview of the proportion of the aggregate loss ceiling taken up by counterparty default risks in the course of 2019.

VALUE AT RISK FOR COUNTERPARTY DEFAULT RISKS IN 2019 in EUR millions

	31.01.2019		31.03.2019		30.06.2019		30.09.2019		31.12.2019	
	Limit	Used	Limit	Used	Limit	Used	Limit	Used	Limit	Used
Aggregate loss ceiling	3,800.0	2,529.6	3,800.0	2,848.8	3,800.0	3,071.8	4,300.0	3,120.2	4,300.0	2,504.4
Share of counterparty default risks in %	42.1	37.8	42.1	42.4	42.1	43.3	37.2	40.6	37.2	29.9
Counterparty default risks	1,600.0	956.2	1,600.0	1,207.5	1,600.0	1,328.8	1,600.0	1,266.8	1,600.0	749.4

In the previous year, the value at risk for counterparty default risk from the periodic perspective, i.e. without migration risks and with a confidence level of 99.0%, was EUR 208.4 million. In the previous year's liquidation perspective, the value at risk for counterparty default risk including migration risks was reported at EUR 1,736.2 million, with a confidence level of 99.98%. The decline of the value at risk for counterparty default risk compared to 31 December 2018 is due essentially to a reduced confidence level, the inclusion of collateral for borrower's bank loans and a more precise treatment of securities deposited as collateral with EUREX. As at 31 December 2019, the calculated value at risk includes individual borrower concentration risks totalling EUR 521.7 million. The largest individual borrower risks are attributable to borrowers in the Baden-Württemberg 'rental housing construction clients' segment and 'companies in the financial sector' segment.

As part of its ongoing loan processing activity, the Bank ensures that potential losses are minimised or averted by defining dedicated procedures for the treatment of non-performing exposures (NPEs). For example, a regulated dunning procedure is specified to ensure that claims are upheld and settled as soon as possible. For this purpose, loans are classified as problem loans if there are strong indications that, to avert or minimise losses, actions may be required that go beyond the normal scope of client support, intensified client contact and the provision of additional collateral as part of the intensive support process. Loans are classified as NPEs according to the following criteria:

- the client is in material default of payment, i.e. is more than 90 days in arrears with a payable that is greater than 1% of the total debt and greater than EUR 100 (in the case of retail businesses) or at least EUR 500 (in the case of other clients), or
- according to the Bank's internal rating, the client is in risk category 13 or 14, or

- an individual risk provision has been made against the client, or
- collateral provided to L-Bank by the client is realised (by compulsory auction excluding partition by auction), or
- the client is classified as 'forborne' and is under problem-loan processing.

'Forborne loans' are balance sheet assets where the Bank has given a borrower in financial difficulties extra concessions as part of the restructuring process (e.g. in the form of debt deferral agreements, maturity extensions, repayment holidays or debt rescheduling) in order to re-establish or assure the borrower's debt servicing capability in the event that the latter has ceased to exist or is acutely at risk. Such a loan must be reported as an NPE and forborne loan for a period of one year after the financial difficulties have been resolved. The loan must then be classified exclusively as a forborne loan for a further two years (forbearance period).

The following table shows the NPE portfolio at the end of 2019. When classifying NPEs, the Bank distinguishes between restructuring exposure (risk category 13) and workout exposure (risk category 14).

NPE PORTFOLIO AS AT 31.12.2019 in EUR millions

	Total risk portfolio	NPE portfolio		Restructuring portfolio		Workout portfolio	
		total	in %	total	in %	total	in %
Private clients	5,860.5	47.8	0.82	28.8	0.49	19.0	0.32
Rental housing construction clients	6,235.4	9.0	0.14	1.9	0.03	7.1	0.11
Companies in the financial sector	39,637.7	0	0.00	0	0.00	0	0.00
Other companies	3,273.2	75.8	2.32	66.3	2.03	9.5	0.29
Public sector	22,818.0	0	0.00	0	0.00	0	0.00
Total	**77,824.9**	**132.6**	**0.17**	**97.0**	**0.12**	**35.6**	**0.05**

The total NPE portfolio as at 31 December 2019 includes forborne loans in the amount of EUR 40.9 million. A further EUR 21.5 million in forborne loans are in the forbearance period and consequently not included in the reported NPE portfolio.

To ensure that risks are identified early, the Bank has installed various early warning indicators, including the trending NPE ratio, trending collateral values, changes in the proportion of NPEs for which the Bank has already made risk provisions and the proportion

of NPEs in financial difficulties that can no longer be rectified by restructuring measures.

As at the balance sheet date and throughout fiscal year 2019, all early warning indicators were at a historically average level, meaning that the Bank did not observe any trend towards a possible future increase in counterparty default risk.

Early and adequate risk provisioning

L-Bank makes appropriate allowance for counterparty default risks that have become acute by setting aside specific risk provisions. The Bank also forms general risk provisions for certain portfolios where the risk structure could cause acute counterparty default risks to arise in the future. Based on various instruments for the early identification of risks, the Bank has set up dedicated processes for forming specific and general risk provisions and issued corresponding guidelines.

The unsecured portion of the NPEs, as determined after prudent valuation of the collateral provided, is fully covered by risk provisions.

Outlook

The counterparty default risk to which L-Bank is exposed is determined by the overall state of the economy, but also by changes in borrowers' personal circumstances (e.g. divorce). Due to the strong alignment of Baden-Württemberg's economy with the automotive industry, structural difficulties associated with the ongoing climate protection debate could result in increased counterparty default risks. The Bank anticipates that any financial difficulties arising from such a scenario could be mitigated by the prevailing low interest rate levels.

Market price risk

Market price risk refers to potential losses caused by unfavourable price movements on the money and capital markets. Market price risk exists mainly in the form of interest rate risks and, to a negligible extent, foreign-currency risks. As the Bank does not maintain trading books, market price risks only arise in connection with the bank book's lending and refinancing transactions. Some of these transactions contain explicit and/or implicit options with associated option risks.

Assessing market price risks

The interest rate and foreign-currency risks in the investment book are quantitatively assessed using the value at risk, based on historical simulations. For this purpose, euro or FX receipts collected on the basis of interest rate risk are compared with euro or FX disbursements made on the basis of interest rate risk, and a market value is calculated for the resulting gap. L-Bank does not separate out funds invested to cover pension commitments to employees, so these investments form part of the euro bank book. Consequently, for the purposes of assessing interest rate risk, anticipated disbursements for covering pension commitments have been taken into consideration on the basis of the payments used to calculate these pension commitments. Since explicit non-behaviour-dependent options must always be perfectly hedged, there is no need to include them in the euro and FX cash flows.

In order to monitor risk-bearing capacity, interest rate and foreign-currency risk are assessed for the economic perspective on the Bank's risk-bearing capacity, based on a historical simulation over an observation period of 2,500 days with a confidence level of 99.90% and a 250-day holding period. For daily control purposes, a value at risk is calculated on the basis of 10- and 25-day holding periods.

A qualitative assessment of the interest rate risk and USD risk is performed using the supervisory standard test and supervisory early warning indicators for interest rate risk in the bank book.

Risks arising from explicit behaviour-dependent options as well as risks associated with implicit options are quantitatively assessed on the basis of the risk factors identified for interest rate and foreign-currency risks as part of the value-at-risk assessment, taking historical observations into account.

The informative value of the above-mentioned quantitative assessments is checked by means of backtesting and sensitivity analyses. In fiscal year 2019, there was no need to adjust the model due to incorrect statements of the calculated value at risk. Sensitivity analyses are used to explore possible losses resulting from varying degrees of extreme interest rate and exchange-rate changes that are not always reflected over the historical observation period applied. These scenarios are also used to determine the risk of loss due to interest rate changes that did not occur over the last 2,500 trading days but may occur in the future. The sensitivity analyses confirm the suitability of the risk factors applied.

Managing, monitoring and controlling market price risk

The management of interest rate and foreign-currency risks for the investment book as a whole is essentially based on the risk strategy laid down by the Board of Management, which specifies that risk positions in the 24-month maturity band may only result from longer-term equity investment. Compliance with this requirement is reviewed by specifying a corresponding target risk structure. In the latter, the Board of Management specifies the target interest rate risk profile, together with deviations per maturity band that are permissible for efficient implementation.

The risk exposure arising from different receipt and disbursement dates for lending and refinancing transactions is hedged primarily by means of interest rate swaps and cross-currency interest rate swaps. As at 31 December 2019, the portfolio of interest rate swaps had a nominal value of EUR 71.5 billion. Cross-currency interest rate swaps had a nominal value of EUR 16.8 billion, currency swaps had a nominal value of EUR 14.2 billion.

Furthermore, the Board of Management has resolved that at the level of individual transactions, all explicit non-behaviour-dependent options in lending and refinancing transactions must be hedged by an identical offsetting transaction. In the Bank's programme-related development business, it is exposed to implicit options based on Section 489 of the German Civil Code (BGB). Any potential losses arising from this exposure are compensated for by the structure of the various development programme mechanisms.

As part of the process of safeguarding the Bank's risk-bearing capacity, the Board of Management also specifies a value-at-risk limit for interest rate and foreign-currency risk (including explicit non-behaviour-dependent options). The following table provides an overview of the proportion of the aggregate loss ceiling taken up by these market price risks in the course of 2019.

VALUE AT RISK FOR MARKET PRICE RISK IN 2019 in EUR millions

	31.01.2019		31.03.2019		30.06.2019		30.09.2019		31.12.2019	
	Limit	Used	Limit	Used	Limit	Used	Limit	Used	Limit	Used
Aggregate loss ceiling	3,800.0	2,529.6	3,800.0	2,848.8	3,800.0	3,071.8	4,300.0	3,120.2	4,300.0	2,504.4
Share of market price exposure in %	5.3	5.4	5.3	4.3	5.3	3.8	4.7	3.5	4.7	5.1
Market price risks	200.0	137.3	200.0	123.5	200.0	118.0	200.0	110.3	200.0	128.5

In the previous year, the value at risk for market price risk in the periodic perspective, i.e. over a projected period of twelve months with a confidence level of 99.0%, was EUR 34.7 million. In the liquidation perspective for the previous year, market price risk was assigned a value at risk of EUR 297.5 million, at a confidence level of 99.98%. The year-on-year decline in value at risk is attributable to the lower confidence level.

The qualitative assessment of the interest rate risk is made by determining the loss of net present value (NPV) resulting from a parallel upward or downward shift in the yield curve by 200 basis points relative to the Bank's available equity capital according to Article 72 CRR (standard supervisory test), as required by the regulator. This interest rate risk coefficient is limited to 20% in L-Bank's internal risk management system and has an early warning threshold of 16%. As of 30 June 2019, the qualitative assessment (pursuant to BaFin Circular 06/2019 (BA) – Interest rate risks in the investment book) was extended to include the calculation of the loss of NPV resulting from the six scenarios required for calculating the supervisory early warning indicator for interest rate risks in the bank book relative to core capital, pursuant to Article 26 CRR. For this purpose, L-Bank has set a limit of 15% for the supervisory threshold and an internal early warning threshold of 12%. These key figures are calculated and reported to the Board of Management on a daily basis.

EBA guidelines on the management of interest rate risk in the investment book (EBA/GL/2018/02) call for the measurement and management of interest rate risks in the investment book from both an NPV and an income perspective. When determining earnings risk, L-Bank uses the same scenarios that are used for the NPV assessment. In each case, the effects of these scenarios on the net interest surplus over the next twelve months are determined on the assumption both that the interest rate risk exposure is retained, and that it is completely closed out. These figures are calculated and reported to the Board of Management every month.

The Controlling department is responsible for monitoring interest rate risk and foreign-currency risk by comparing the VaR figures calculated each day with the specified limits. The Board of Management is informed of market price risks in a daily risk report and a monthly aggregated report, which is distributed to the Risk Committee/Supervisory Board on a quarterly basis.

Loss-free valuation of the non-trading portfolio (bank book)

The Bank uses the so-called loss-free valuation of interest rate derivatives to determine a possible provision for impending losses, because the bank book derivatives are in an – albeit abstract – hedging relationship with recognised financial instruments with corresponding or opposing risk profiles. Accordingly, a provision for impending losses would have to be formed if, as a consequence of this (abstract) hedging relationship, a so-called commitment surplus results from the valuation of the interest rate book as a whole after comparing book values with NPVs. As at 31 December 2019, these calculations show significant hidden reserves on which even a negative change in the yield curve determined on the basis of the value-at-risk calculation would only impact to a limited extent.

Liquidity risk

Liquidity risk includes first, the risk that the Bank may not be able to obtain sufficient liquidity on the expected terms when required (funding liquidity risk) and second, the risk that the Bank will be unable to meet payment obligations when they fall due (insolvency risk).

Assessing liquidity risks

The funding liquidity risk for existing transactions (i.e. without taking account of new and interest rate adjustment transactions) is measured quantitatively by calculating a value at risk with a 250-day holding period and a 99.90% confidence level. This VaR is calculated on the basis of changes in L-Bank's refinancing conditions observed in the past. The underlying assumption is that the Bank is only able to refinance net disbursements on less advantageous terms. Sensitivity analyses that assume a certain deterioration in refinancing conditions, or a widening of the refinancing gap, are used to confirm the validity of the calculated results.

There is no meaningful way of making a quantitative assessment of the insolvency risk. The risk is assessed qualitatively by calculating the LCR and survival time frame.

Managing, monitoring and controlling liquidity risk

To limit the funding liquidity risk, the calendar-year requirement to refinance the Bank's open position – in terms of liquidity – from portfolio transactions may not exceed EUR 10 billion. This target was met throughout the fiscal year.

The Bank complied with the value-at-risk limit granted for the economic perspective on risk-bearing capacity throughout fiscal year 2019.

VALUE AT RISK FOR FUNDING LIQUIDITY RISK IN 2019 in EUR millions

	31.01.2019		31.03.2019		30.06.2019		30.09.2019		31.12.2019	
	Limit	Used	Limit	Used	Limit	Used	Limit	Used	Limit	Used
Aggregate loss ceiling	3,800.0	2,529.6	3,800.0	2,848.8	3,800.0	3,071.8	4,300.0	3,120.2	4,300.0	2,504.4
Share of liquidity risks in %	13.2	14.5	13.2	13.8	15.8	15.3	16.3	17.1	16.3	19.1
Liquidity risks	500.0	365.8	500.0	391.8	600.0	469.9	700.0	534.0	700.0	479.0

In the previous year, the value at risk for the funding liquidity risk in the periodic perspective, i.e. over a projected period of twelve months with a confidence level of 99.0%, was EUR 42.7 million. In the liquidation perspective for the previous year, the value at risk for the funding liquidity risk was EUR 344.7 million with a confidence level of 99.98%. The increase in funding liquidity risks results from higher market values for interest rate derivatives, which is why the level of cash collateral to be provided – and thus refinanced – by L-Bank has risen in parallel.

The Controlling department is responsible for monitoring the funding liquidity risk by comparing the VaR figures calculated each month with the specified limits. The risk of possible future price increases due to higher expenses for follow-up refinancing (funding liquidity) is assessed with the help of various early warning indicators, based, among other things, on the owner's creditworthiness and an increase in the cost of short-term refinancing.

The Bank manages insolvency risk by means of qualitative performance ratios (liquidity coverage ratio – LCR, survival time frame); the Bank must comply with these ratios both in a credible baseline scenario and in an appropriately Bank-specific adverse scenario. Furthermore, the Board of Management has placed limits on monthly maximum liquidity needs and stipulated that the portfolio of securities in the ECB's deposit account may not fall below a specified minimum threshold. The Bank must also comply with the requirement to ensure that a sufficient liquidity buffer is always available, so that all payment obligations over the next 7 or 30 days are covered in both normal and stress scenarios.

The basis for the operational management of insolvency risk is 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 following two months. A monthly analysis is produced for any remaining months in the fiscal year, and for the following fiscal year.

Subsequently, an annual review is carried out. When producing this liquidity forecast, the Bank assumes that contractual maturities will apply.

The baseline scenario matches the baseline scenario created for the purpose of checking the normative perspective on the Bank's risk-bearing capacity.

In fiscal year 2019, neither the LCR nor the survival time frame ever fell below the internally specified minimum thresholds.

The projections carried out as at 31 December 2019 also confirm L-Bank's future solvency.

Because the internally specified survival time frame is longer than the period stipulated in the Minimum Requirements for Risk Management (MaRisk) for checking the adequacy of the free liquidity buffer, the available liquidity buffer is always sufficient to ensure the Bank's compliance with the specified survival time frame.

All risk management policies were complied with at all times during fiscal year 2019. The Board of Management is informed of liquidity risks in a daily risk report and a monthly aggregated report, which is distributed to the Risk Committee/Supervisory Board on a quarterly basis.

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.

Operational risks resulting from unlawful actions detrimental to the Bank are assessed by means of a threat analysis. Risks arising from outsourced services that fail to comply with contractual terms are accounted for in the materiality analysis of outsourced contracts. Whereas central risk managers are appointed by the Board of Management, the role of decentralised risk manager is generally fulfilled by the heads of individual departments, who may also delegate specific tasks to departmental staff as part of their organisational remit.

Assessment procedures and management

The size and scope of operational risks are identified and assessed with the aid of structured interviews across all departments. These interviews are held throughout the year. Any risks identified are assigned to one of five loss-level or loss-frequency classes. These are measured by the impact on L-Bank's financial position of a potential risk were it to materialise, and also the anticipated frequency of such an occurrence. The Bank is obliged to resort to estimates simply because, to date, the Bank has only experienced a minimal number of loss events associated with operational risks, and the consequential damages have been negligible. Hence it is not possible to calculate the VaR on the basis of historical loss events alone. An aggregated VaR for the bank as a whole is calculated from experts' estimates with the help of a Monte Carlo simulation.

VALUE AT RISK FOR OPERATIONAL RISK IN 2019 in Mio. Euro

	31.01.2019		31.03.2019		30.06.2019		30.09.2019		31.12.2019	
	Limit	Used	Limit	Used	Limit	Used	Limit	Used	Limit	Used
Aggregate loss ceiling	3,800.0	2,529.6	3,800.0	2,848.8	3,800.0	3,071.8	4,300.0	3,120.2	4,300.0	2,504.4
Share of operational risks in %	1.32	1.08	1.32	0.93	1.32	1.16	1.16	1.02	1.16	1.30
Operational risk	50.0	27.4	50.0	26.5	50.0	35.6	50.0	31.9	50.0	32.6

The Controlling department is responsible for monitoring operational risk by comparing the VaR figures calculated each quarter with the specified limits. The Board of Management is informed of operational risk in the monthly risk report, which is distributed to the Risk Committee/Supervisory Board on a quarterly basis.

The changes in the VaR in 2019 are due to changes in the experts' assessments of individual risk-bearing transactions. Due to their modest number and impact, claims had no influence on these assessments.

In addition to the usual insurance policies taken out to mitigate the business impact of certain loss events, the internal control system acts as the basis for avoiding operational risks. It includes comprehensive implicit and explicit procedures for safeguarding the Bank's process workflows. Typical procedures include two-person verification, random spot checks, explicit steps to take in the event of changes to operating processes or structures, an IT permissions management system that excludes conflicts of interest between incompatible activities, and 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.

To ensure that the Bank only enters into business transactions that it can process and manage in a manner commensurate with the associated risk, a new product process is applied to all new types of business. Prior to first-time acceptance, test cases are used to determine the extent to which existing processes and procedures are sufficient to map the new type of business. In each case, the result of these test runs is a concept that is used to present all HR, organisational, IT, accounting and fiscal consequences associated with the new business.

Operational risk is also reduced through ongoing monitoring of adherence to relevant legal and regulatory provisions (e.g. compliance, prevention of money laundering and fraud, data protection). The aim of the Compliance department is to exclude risks that could arise from non-compliance with legal requirements. Consequently, the department's role is to help implement effective procedures to ensure that L-Bank complies with the statutory regulations and policies that govern the Bank's activities, and to put in place the necessary controls. Compliance with these requirements is assured by appropriate organisational measures and the ongoing monitoring of relevant business transactions.

Given the Bank's portfolio structure, transfer and conversion risks are generally of very limited significance. The risk that L-Bank might suffer losses as a result of restrictions on payment transactions and/or currency convertibility as a result of statutory interventions in or against the countries involved is regarded as negligible.

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 and IT user manuals, on the other hand, describe specific processes. L-Bank has broken down the entire loan administration process into multiple stages: granting of loans, further processing of loans and processing of problem loans (restructuring and workout). 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 transactions 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 specify where particular business activities are carried out (organisation chart and schedule of responsibilities). The rules governing 'management and representation' specify who may carry out specific business activities. Finally, service agreements and employment policies are used to comply with statutory requirements pertaining to employment law and industrial relations.

Outlook for risk situation

In the year under review, L-Bank's excellent position on the capital market – supported by the State of Baden-Württemberg's guarantee – meant that refinancing could be obtained on terms that were favourable to both the Bank and its investors' interests. The Bank continues to be able to obtain refinancing on very favourable terms thanks to the explicit guarantee provided by the State of Baden-Württemberg and the latter's unchanged first-class credit ratings. The ongoing high international demand for liquid and safe investments will continue to offer the Bank broadly diversified and reliable opportunities to raise capital in the future.

The Bank's market price risk is due mainly to the longer-term investment of equity. Risks to earnings are due to the ongoing low level of interest rates. An increase in interest rates would gradually lead to higher investment income.

Low interest rates do, however, justify the assumption that clients will still be able to service their capital in the future and that no higher risk provisioning will be necessary.

With respect to operational risk, the Bank assumes that higher expenses will be incurred to meet various external requirements in particular.

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 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 regularity and reliability of the Bank's accounting functions. The accounting process set down in this system covers everything from the booking and processing of a business transaction through to the preparation of the annual financial statements and management report. L-Bank's senior management team 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 department and the Payment Transactions and Trade Settlement department. In addition, the Internal Audit unit carries out regular, process-independent checks 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 the Accounting department's involvement in the standardised process for introducing 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 archived in compliance with the statutory time frames.

The departments most heavily involved in the accounting process have clearly separated functions. The Payment Transactions and Trade Settlement department manages sub-ledgers for loans, securities, and debt and equity accounting. The data is transferred to the general ledger via an automated interface.

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.

L-Bank uses standard software for its financial accounting. This provides

- protection against unauthorised access through a system of permissions based on authorisation levels,
- prevention of errors by means of plausibility checks,
- detection of errors by means of two-person verification, standardised reconciliation routines, and comparisons of budgeted with actual figures.

At the same time, these measures serve to ensure that assets and liabilities are correctly assigned and reported, and also plausibly valued.

The annual financial statements and management report are derived from the Bank's financial accounting. For the management report in particular, financial and risk control data is obtained from the internal management information system, which is subject to a comparable system of internal controls. The annual financial statements and management report are also subject in their entirety to additional manual controls based on the two-person verification principle (routine double checks).

Up-to-date, reliable and relevant reports on the risk management system as it applies to accounting are regularly submitted to senior management and heads of department. Senior management provides the Supervisory Board and its committees with regular updates on the progress of the Bank's business activities. They also provide ad-hoc reports on exceptional events, as and when they occur.

Karlsruhe, 3 March 2020

Edith Weymayr Dr. Ulrich Theileis

Dr. Iris Reinelt Johannes Heinloth

Separate Non-financial Report – Report of the Board of Management of L-Bank for fiscal year 2019

Background, classification and methodology

The business activities of Landeskreditbank Baden-Württemberg – Förderbank – (L-Bank) are focused on the sustainable development of the Bank and the State of Baden-Württemberg. All the Bank's actions are based on its statutory public-service mandate. To fulfil this mandate, L-Bank's actions must always be exemplary and entirely trustworthy. The L-Bank Sustainability Guidelines and Sustainability Code serve as a frame of reference. The Bank established a Bank-wide sustainability management system in 2013, and the sustainable development model was incorporated into the Bank's business strategy to act as a framework for the Bank's business activities.

With the entry into force of the Paris Convention, the international community has committed itself under international law to limiting global warming. At the same time, the Agenda 2030 for Sustainable Development has established an ambitious list of 17 Sustainable Development Goals (SDG). It assigns an important role to the financial sector. To achieve the agenda's goals, it will be important to establish a financial system that prioritises sustainability and supports social transformation. Politicians and regulators are vigorously pursuing this agenda at various levels. To take account of the complexity and dynamics involved, in 2019 the Board of Management decided to set up a Sustainable Finance working group. Its role will be to assess developments from a strategic Sustainable Finance perspective and develop suitable options for future action by L-Bank.

Sections 289b to 289e HGB extend the statutory requirements for documenting the impacts of L-Bank's business activities. These requirements are discussed in a separate non-financial report, which forms a chapter in the annual report. The disclosures in the non-financial report were subjected to a limited-assurance audit ('engagement') of business operations by auditing firm PwC in accordance with ISAE 3000 (Revised), and the limited-assurance engagement was awarded an unqualified auditor's opinion. The way in which the content of the non-financial report is structured reflects the relevant legal requirements. The report is based on the Sustainability Reporting Standards of the Global Reporting Initiative (GRI). These act as the framework for the non-financial report's descriptions of management approaches and the underlying concepts.

In an interdisciplinary, multistage process, various non-financial criteria or 'aspects' (environmental matters, employee-related matters and social matters; respect for human rights; prevention of bribery and corruption) were assessed for their relevance to L-Bank, and the individual components were then reassessed in terms of materiality within the meaning of Section 289c (3) HGB. An additional aspect specific to L-Bank was also identified. The results are shown in the table below.

NON-FINANCIAL ASPECT	COMPONENTS DEFINED AS MATERIAL PURSUANT TO SECTION 289C (3) HGB
Environmental matters	Ecological value added/impact of products
Employee-related matters	Working conditions, personnel development, personnel planning and recruitment
Social matters	Support for entrepreneurship, social value added and development products
Respect for human rights	Protection of personal data – informational self-determination, freedom of assembly and freedom to bargain collectively
Prevention of bribery and corruption	Prevention of money laundering, prevention of terrorist financing
Client matters (additional aspect)	Corporate security, digitisation of business partner relationships, product portfolio/services offered

In fiscal year 2019, and as at the reporting date, no material net risks have been identified that are having, or will be very likely to have, severely negative impacts on the above-mentioned aspects. No references to issues associated with the amounts reported in the annual financial statements were required, nor were any additional explanations.

L-Bank's business model and the way it has been implemented in each of the Bank's areas of development activity, as well as the relevant figures, are described in the 'Background' and 'Economic Report' sections of the management report. In accordance with the Minimum Requirements for Risk Management (MaRisk) in banking institutions, L-Bank has installed a risk management system that is Bank-specific and optimised to meet the requirements of L-Bank's statutory public-service mandate. L-Bank reports on this in the 'Opportunities and risk report' section of the management report.

Environmental matters

According to the state constitution, all public institutions in Baden-Württemberg are responsible for protecting the natural environment and its resources for future generations. Climate protection has been firmly embedded in Baden-Württemberg's legislation since 2013. With this in mind, the federal state has set itself the goal of organising the state's administrative bodies so they are largely climate-neutral by 2040. L-Bank has voluntarily adopted this objective for its own business management. In doing so, the Bank regards itself as having a dual duty to protect the environment and the climate; first, as a development bank providing relevant incentives to private individuals, municipalities and businesses, and second, by acting as a role model for other companies and society as a whole. To fulfil this obligation, L-Bank has implemented an integrated environmental management system validated under EMAS and certified to ISO 14001:2015 standard.

EMAS follows a three-year cycle, and in 2019, the environmental management system was successfully revalidated and recertified. L-Bank's environmental indicators are recorded and evaluated annually, validated by an independent environmental auditor and published in the Bank's environmental statement.

L-Bank's carbon footprint amounted to 991 tonnes of CO_2 equivalents (CO_2e) in 2019, breaking down as follows:

Direct greenhouse-gas emissions (GHG emissions) (Scope 1)*	190 tonnes CO_2e
Indirect GHG emissions from energy supply (Scope 2)	483 tonnes CO_2e
Other indirect GHG emissions (Scope 3)	318 tonnes CO_2e
Total	**991 tonnes CO_2e**

* The decline in Scope 1 emissions compared to the previous year can be attributed, among other things, to the replacement of a faulty cooling system.

The Bank's carbon footprint was calculated using the methodology provided by the Association for Environmental Management and Sustainability in Financial Institutions (Verein für Umweltmanagement und Nachhaltigkeit in Finanzinstituten e.V. – VfU), as updated in 2018 (version 1.3). Scope 3 includes, for example, GHG emissions from business travel, outsourced activities, water treatment and waste treatment. It also includes GHG emissions associated with consumables.

L-Bank uses development programmes to provide investment incentives for greater energy-efficiency, environmentally compatible refurbishment and the use of renewable energies. Thus the Bank indirectly contributes to reducing carbon emissions. Many of L-Bank's housing development products provide direct incentives for environmental and climate protection. The 'Resource Efficiency Finance' development programme exerts significant influence as an incentive for environmental protection measures, encouraging businesses to save energy and materials. This programme, offered in conjunction with the Ministry of Economic Affairs, Labour and Housing and the Ministry of the Environment, Climate and Energy, awards low-interest development loans, in some cases with repayment subsidies, to small and medium-sized businesses (see also the 'Economic report' section of the management report).

The 'Digital Filing' system already in use by individual departments is being rolled out across the whole of L-Bank. The project is currently in the implementation phase.

Employee-related matters

L-Bank's long-term success is based on the hard work of its employees. As part of its strategic approach to corporate governance, L-Bank's personnel strategy is based on the Bank's business strategy. Among other things, it includes the Bank's remuneration and recruitment strategy, personnel planning and a fully integrated staff development plan. Personnel planning involves analysing how many employees L-Bank needs and which skills sets and abilities these employees should have. The next step involves deciding whether the identified needs should be covered by in-house professional development training or by recruitment. Personnel planning is refined in the light of the specialist departments' objectives, which include planning criteria for staffing. External recruitment needs are established after assessing them against the CPD options for current L-Bank employees, whose future prospects are always given priority. Working conditions and employee benefits are designed to optimise L-Bank's attractiveness as an

employer. This serves to both attract and retain highly qualified employees. As an important part of business planning, personnel planning and recruitment are approved by the Board of Management. The recruitment strategy calls for even more vigorous recruitment of junior staff by expanding training opportunities for and retaining trainees, students at the Baden-Württemberg Cooperative State University (DHBW Mosbach) and working students. In addition, L-Bank uses a phased retirement programme to structure the transition from one generation of employees to the next; this makes the planning process more dependable.

L-Bank's employee competencies are managed and further developed by systematic staff development courses based on the 360-degree personnel development plan adopted by the Board of Management. All training and continuing education initiatives take account of the ever-shortening half-life of knowledge. The design of the staff development programme is discussed and approved by the interdepartmental Personnel Development committee. The committee is a decision-making body that meets several times a year.

Attractive training schemes are central to L-Bank's development of junior staff. The range of training courses on offer is constantly reviewed and, where necessary, adapted to the Bank's operational circumstances and needs. To deliver this training, L-Bank works closely with DHBW Mosbach and the Chamber of Industry and Commerce (IHK). L-Bank offers high-school graduates work-study places as students specialising in Business Administration for Banks, and in Business IT. In 2020, this offer will be extended to cover computer science. In addition, L-Bank offers a wide range of training opportunities, including a trainee programme, apprenticeships for aspiring chefs, winemakers and, starting in 2020, IT specialists, as well as voluntary work and internships. In-house talent management is a key element in employees' continuing professional development (CPD). Based on L-Bank's skills profile, it opens up a wide variety of CPD options for employees by focusing on their strengths. Employees are given the opportunity to participate in the staff development programme and thus develop new career prospects.

Employees spend a large part of their lives in the workplace, so working conditions have a major impact on their overall physical and mental well-being. The Bank's Code of Ethics and Conduct forms the basis for teamwork and collaboration. The code formulates binding principles, values and standards of conduct for all Bank employees.

L-Bank fulfils its duty of care by protecting its employees from health hazards arising at work or through work. Occupational health and safety are continuously developed with the active involvement of employees and the Staff Council. The central body is the Occupational Safety Committee, which meets quarterly. The committee discusses any issues arising, agrees corrective actions and monitors their implementation. As part of the EMAS audit, an external environmental auditor checks whether the Bank is complying with the relevant environmental protection and occupational safety regulations and standards. The Bank uses risk assessment to ensure that hazards to which employees are exposed in the course of their professional activities are identified, assessed and eliminated by taking the necessary steps. As part of the ongoing occupational safety review, L-Bank carried out a risk assessment of mental stress in 2017. In the year under review, the first steps emerging from the assessment's recommendations for action were implemented.

Of particular importance to L-Bank is occupational health management that focuses on prevention. At the Bank's in-house health centres, for example, employees can train on stamina-building machines and use special back-training equipment.

Further information on employee-related matters can be found in the 'Personnel' section of the management report.

Social matters

In the economic system favoured by social market economies, companies are the initiators and facilitators of change and progress, thereby safeguarding a society's prosperity. While the economic platform represents one side of the social equation, social cohesion is the other. To build a strongly cohesive society, it is vital to promote equal opportunities. L-Bank's development objectives and operational targets are all guided by the State of Baden-Württemberg's development policy.

L-Bank offers a broad range of social development services, ranging from family benefits to the creation of affordable housing. These include the promotion of equal opportunities, accompanied by the promotion of entrepreneurship and job creation, as the basis of a successful social market economy. In 2019, development applications for the construction of new social housing for rent and regulated tenancies for existing social housing for rent were approved for around 2,600 residential units in Baden-Württemberg, of which 2,100 related to new-build projects. Once again, the barely acceptable minimum threshold of 1,500 residential units per year identified as the breakeven point in the Prognos report was substantially exceeded in 2019.

In terms of family support, for example, L-Bank is the central issuer of family allowances in Baden-Württemberg. The relative significance of each development programme in terms of volume is discussed in the 'Economic report' section of the management report.

The starting point for all development projects is the provision of development funding. To safeguard its development business in the long term – not least from a regulatory perspective – L-Bank set up the development contribution system described in the 'Financial performance' section of the management report.

So that development funding does not distort competition in the commercial sector, L-Bank ensures that all development programmes are implemented in accordance with European Union rules on state aid. Depending on the development programme, L-Bank carries out contract-award and state-aid audits as one of the steps in the development finance process. Irrespective of the individual development programme, L-Bank uses documentary evidence to ensure that public funding is used appropriately.

Entrepreneurship is the foundation of market economies and the driving force behind economic development. L-Bank supports entrepreneurship by providing advice and training, by raising awareness and through its development funding programmes. The Bank aims to work with the State of Baden-Württemberg to create attractive conditions for entrepreneurship and thus create and safeguard jobs in Baden-Württemberg. L-Bank supports fledgling companies and SMEs at various stages of development and in every business situation by providing suitable instruments – from debt financing to quasi-equity financing, and from equity and sureties through to grants awarded on behalf of the federal state. Furthermore, by building technology parks, the Bank is creating an innovation-friendly environment. Another L-Bank priority is the provision of funding for projects of particular significance for the future viability and competitiveness of Baden-Württemberg's businesses; this includes the Digitisation Premium which forms part of the state-wide digitisation strategy.

L-Bank extends loans for business development purposes using the 'borrower's bank' principle. The commercial banks ensure that funding requirements are met and, once the project has been completed, provide L-Bank with proof that the public funding has been used as intended. L-Bank ensures that the process of extending loans is carried out lawfully by auditing commercial banks on a spot-check basis. To identify changing needs as early as possible, L-Bank commissions studies from specialist third parties.

These enable the Bank to further refine the Bank's existing development finance products to meet real-world needs, thereby ensuring that the public funding provided adds the desired social value. L-Bank also runs promotional campaigns to raise public awareness of the importance of entrepreneurship. Competitions such as the state-wide Start-up BW Elevator Pitch and the State Prize for Young Companies play an important role here.

Respect for human rights

Human rights are fundamental rights protecting the freedom and autonomy of every individual. Respect for human rights is a central standard in all L-Bank's business activities and part of its self-image as a state-owned company. Thanks to L-Bank's compliance with statutory and legal regulations, and taking into account the fact that the Bank's development business is limited to Baden-Württemberg, there is no material risk that the Bank could violate the rights of indigenous peoples or come into conflict with forced or child labour. With the adoption of the National Action Plan on Human Rights (NAP) in 2016, the German federal government aims to further improve the human rights situation. Building on an impact analysis, companies should assume their share of the responsibility for this. The foundations for further developing L-Bank's human rights due diligence processes have been laid in the form of the Bank's 'FIT FOR NAP' programme. The existing procedure was consolidated by means of an industry analysis.

As a public-sector contracting authority, L-Bank complies with the Public Procurement Directives and all relevant laws when awarding contracts. This ensures that all companies involved comply with their legal obligations when executing commissions.

A complaints management system safeguards the fundamental right to report violations by, or make complaints about, the Bank. The system was evaluated last year, and further steps were taken towards process standardisation.

The legal basis for the protection of personal data is the General Data Protection Regulation (EU GDPR). This embodies the basic right to informational self-determination: every individual has the right to decide for him- or herself who collects, processes or uses which parts of his or her personal information. It is vital to protect the personal data of clients and partners, as well as employees. L-Bank safeguards the right to informational self-determination, hence also to data protection, by means of IT systems, clearly defined processes and the conduct of its employees. Upon joining L-Bank, every new employee is given a mandatory training course in data protection.

The Board of Management has appointed a Data Protection Officer. The latter is the main point of contact and source of information for data protection issues and submits regular reports to the Board of Management. In 2019, there were no data protection incidents that needed to be reported to Baden-Württemberg's State Commissioner for Data Protection, as required by law.

As both employer and contracting authority, L-Bank has an impact on human and labour rights. Freedom of assembly and the right to collective bargaining are fundamental to the protection of workers' rights. Because L-Bank's employees work in Germany, we believe that we comply with and guarantee our employees' rights by complying with Germany's statutory regulations. The State Staff Representation Act (Landespersonalvertretungsgesetz) governs the representation of employee interests at L-Bank, hence also employees' operational participation. Staff interests are represented by a Central Staff Council,

responsible for handling issues at all Bank locations, and by two local Staff Councils, in Karlsruhe and Stuttgart, respectively.

Employer and staff representatives work together in a spirit of partnership and trust, in compliance with German legislation and collective bargaining agreements, for the benefit of all employees and to fulfil the duties incumbent upon the council. The Staff Council exercises its rights of participation through co-determination, collaboration and consultation. In addition, the Chair of the Central Staff Council and the two Chairs of the Karlsruhe and Stuttgart Staff Councils sit on L-Bank's Supervisory Board in an advisory capacity, as consulting members.

Prevention of bribery and corruption

L-Bank's credibility and success are directly related to the personal integrity and honesty of all individuals acting on behalf of L-Bank. In view of this, a sound and responsible approach to corporate governance is a self-evident component of the Bank's corporate culture. L-Bank has enshrined the Public Corporate Governance Code of the State of Baden-Württemberg in the Bank's in-house rule book by resolutions of both the Board of Management and Supervisory Board, and observes all provisions of the code. L-Bank does not tolerate any form of corruption or bribery. This attitude is also reflected in the Bank's Code of Ethics and Conduct. Whenever further regulations and process descriptions are required over and above this set of values, they are supplemented and defined by internal guidelines (operational directives).

The fight against bribery and corruption has many facets. As a financial institution, the prevention of money laundering and the financing of terrorism are material issues for L-Bank. Our management approach is based on compliance with legal and regulatory requirements. The central unit set up within the Bank to prevent money laundering, terrorist financing and other crimes, which forms part of the Compliance unit, enjoys the full support of the Board of Management. The Compliance unit ensures compliance with internal, statutory and regulatory provisions and policies by monitoring compliance with due diligence requirements and other precautionary policies. The Compliance unit reports directly to the Board of Management at departmental level, and all heads of compliance-related functions – such as the Compliance Officer, Money Laundering Officer and Compliance Officer for the purposes of the German Securities Trading Act (WpHG), as well as their corresponding deputies – work out of this unit. All internal security measures required under Section 25h KWG in conjunction with Section 6 GwG have been implemented. Employees who wish to report their suspicions of possible violations of the legal provisions that apply to L-Bank can use an internal whistle-blowing system for this purpose, which also allows reports to be made anonymously. The confidential treatment of this information is a top priority for L-Bank.

Risk analyses are used as the basis for devising security measures for preventing money laundering and terrorist financing, tailored specifically to L-Bank. Every two years, Internal Audit checks whether, and to what extent, laws are being correctly implemented and applied, and also checks compliance with internal guidelines (operational directives).

When new recruits join L-Bank, they are given mandatory in-house training on the prevention of money laundering and fraud, securities compliance, data protection and information security. In departments to which money laundering is relevant, supplementary

training courses are compulsory every three years. The Bank monitors participation in these courses. To prevent fraud and other criminal acts, staff are given extended training courses every three years.

Identifying contractual partners pursuant to Section 10 (1) article 1 of the Anti-Money Laundering Act (AMLA) is one of the most important aspects of the Bank's general duty of care towards clients. L-Bank has set up the processes and procedures necessary to fulfil this duty of care. Here, L-Bank's business model as a development bank which does not accept deposits from the general public, and which has neither branches nor cash operations, was considered to mitigate the risks associated with the prevention of money laundering and terrorist financing.

The multiple-control principle applied by L-Bank ensures that important decisions which must be made when, for example, onboarding new clients or engaging in critical activities, are neither made nor implemented by a single individual. In addition to the multiple-control principle, powers of authorisation are clearly defined and regulated in an internal guideline (operational directive).

A comprehensive reporting system ensures that the Board of Management is continuously updated on these issues. The Board of Management is informed, on a monthly basis, of any regulatory risks arising from supervisory regulations or regulatory projects that have been identified as relevant. The Board of Management is informed of the results of ongoing controls in quarterly reports on operational compliance. This quarterly report covers all areas of the Compliance unit's responsibilities, including money-laundering and fraud prevention, corporate compliance and securities compliance. The corresponding annual reports on compliance are submitted to the Board of Management once per calendar year. In addition, ad-hoc reports are submitted to the Board of Management if there is any suspicion of serious compliance violations.

In short, L-Bank has the resources and internal procedures at its disposal to detect and prevent money-laundering operations involving profits from terrorist activities, organised crime or other serious criminal offences.

Client matters

As the State Bank, L-Bank issues public development funding for the whole of Baden-Württemberg. L-Bank's principal, the State of Baden-Württemberg, as well as its development clients and business partners, expect L-Bank to process their requests swiftly and cost-efficiently while applying a high level of data security.

Digitisation is enabling L-Bank to operate more efficiently and establish new relationships with clients and business partners. In its business strategy, L-Bank has given a high priority to the gradual digitisation of internal processes, as well as the various interfaces with clients and business partners. Together with the Bank's IT strategy, digitisation is the most concrete reflection of the technological direction taken by the Bank. While the IT strategy contains information on the restructuring of IT systems and IT processes, it is also the basis for the ongoing phased development of the Bank's value chain and the configuration of client contact points.

In its digitisation efforts, L-Bank is dependent on client-side developments, as well as developments among business and joint-venture partners. One example of this is the online system for family allowance applications, which was implemented in May 2019 in close collaboration with the Ministry of Social Affairs and Integration, and in partnership with the Ministry of the Interior.

L-Bank also regards itself as a provider of information on all aspects of development finance. For this purpose, L-Bank has fundamentally revised its online presence over the last few years. Since May 2019, L-Bank's website has been divided up into three portals for three different target audiences: www.l-bank.de for development finance clients, www.l-bank.info for stakeholders, applicants, journalists and investors, and expertenportal.l-bank.de for financing partners, financial intermediaries and development agencies.

With the L-Bank funding calculator for state housing development, access to home ownership funds has become considerably easier and the attractiveness of L-Bank's online services has been further enhanced. The funding calculator is also a key component in the gradual digitisation of state housing assistance. Another element in our social home ownership programme is the very personal client support we have been offering since early August as part of a pilot project in partnership with the state housing development agency in Heilbronn. If it becomes apparent that online (digital) advisory sessions are generally suitable for supporting social home ownership, and that they are accepted by the target market, we plan to extend the service to other housing development agencies.

L-Bank's aim is to make the most of these opportunities by digitising and automating the Bank's intermediation business to make the sale of development finance products even more efficient and client-centric for L-Bank and its financing partners. With this in mind, L-Bank linked residential housing products offered via clients' commercial banks to KfW's 'Bankdurchleitung Online 2.0' (BDO 2.0) platform back in 2016. In the course of the year, KfW and L-Bank agreed not to pursue the integration of L-Bank's residential housing products into KfW's development finance portal, originally planned for 2019. In view of the fundamental importance of projects with a strategic focus on the low-interest/negative-interest conditions prevailing in 2020, L-Bank and KfW have also deferred the implementation of a project to set up a central development finance platform for the federal state's development agencies.

With respect to the Bank's intermediation business, L-Bank has entered into a partnership with an online brokerage portal. Brokered commercial development loans from L-Bank can be incorporated into attractive financing solutions. This provides companies with even greater transparency and strengthens the tried-and-tested 'borrower's bank' principle.

The Portfolio Management committee coordinates and prioritises the Bank's individual digitisation projects, reporting to the Board of Management on the status of the project portfolio at least every quarter. Rules have been defined for the change process: the operational risks are assessed and managed; the process follows the defined new product process where appropriate, and the level of protection is determined by a Security Office that is independent of the Bank's operational IT units. In terms of process, scrum methodology is used, following an agile software development approach. The IT security strategy is used to support this approach, enabling L-Bank to protect business partners and specialist knowledge from attacks by third parties. In particular, the Security Office is responsible for supporting the Board of Management in all matters relating to corporate security. For this purpose, the office runs a fully integrated management system which, in addition to managing information security, also takes care of emergency planning and physical security, as well as continuous process improvement. Security Office activities are always based on a factually relevant, cross-departmental approach. The office reports to the full Board of Management as and when required, or else once a quarter.

Karlsruhe, 3 March 2020

Edith Weymayr Dr. Ulrich Theileis

Dr. Iris Reinelt Johannes Heinloth

Report of the Supervisory Board

During fiscal year 2019, the Supervisory Board and the committees set up by the Board discharged the duties assigned to them by law and by the Bank's articles of association and standard operating procedures. In particular, the Supervisory Board monitored the orderly conduct of the Bank's business. For this purpose, pursuant to the relevant statutory provisions, as well as the Bank's articles of association and rules of procedure, the Board of Management regularly briefed the Supervisory Board and its committees on the development of the Bank's business and risk exposure, as well as major and material business transactions throughout 2019.

The Supervisory Board and its committees discussed and made decisions on matters falling within the scope of its/their responsibilities, as well as any business transactions that required its/their approval. To determine the guidelines for business activities, the Supervisory Board discussed business policy issues with the Board of Management and, in particular – following prior discussion in the Risk Committee – approved the Bank's business and risk strategy.

The Supervisory Board consists of 15 voting members and three consulting members. The composition of the Supervisory Board changed in 2019 following the resignation of Minister Thomas Strobl and the appointment of Manuel Hagel (MSP). The Supervisory Board met three times in the course of 2019; the Supervisory Board's committees met a total of eleven times. Three of these committee meetings were held by the Risk Committee, three by the Audit Committee and four by the Personnel Committee; one meeting was held by the Remuneration Control Committee, newly constituted in 2018. Between meetings, urgent decisions were taken by written circular on a total of four occasions.

During the first half of 2019, the Supervisory Board's activities focused on the selection of a new Chair for L-Bank's Board of Management. Following a proposal by the Personnel Committee, which discussed the matter at several meetings, in June 2019 the Supervisory Board decided to appoint the new Chair of L-Bank's Board of Management with effect from 1 January 2020, and to extend the service contracts of two other Board of Management members.

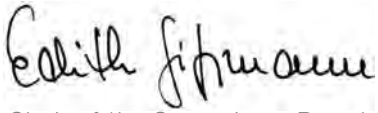
The Supervisory Board has reviewed the separate non-financial report for fiscal year 2019. PricewaterhouseCoopers GmbH Wirtschaftsprüfungsgesellschaft was commissioned to carry out an external limited-assurance engagement of the report's content. The auditor's notes on the report were discussed by the Supervisory Board and Audit Committee with the auditor's involvement. On completion of this review, the Supervisory Board concluded that no objection needed to be raised to the separate non-financial report for 2019.

PricewaterhouseCoopers GmbH Wirtschaftsprüfungsgesellschaft carried out the statutory annual audit for fiscal year 2019. An unqualified auditor's opinion was issued. The Audit Committee consulted with the auditor on the starting date of the audit. The auditor provided the Audit Committee with progress reports on the audit, and also took part in discussions of the 2019 financial statements by the Supervisory Board and Audit Committee. In these discussions, the auditors reported on the main findings of their audit activities, answered questions and provided additional information. The Supervisory Board and Audit Committee discussed the auditor's report. In accordance with the outcome of the audit, the Supervisory Board has concluded that the annual financial statements for 2019 prepared by the Board of Management do not give rise to any objections. Accordingly, in its teleconference/videoconference on 20 April 2020 and/or the accompanying written circular, the Supervisory Board took note of and approved the Bank's annual financial statements for 2019.

The Supervisory Board also approved the Board of Management's proposal to allocate EUR 50,000,000.00 of the distributable net profit for fiscal year 2019 (totalling EUR 50,959,453.24) to other retained earnings and to carry forward the remaining amount of EUR 959,453.24.

The Supervisory Board warmly thanks Dr. Axel Nawrath for his work as Chairman of the Board of Management of L-Bank and looks forward to working with Edith Weymayr, who succeeded him on 1 January 2020.

Stuttgart, 20 April 2020



Chair of the Supervisory Board
Edith Sitzmann MSP
Minister of Finance
for the State of Baden-Württemberg

L-BANK BALANCE SHEET AS AT 31 DECEMBER 2019

ASSETS	31.12.2019 EUR	31.12.2019 EUR	31.12.2019 EUR	31.12.2018 EUR
1. CASH RESERVE				
a) cash in hand		12,493.42		20,662.12
b) current balances with central banks thereof: with Deutsche Bundesbank EUR 3,754,815,808.51 (EUR 115,106,834.94)		3,754,815,808.51		115,106,834.94
			3,754,828,301.93	**115,127,497.06**
2. RECEIVABLES FROM BANKS				
a) due on demand		6,049,204.09		4,345,095.94
b) other claims		25,205,089,745.89		23,388,775,902.51
			25,211,138,949.98	**23,393,120,998.45**
3. RECEIVABLES FROM CLIENTS thereof: secured through real-estate liens EUR 4,472,206,792.20 (EUR 4,639,401,627.23) municipal loans EUR 9,728,171,238.56 (EUR 9,443,632,792.42)			**22,862,293,061.59**	**22,645,318,589.62**
4. BONDS, DEBENTURES AND OTHER FIXED-INCOME SECURITIES				
a) money-market instruments				
aa) from other issuers thereof: eligible as collateral with Deutsche Bundesbank EUR 720,998,218.29 (EUR 0.00)		1,486,202,306.73		0.00
b) bonds and debentures				
ba) from public issuers thereof: eligible as collateral with Deutsche Bundesbank EUR 5,332,302,106.15 (EUR 5,702,626,767.28)	5,457,789,593.27			5,810,502,419.97
bb) from other issuers thereof: eligible as collateral with Deutsche Bundesbank EUR 13,638,143,512.55 (EUR 13,700,304,026.50)	17,452,433,092.45			16,208,291,471.37
		22,910,222,685.72		22,018,793,891.34
c) own notes nominal value EUR 0.00 (EUR 5,000,000.00)		0.00		5,007,858.22
			24,396,424,992.45	**22,023,801,749.56**

ASSETS	31.12.2019 EUR	31.12.2019 EUR	31.12.2019 EUR	31.12.2018 EUR
5. ASSETS thereof: in financial institutions EUR 1,986,360.52 (EUR 1,986,360.52)			229,561,766.84	213,342,241.51
6. HOLDINGS IN AFFILIATED COMPANIES			8,909,201.00	17,809,201.00
7. FIDUCIARY ASSETS thereof: fiduciary loans EUR 23,621,267.30 (EUR 28,332,398.06)			23,621,842.84	28,333,004.16
8. INTANGIBLE ASSETS a) licences acquired for consideration, industrial property rights and similar rights and assets, and licences to such rights and assets			2,949,520.40	2,941,149.40
9. TANGIBLE ASSETS			75,910,130.29	100,338,468.10
10. OTHER ASSETS			283,186,524.93	212,555,709.19
11. ACCRUED ITEMS			773,732,491.14	856,184,326.02
TOTAL ASSETS			77,622,556,783.39	69,608,872,934.07

L-BANK BALANCE SHEET AS AT 31 DECEMBER 2019

LIABILITIES	31.12.2019 EUR	31.12.2019 EUR	31.12.2019 EUR	31.12.2018 EUR
1. LIABILITIES TO BANKS				
a) due on demand		11,480,127.01		8,566,884.64
b) with agreed term or notice period		25,976,466,757.13		25,854,349,148.30
			25,987,946,884.14	**25,862,916,032.94**
2. LIABILITIES TO CLIENTS				
a) other liabilities				
aa) due on demand		99,657,190.33		128,775,951.97
ab) with agreed term or notice period		10,657,108,095.99		8,884,340,932.51
			10,756,765,286.32	**9,013,116,884.48**
3. SECURITISED LIABILITIES				
a) notes issued			**34,450,313,104.27**	**28,277,890,956.05**
4. FIDUCIARY LIABILITIES				
thereof: fiduciary loans EUR 23,621,267.30 (EUR 28,332,398.06)			**23,621,842.84**	**28,333,004.16**
5. OTHER LIABILITIES			**23,309,943.69**	**24,704,683.98**
6. DEFERRED ITEMS			**1,596,639,151.77**	**1,702,864,474.81**
7. PROVISIONS				
a) provisions for pensions and similar obligations		336,679,009.00		293,190,920.00
b) tax provisions		100,000.00		100,000.00
c) other provisions		353,808,990.57		362,361,918.79
			690,587,999.57	**655,652,838.79**
8. SUBORDINATED LIABILITIES			**118,434,727.86**	**118,435,918.91**

LIABILITIES	31.12.2019 EUR	31.12.2019 EUR	31.12.2019 EUR	31.12.2018 EUR
9. PROFIT-SHARING RIGHTS OUTSTANDING thereof: due within two years EUR 143,000,000.00 (EUR 143,000,000.00)			**260,975,600.00**	**260,975,600.00**
10. FUND FOR GENERAL BANKING RISKS			**700,000,000.00**	**700,000,000.00**
11. EQUITY				
a) subscribed capital		250,000,000.00		250,000,000.00
b) capital reserve		1,048,002,789.69		1,048,002,789.69
c) retained earnings				
ca) other retained earnings		1,665,000,000.00		1,615,000,000.00
d) net profit		50,959,453.24		50,979,750.26
			3,013,962,242.93	**2,963,982,539.95**
TOTAL LIABILITIES			**77,622,556,783.39**	**69,608,872,934.07**

1. CONTINGENT LIABILITIES				
a) liabilities from sureties and guarantee contracts			**183,377,681.82**	**205,055,661.29**
2. OTHER COMMITMENTS				
a) irrevocable lending commitments			**3,591,023,484.64**	**4,698,672,915.93**

L-BANK STATEMENT OF INCOME FOR THE FISCAL YEAR 1 JANUARY TO 31 DECEMBER 2019

		2019 EUR	2019 EUR	2019 EUR	2018 EUR
1.	INTEREST INCOME FROM				
	a) lending and money market transactions	1,019,935,791.20			1,018,479,754.90
	b) fixed-income and book-entry securities	457,666,741.50			467,710,168.58
			1,477,602,532.70		1,486,189,923.48
2.	INTEREST EXPENSES		1,235,235,488.73		1,231,867,006.83
				242,367,043.97	**254,322,916.65**
3.	CURRENT INCOME FROM				
	a) shareholdings			**1,672,548.77**	**5,543,706.31**
4.	COMMISSION INCOME			**45,726,212.01**	**43,095,311.04**
5.	COMMISSION EXPENSES			**4,537,170.40**	**5,179,308.40**
6.	OTHER OPERATING INCOME			**8,433,872.60**	**25,613,301.63**
7.	GENERAL ADMINISTRATIVE EXPENSES				
	a) personnel expenses				
	aa) wages and salaries	81,551,021.63			77,763,229.10
	ab) social security contributions and expenses for pensions and other benefits thereof: for pensions EUR 14,722,757.96 (EUR 9,448,462.46)	28,274,527.34			22,219,136.02
			109,825,548.97		99,982,365.12
	b) other administrative expenses		64,512,302.27		60,087,157.94
				174,337,851.24	**160,069,523.06**
8.	WRITE-DOWNS AND VALUATION ADJUSTMENTS ON INTANGIBLE ASSETS AND TANGIBLE ASSETS			**5,621,347.59**	**7,859,946.60**

	2019 EUR	2018 EUR
9. OTHER OPERATING EXPENSES	28,245,927.51	14,352,887.77
10. WRITE-DOWNS AND VALUATION ADJUSTMENTS ON RECEIVABLES AND CERTAIN SECURITIES AS WELL AS ADDITIONS TO PROVISIONS FOR LOAN LOSSES	44,007,912.40	46,542,000.60
11. INCOME FROM REVALUATION OF RECEIVABLES AND SELECTED SECURITIES AS WELL AS FROM REVERSALS OF LOAN-LOSS PROVISIONS	8,941,866.59	6,683,998.10
12. ADDITIONS TO FUND FOR GENERAL BANKING RISKS	0.00	50,000,000.00
13. INCOME FROM ORDINARY BUSINESS ACTIVITIES	50,391,334.80	51,255,567.30
14. TAXES ON INCOME AND EARNINGS	260,975.65	900,712.96
15. OTHER TAXES NOT STATED UNDER ITEM 9	150,656.17	177,866.86
16. NET INCOME	49,979,702.98	50,176,987.48
17. PROFIT CARRIED FORWARD FROM THE PREVIOUS YEAR	979,750.26	802,762.78
	50,959,453.24	50,979,750.26
18. NET PROFIT	50,959,453.24	50,979,750.26

L-BANK CASH FLOW STATEMENT FOR THE FISCAL YEAR 1 JANUARY TO 31 DECEMBER 2019

	01.01.–31.12.2019 EURk	01.01.–31.12.2018 EURk
Net profit/loss for the period	49,980	50,177
Amortisation, value adjustments and write-ups on receivables including contingent liabilities and securities	38,507	102,766
Depreciation/amortisation, value adjustments and write-ups on tangible assets and intangible assets	5,621	7,860
Amortisation, value adjustments and write-ups on financial assets (excluding securities)	6,807	8,364
Change in provisions (excluding loan-loss provisioning)	125,773	99,031
Profit/loss on the sale of tangible and intangible assets	–1	–17,058
Profit/loss on the sale of financial assets	–14,408	–12,648
Other adjustments (net)	–85,834	–98,612
Change in receivables from banks	–1,817,485	479,715
Change in receivables from clients	–257,749	1,435,901
Change in securities	–2,368,696	–885,102
Change in other assets from operating activities	16,531	–22,842
Change in liabilities to banks	125,031	594,183
Change in liabilities to clients	1,743,648	1,004,561
Change in securitised liabilities	6,172,422	–2,105,526
Change in other liabilities from operating activities	–205,362	–768,208
Net interest income	–242,368	–254,323
Income taxes charges	261	901
Interest payments and dividend payments received	1,518,649	1,573,682
Interest paid	–1,190,448	–1,220,747
Income tax payments	–261	–901
Cash flow from operating activities	**3,620,618**	**–28,826**
Proceeds from sales of financial assets	25,887	25,612
Disbursements for investments in financial assets	–25,605	–62,758
Proceeds from sales of tangible assets	24,093	18,642
Disbursements for investments in tangible assets	–4,275	–6,439
Disbursements for investments in intangible assets	–1,018	–2,788
Cash flow from investment activities	**19,082**	**–27,731**
Proceeds from additions to shareholders' equity	0	48,576
Cash flow from financing activities	**0**	**48,576**
Cash and cash equivalents at start of period	115,128	123,109
Cash flow from operating activities	3,620,618	–28,826
Cash flow from investment activities	19,082	–27,731
Cash flow from financing activities	0	48,576
Cash and cash equivalents at end of period	**3,754,828**	**115,128**

L-BANK STATEMENT OF CHANGES IN EQUITY AS AT 31 DECEMBER 2019

	Subscribed capital EURk	Reserves			Net profit EURk	Equity EURk
		Capital reserve pursuant to Section 272 (2) art. 4 HGB EURk	Other retained earnings EURk	Total EURk		
Balance as at 31.12.2017	**250,000**	**999,427**	**1,565,000**	**2,564,427**	**50,803**	**2,865,230**
Transfer to reserves		48,576	50,000	98,576	–50,000	48,576
Net income for the year					**50,177**	**50,177**
Balance as at 31.12.2018	**250,000**	**1,048,003**	**1,615,000**	**2,663,003**	**50,980**	**2,963,983**
Transfer to reserves			50,000	50,000	–50,000	0
Net income for the year					**49,979**	**49,979**
Balance as at 31.12.2019	**250,000**	**1,048,003**	**1,665,000**	**2,713,003**	**50,959**	**3,013,962**

NOTES TO THE ANNUAL FINANCIAL STATEMENTS OF L-BANK AS AT 31 DECEMBER 2019

GENERAL PRINCIPLES

L-Bank (Landeskreditbank Baden-Württemberg – Förderbank –) was established by a law passed on 11 November 1998, effective as from 1 December 1998. It is the development bank of the German federal state of Baden-Württemberg. The Bank's business activities are governed by its statutory remit, namely to support the state government of Baden-Württemberg in the fulfilment of its duties, especially in terms of structural, economic and social policy, by implementing development programmes that comply with European Union regulations governing state aid.

L-Bank has its head office in Karlsruhe, with a branch office in Stuttgart. It is entered in the commercial register of the City of Mannheim under number HRA 104441. Section 2 (1), sentence 1 of the above-mentioned law sets the share capital of L-Bank at EUR 250 million.

The annual financial statements of L-Bank were 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. Additions to the fund for general banking risks are shown in a separate item.

When taken together, the majority shareholdings reported are of secondary importance. Preparation of a consolidated financial statement was thus waived pursuant to Section 290 (5) HGB in conjunction with Section 296 (2) HGB.

The disclosures required pursuant to Section 26a (1) sentence 2 of the German Banking Act (KWG) (country-by-country reporting) are provided in these notes to the annual financial statements. The other disclosures required pursuant to Section 26a (1) KWG, and disclosures pursuant to Section 1a (1) KWG in conjunction with Article 435 et seq. CRR (Regulation (EU) 575/2013 of the European Parliament and of the Council of 26 June 2013 on prudential requirements for credit institutions and investment firms and amending Regulation (EU) 646/2012) are contained in a separate disclosure report, which is updated annually and published on the L-Bank website shortly thereafter.

ACCOUNTING AND VALUATION METHODS

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

Financial assets and liabilities

Cash reserves and receivables from banks and clients are always stated at their nominal value, whereas liabilities are stated at repayment value. Differences (premiums and discounts) with respect to receivables and liabilities are stated under accrued or deferred items and written back pro rata temporis. 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.

Negative interest from financial investments is reported under interest income, while negative interest from borrowing is reported under interest expenses.

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 are 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.

When assessing risks in the lending business, a distinction is made between the recognition of risk provisions for non-performing loans and non-impaired loans. Individual value adjustments, specific provisions and generalised value adjustments are made for non-performing loans. Uncollectable receivables are written off. Portfolio or general loan-loss provisions and a provision for general banking risks in accordance with Section 340f HGB are set up for non-impaired risk positions. The generalised value adjustments are measured on the basis of historical losses for homogeneous portfolios. Portfolio and general loan-loss provisions are based on historical or expected losses. Current risk factors are also taken into account. All value adjustments are offset against assets or stated under provisions.

Securities in the liquidity reserve are stated at the lower of acquisition cost or stock exchange/market price at the balance sheet date, in accordance with the strict 'lower of cost or market' principle. Where possible, stock-market prices 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 amortised cost, whereby differences between the book value and the repayment amount are treated as income in proportion to their term. Securities in the financial investment portfolio are written down in the event of a loss of value that is likely to be permanent. If the reasons for a permanent loss of value no longer exist, the write-down is reversed accordingly. A generalised provision has been set up for latent risks, calculated on the basis of anticipated losses.

Holdings and shares in affiliated companies are stated at acquisition cost or, in the event of a likely permanent loss of value, at the lower fair value as at the balance sheet date, analogous to the rules governing fixed assets. If the reasons for a permanent loss of value no longer exist, the write-down is reversed accordingly.

Tangible and intangible assets

Intangible assets and tangible assets are valued at acquisition or production cost, less scheduled depreciation and amortisation. Where necessary, i.e. where it is anticipated that a loss 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. Individually capitalised assets are depreciated on a straight-line basis over their assumed useful lives. The useful lives are generally derived from the tax depreciation tables.

Provisions

Provisions for pensions and similar obligations are determined according to actuarial principles using Professor Dr Heubeck's RT 2018 G mortality tables. The projected unit credit (PUC) method is used for valuation purposes. Future wage and salary adjustments are included in the calculation, based on a projected average increase of 2% p.a.; future pension adjustments are also included, based on increases of 1.6% or 2%. Pursuant to the specifications of Section 253 (2) sentence 1 HGB, provisions are discounted at the average market interest rate over the last ten fiscal years, assuming a residual term of 15 years. The rate of interest applied is 2.71% (2018: 3.21%). The difference between the recognition of provisions based on the average market interest rate over the last ten fiscal years and their recognition based on the equivalent average market interest rate over the last seven fiscal years came to EUR 44 million as at 31 December 2019 (2018: EUR 42 million). This amount is barred from distribution.

The remaining provisions are stated at the repayment amount deemed necessary by sound business judgement, taking account of all risks from doubtful liabilities that can be identified, as well as anticipated losses from pending transactions. Provisions with a residual 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 Section 249 (1) sentence 3, (2) HGB (old version) are 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 apply.

Interest accruing on provisions (including provisions for pensions and similar obligations) totalling EUR 35 million (2018: EUR 30 million) is stated under net interest income.

Development funds

To fulfil L-Bank's statutory public-service mandate, the Bank provides funds from earned income in the form of a development fund provision.

Out of the development fund for 2019, totalling EUR 87 million, EUR 78 million was utilised. The remaining balance was carried forward to the following year, increasing the development fund available for the 2020 fiscal year to EUR 89 million in total. On 31 December 2019, L-Bank made a provision of EUR 80 million to cover its obligation to pay out development contributions in fiscal year 2021.

Allocations to this provision in the current year are recognised in the statement of income as follows, taking account of the type of development activity envisaged (interest rate reductions, subsidised sureties or grants):

	EURk
Interest expenses	58,000
Commission expenses	3,500
Other operating expenses	18,500
Total	**80,000**

Currency translation

Currency translation has been carried out according to the provisions of Section 256a in conjunction with Section 340h HGB, as well as IDW RS BFA Opinion 4. Assets and liabilities denominated in foreign currencies, as well as all pending foreign-currency cash transactions, are translated at the mean spot rate on 30 December 2019. In the case of forward currency contracts, the forward rate is separated out into cash and interest portions.

For currency translation 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 translation within the meaning of Section 340h HGB are included in the statement of income. Any valuation surplus is reported in a balancing item under 'Other assets'.

Loss-free valuation of the non-trading portfolio (bank book)

Reviews of the non-trading portfolio (bank book) within the meaning of IDW RS BFA Opinion 3, with the aim of ensuring loss-free valuation, are based on a net-present-value approach. Calculations are 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 valuation of transactions continued to show that 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 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 Section 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', otherwise known as the net hedge presentation 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 consideration in the financial statements.

Hedged transactions in macro hedges within the meaning of Section 254 HGB are presented in the table below. Where applicable, the stated book values have been translated into EUR at the mean spot rate on 30 December 2019.

Underlying transaction in macro hedge	Book value in EURk	of which interest rate risk	of which currency risk	of which price risk
Assets	433,680	–	–	433,680
Liabilities	1,532,387	1,357,250	175,137	–
Total	**1,966,067**	**1,357,250**	**175,137**	**433,680**

NOTES TO THE ANNUAL FINANCIAL STATEMENTS OF L-BANK AS AT 31 DECEMBER 2019

BREAKDOWN OF SELECTED BALANCE SHEET ITEMS BY TIME TO MATURITY OR CALL	31.12.2019 EURk	31.12.2018 EURk
RECEIVABLES FROM BANKS		
due on demand	6,049	4,345
up to three months	986,142	1,002,999
more than three months and up to one year	6,019,016	4,309,307
more than one year and up to five years	7,281,323	7,239,599
more than five years	10,918,609	10,836,871
RECEIVABLES FROM CLIENTS		
up to three months		465,915
more than three months and up to one year	1,741,311	1,226,937
more than one year and up to five years	3,528,142	3,517,413
more than five years	17,011,507	17,435,054
BONDS, DEBENTURES AND OTHER FIXED-INCOME SECURITIES		
maturing in the following year	2,987,369	761,993
LIABILITIES TO BANKS		
due on demand	11,480	8,567
up to three months	1,404,132	1,178,040
more than three months and up to one year	1,923,998	1,654,247
more than one year and up to five years	9,040,216	8,945,795
more than five years	13,608,121	14,076,267
LIABILITIES TO CLIENTS		
due on demand	99,657	128,776
up to three months	4,430,351	2,107,530
more than three months and up to one year	140,806	58,257
more than one year and up to five years	508,377	600,956
more than five years	5,577,574	6,117,598
SECURITISED LIABILITIES		
maturing in the following year	17,748,145	13,375,588

EXPLANATIONS OF INDIVIDUAL BALANCE SHEET ITEMS	31.12.2019 EURk	31.12.2018 EURk
RECEIVABLES FROM BANKS		
This item comprises:		
– receivables from companies in which an equity interest is held	144,987	100,000
RECEIVABLES FROM CLIENTS		
This item comprises:		
– receivables from affiliated companies	48,544	56,334
– receivables from companies in which an equity interest is held	62,378	92,366
– subordinated claims	0	36
BONDS, DEBENTURES AND OTHER FIXED-INCOME SECURITIES		
This item comprises:		
– receivables from companies in which an equity interest is held	1,715,228	1,715,267
The securities in this item eligible for listing break down as follows:		
– listed	22,491,292	21,631,656
– unlisted	1,914,133	405,846
Securities with a book value (excluding prorated interest accrued) of EUR 22,568,242,000 are assigned to investment assets. Of these, securities with a book value of EUR 801,686,000 have a market value of EUR 786,719,000. No depreciation or amortisation has been applied to these items, as short-term market fluctuations are not taken into account due to the intention to hold these assets on a long-term basis.		
FIDUCIARY ASSETS		
This item breaks down as follows:		
– receivables from banks	22,815	26,889
– receivables from clients	806	1,443
– other assets	1	1
TANGIBLE ASSETS		
This item comprises:		
– plots and buildings used for the Bank's own activities	69,602	70,137
– plant and office equipment	6,024	5,702

NOTES TO THE ANNUAL FINANCIAL STATEMENTS OF L-BANK AS AT 31 DECEMBER 2019

EXPLANATIONS OF INDIVIDUAL BALANCE SHEET ITEMS	31.12.2019 EURk	31.12.2018 EURk
ACCRUED ITEMS – ASSETS		
– Difference between disbursement amount or acquisition cost and lower nominal value of receivables	591,079	667,100
– Difference between issue price and higher repayable amount of liabilities	37,338	35,377
FIDUCIARY LIABILITIES		
Fiduciary liabilities break down into		
– liabilities to banks	411	694
– liabilities to clients	23,210	27,638
– other liabilities	1	1
DEFERRED ITEMS – LIABILITIES		
– Difference between disbursement amount or acquisition cost and higher nominal value of receivables	705	996
– Difference between issue price and lower repayable amount of liabilities	48,953	29,627
SUBORDINATED LIABILITIES AND PROFIT-SHARING RIGHTS		
– Interest expenses on subordinated liabilities	2,848	3,953
– Interest expenses on profit-sharing rights	12,995	12,995

The following subordinated liabilities exceed 10% of the total value of all subordinated liabilities:

CURRENCY	Amount in EURk	Interest rate in %	Maturity date
EUR	40,000	2.265	14.11.2023
EUR	20,000	2.265	14.11.2023

EXPLANATIONS OF INDIVIDUAL BALANCE SHEET ITEMS

Profit-sharing rights consist of profit participation certificates and break down as follows:

Amount in EURk	Interest rate in %	Maturity date	Number
10,000	5.000	01.07.2020	2
25,000	5.125	01.07.2020	1
25,000	5.140	01.07.2020	2
5,000	5.160	01.07.2020	2
25,000	5.170	01.07.2020	1
10,000	5.170	01.07.2020	1
3,000	5.170	01.07.2020	1
50,000	5.375	01.07.2025	1
10,000	5.375	01.07.2025	4
5,000	5.375	01.07.2025	3

Under the terms and conditions of the profit participation certificates, the servicing of distribution and repayment claims is linked to the result of the Bank's ordinary business activities.

Subordinated liabilities and profit-sharing rights are intended for use as supplementary capital and comply with CRR eligibility requirements. The important factor here is the subordinated nature of the Bank's liability in these cases 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 OF L-BANK AS AT 31 DECEMBER 2019

INDIVIDUAL AMOUNTS THAT ARE MATERIAL IN ASSESSING THE ANNUAL FINANCIAL STATEMENTS	31.12.2019 EURk	31.12.2018 EURk
OTHER ASSETS		
– Balancing item from currency translation	218,759	141,199
– Receivables from swaps	42,477	50,772
– Works of art	11,617	11,791
PREPAYMENTS AND ACCRUED ITEMS		
– Single payments made in advance for swaps	137,934	146,973
OTHER LIABILITIES		
– Single (bullet) repayments on swaps	12,133	11,620
DEFERRED ITEMS		
– Single payments received in advance for swaps	1,544,738	1,669,831
PROVISIONS		
under other provisions:		
– Provisions for development funds	169,171	166,595
– Provisions for development contributions already made	51,977	63,945
INTEREST INCOME		
– Negative interest from financial investments	35,853	26,792
INTEREST EXPENSES		
– Negative interest from borrowing	27,981	18,878
COMMISSION INCOME		
– Income from other services	42,663	38,535
Other services relate mainly to services on behalf of the State of Baden-Württemberg.		
GENERAL ADMINISTRATIVE EXPENSES		
Other administrative expenses include auditor's fees (excluding sales tax):		
– for year-end auditing services	389	394
– for other auditing services	36	92
Other auditing services include the limited-assurance engagement related to the non-financial report, and investigations associated with the reporting of the bank levy.		

INDIVIDUAL AMOUNTS THAT ARE MATERIAL IN ASSESSING THE ANNUAL FINANCIAL STATEMENTS	31.12.2019 EURk	31.12.2018 EURk
OTHER OPERATING EXPENSES		
– Addition to the provision for development funds	18,500	5,000
TOTAL VALUE OF ASSETS AND LIABILITIES DENOMINATED IN FOREIGN CURRENCIES		
– Assets	5,003,276	4,480,416
– Liabilities	27,425,183	19,872,996
The exchange-rate risk from foreign-exchange balance-sheet items is essentially covered by off-balance-sheet hedging transactions. Currency translation produced: other operating income in the amount of	79	10

CONTINGENT LIABILITIES AND OTHER COMMITMENTS

The assessment of utilisation risk is based on the Bank's risk management approach. The overwhelming proportion of contingent liabilities and other commitments comprise credit risks from borrowers with good to very good credit ratings. Acute and latent credit risks are accounted for in the balance sheet by making suitable provisions.

PROVISION OF COLLATERAL

For refinancing purposes, securities in the amount of EUR 3,367 million (2018: EUR 3,172 million) were deposited with Deutsche Bundesbank. Securities in the amount of EUR 784 million (2018: EUR 304 million) were deposited in respect of membership of EUREX (the electronic derivatives exchange).

As collateral for OTC transactions, the Bank posted cash surety bonds totalling EUR 5,120 million (2018: EUR 3,432 million), reported under receivables from banks or clients.

OTHER FINANCIAL COMMITMENTS

By acquiring a shareholding in Landesbank Baden-Württemberg (LBBW) with effect from 1 January 2005, L-Bank became a guarantor of LBBW. Even after withdrawing from its role as LBBW guarantor with effect from midnight on 28 December 2015, L-Bank remains liable to third parties for all LBBW liabilities incurred prior to 18 July 2001. However, in the event of claims against L-Bank, the Bank is entitled to hold any guarantors with inter partes liability jointly and severally liable in full.

As at the balance-sheet date, there are no transactions within the meaning of Section 285 (3) and (3a) HGB that are significant for the assessment of the Bank's financial position.

NOTES TO THE ANNUAL FINANCIAL STATEMENTS OF L-BANK AS AT 31 DECEMBER 2019

DERIVATIVE TRANSACTIONS

As at the balance-sheet date, L-Bank had concluded the derivative transactions (forward transactions within the meaning of Section 36 RechKredV) listed below. They are used as hedges against interest rate and currency risks. For the 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 arrangements 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 (hedged items) are not included in the tables.

The derivative transactions break down as follows:

DERIVATIVE TRANSACTIONS – SUMMARY OF AMOUNTS

in EUR millions	Nominal values 31.12.2019	Nominal values 31.12.2018	Market values positive 31.12.2019	Market values negative 31.12.2019	Market values positive 31.12.2018	Market values negative 31.12.2018
INTEREST RATE RISKS						
Interest rate swaps	71,512	72,138	2,280	–6,505	2,088	–4,676
Interest rate risks – total	**71,512**	**72,138**	**2,280**	**–6,505**	**2,088**	**–4,676**
CURRENCY RISKS						
Forward currency contracts/ swaps	14,170	10,087	124	–53	146	–46
Currency swaps/cross-currency interest rate swaps	16,779	12,991	467	–1,108	251	–1,024
Currency risks – total	**30,949**	**23,078**	**591**	**–1,161**	**397**	**–1,070**

On balance, no significant 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 bonds or debentures issued in foreign currencies. Market values of interest rate/currency swaps totalling EUR 219 million are due to changes in spot exchange rates. A balancing item from currency translation was set up in this amount on the assets side and stated under 'Other assets'. If individual swap contracts include bullet payments, these are reported under 'Other assets' or 'Other liabilities'. Any advance payments are included in 'Accrued items'.

Interest rate swaps in the non-trading portfolio (bank book) are used primarily to control total interest rate exposure and show a net negative market value of EUR 4,225 million as at year-end 2019. These interest rate swaps are not valued in the balance sheet, because both assets and liabilities contain interest-related hidden reserves that are significantly higher than the negative market values of the interest rate swaps.

DERIVATIVE TRANSACTIONS – BY COUNTERPARTY

in EUR millions	Nominal values 31.12.2019	Nominal values 31.12.2018	Market values positive 31.12.2019	Market values negative 31.12.2019	Market values positive 31.12.2018	Market values negative 31.12.2018
Banks in the OECD	91,753	83,626	2,605	–6,439	2,138	–4,833
Other counterparties (including stock-exchange transactions)	10,708	11,590	266	–1,227	347	–913
Total	**102,461**	**95,216**	**2,871**	**–7,666**	**2,485**	**–5,746**

DERIVATIVE TRANSACTIONS – BY TERM

Nominal values in EUR millions	Interest rate risks 31.12.2019	Interest rate risks 31.12.2018	Currency risks 31.12.2019	Currency risks 31.12.2018
RESIDUAL MATURITIES				
– up to three months	2,806	1,727	12,488	8,008
– more than three months	4,756	3,810	2,843	3,409
and up to one year	24,396	23,509	11,829	7,611
– more than one year	39,554	43,092	3,789	4,050
and up to five years				
– more than five years				
Total	**71,512**	**72,138**	**30,949**	**23,078**

There are no trading transactions.

VALUING DERIVATIVE FINANCIAL INSTRUMENTS

The market valuation of derivatives is based on market data as at 31 December 2019, including yield curves, exchange rates 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
Interest rate structures	Interest rate-structure models (BGM model, Bachelier model, Hull-White model, modified Hull-White model for multiple currencies)

NOTES TO THE ANNUAL FINANCIAL STATEMENTS OF L-BANK AS AT 31 DECEMBER 2019

INFORMATION ON TAX LIABILITIES

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

COUNTRY-BY-COUNTRY REPORTING PURSUANT TO SECTION 26A (1) SENTENCE 2 KWG

All disclosures in the annual financial statements within the meaning of Section 26a (1) sentence 2 KWG apply exclusively to the Federal Republic of Germany.

L-Bank's turnover for the fiscal year from 1 January to 31 December 2019 breaks down as follows:

in EUR millions	2019	2018
Net interest income (including current income)	244	260
Net commission income	41	38
Other operating income	9	25
Turnover	**294**	**323**

During 2019, L-Bank employed the equivalent of 1,128 full-time salaried employees on average (2018: 1,089).

The Bank's pre-tax profit for fiscal year 2019 was EUR 50 million (2018: EUR 51 million).

After rounding, taxes on income during fiscal year 2019 totalled EUR 0 million (2018: EUR 1 million). These related exclusively to non-reimbursable taxes on capital, plus the solidarity surcharge.

The Bank did not receive any public funding (state aid) in the year under review or in the previous year.

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

No.	Name	Registered office	Direct shareholding in %	Equity* in EURk	Result* in EURk
1	Austria Beteiligungsgesellschaft mbH	Stuttgart	33.34	36,287	163
2	Baden-Württemberg International – Gesellschaft für internationale wirtschaftliche und wissenschaftliche Zusammenarbeit mbH	Stuttgart	24.00	3,928	–4,400
3	BrandMaker GmbH	Karlsruhe	33.10	3,195	–1,695
4	BWK GmbH Unternehmensbeteiligungsgesellschaft	Stuttgart	10.00	241,927	5,084
5	DBAG Expansion Capital Fund GmbH & Co. KG	Frankfurt	21.77	51,408	1,815
6	European Investment Fund	Luxembourg	0.18	1,991,030	127,561
7	Landesbeteiligungen Baden-Württemberg GmbH	Stuttgart	12.14	807,911	12,346
8	LEA Mittelstandspartner GmbH & Co. KG	Karlsruhe	25.00	28,872	–3,533
9	LEA Venturepartner GmbH & Co. KG	Karlsruhe	49.00	2,919	–400
10	MBG Mittelständische Beteiligungsgesellschaft Baden-Württemberg GmbH	Stuttgart	26.80	76,993	4,504
11	Micropelt Abwicklungsgesellschaft GmbH	Freiburg	20.10	**	**
12	OnSee Holding GmbH	Bruchsal	47.71	653	677
13	Selbca Holding GmbH	Berlin	36.55	6,301	–393
14	StEP Stuttgarter EngineeringPark GmbH	Stuttgart	100.00	16,176	6,953
15	Strohheker Holding GmbH	Pforzheim	49.50	49	37
16	Technologiepark Karlsruhe GmbH	Karlsruhe	96.00	23,163	1,848
17	Technologiepark Mannheim GmbH	Mannheim	100.00	1,532	–268
18	Technologieparks Tübingen-Reutlingen GmbH	Tübingen	100.00	11,124	977
19	Wessel-Werk Beteiligungsverwaltung GmbH	Karlsruhe	35.00	**	**

* As at the last fiscal year for which annual financial statements are available in each case.
** No annual financial statements were prepared due to insolvency.

The Bank opted to apply Section 286 (3) sentence 1 HGB.

NOTES TO THE ANNUAL FINANCIAL STATEMENTS OF L-BANK AS AT 31 DECEMBER 2019

STATEMENT OF CHANGES IN FIXED ASSETS

Fixed assets Balance sheet items	Acquisition costs 01.01.2019 EURk	Additions EURk	Retire-ments EURk	Transfers EURk	Write-ups, cumulative EURk	Depreciation/ amortisation, cumulative EURk	Book value 31.12.2019 EURk	Annual depreciation/ amortisation for 2019 EURk
Bonds, debentures and other fixed-interest securities	22,724,958	Net change pursuant to Section 34 (3) sentence 2 RechKredV: –281,767					22,568,242	–
Shareholdings	340,190						229,562	–6,807
Holdings in affiliated companies	23,332						8,909	–
Intangible assets	38,717	1,018	–7,350	–	–	–29,435	2,950	–1,010
Tangible assets	223,598	4,275	–34,888	–	–	–117,075	75,910	–4,611
Other assets	13,129	–	–21	–	–	–1,491	11,617	–153

Depreciation/amortisation	01.01.2019	Addition	Write-up	Transfer	Retirement	31.12.2019
Intangible assets	35,776	1,010	–	–	7,351	29,435
Tangible assets	123,259	4,611	–	–	10,795	117,075
Other assets	1,338	153	–	–	–	1,491

REMUNERATION PAID TO MEMBERS OF THE BOARD OF MANAGEMENT AND SUPERVISORY BOARD

Remuneration paid to members of the Board of Management for 2019 in EURk

Name	Membership period	Fixed remuneration	Other non-cash benefits	Payments from third parties in relation to Board of Management activities	Total
Dr. Axel Nawrath Chair	01.01.–31.12.	682	25	8	714
Dr. Ulrich Theileis Vice-Chair	01.01.–31.12.	525	27	25	577
Dr. Iris Reinelt	01.01.–31.12.	425	29	9	464
Johannes Heinloth	01.01.–31.12.	425	25	5	455
Total		**2,057**	**107**	**47**	**2,211**

An occupational pension scheme is in place for members of the Board of Management based on the rules applicable to L-Bank employees.

REMUNERATION PAID TO MEMBERS OF THE BOARD OF MANAGEMENT AND SUPERVISORY BOARD

Remuneration paid to members of the Supervisory Board for 2019 in EURk

Name	Membership period	Membership of Supervisory Board	Membership of committees	Attendance fees	Total
Edith Sitzmann[1)] Chair	01.01.–31.12.	9.0	14.0	2.1	25.1
Dr. Nicole Hoffmeister-Kraut[1) 2)] 1st Vice-Chair	01.01.–31.12.	7.5	5.3	1.1	13.9
Franz Untersteller[1) 3)] 2nd Vice-Chair	01.01.–31.12.	6.7	2.4	0.6	9.7
Dr. Jürgen Bufka	01.01.–31.12.	6.0	–	0.6	6.6
Dr. Maximilian Dietzsch-Doertenbach	01.01.–31.12.	6.0	12.9	2.0	20.9
Martin Gross	01.01.–31.12.	6.0	2.6	0.9	9.5
Manuel Hagel	09.07.–31.12.	2.9	–	0.2	3.0
Roger Kehle	01.01.–31.12.	6.0	–	0.5	6.5
Gabriele Kellermann	01.01.–31.12.	6.0	8.1	1.4	15.5
Andrea Lindlohr	01.01.–31.12.	6.0	–	0.6	6.6
Rainer Reichhold	01.01.–31.12.	6.0	–	0.6	6.6
Prof. Dr. Wolfgang Reinhart	01.01.–31.12.	6.0	–	0.3	6.3
Dr. Florian Stegmann[1)]	01.01.–31.12.	6.0	5.8	0.8	12.5
Thomas Strobl[1)]	01.01.–04.07.	3.8	4.8	0.9	9.5
Harald Unkelbach	01.01.–31.12.	6.0	2.4	0.8	9.2
Joachim Walter	01.01.–31.12.	6.0	–	0.5	6.5
Clemens Meister	01.01.–31.12.	6.0	–	0.8	6.8
Barbara Bender-Wieland	01.01.–31.12.	6.0	–	0.8	6.8
Thomas Dörflinger	01.01.–31.12.	6.0	–	0.6	6.6
Total		**113.9**	**58.3**	**15.6**	**187.8**

[1)] Subject to a duty of surrender to the State of Baden-Württemberg.
[2)] Appointed as first Vice-Chair with effect from 09.07.2019.
[3)] Appointed as second Vice-Chair with effect from 09.07.2019.

NOTES TO THE ANNUAL FINANCIAL STATEMENTS OF L-BANK AS AT 31 DECEMBER 2019

REMUNERATION PAID TO MEMBERS OF THE BOARD OF MANAGEMENT AND SUPERVISORY BOARD

	31.12.2019 EURk	31.12.2018 EURk
– Payments to former members of the Board of Management or their surviving dependants	1,550	1,681
– Advisory Board remuneration (including travel costs)	–	66
– Pension provisions for former members of the Board of Management and their surviving dependants	25,300	26,537

LOANS TO ADMINISTRATIVE BODIES (INCLUDING CONTINGENT LIABILITIES)

	31.12.2019 EURk	31.12.2018 EURk
Supervisory Board	8	9

All loans bear interest at market rates.

NUMBER OF EMPLOYEES (ANNUAL AVERAGE)

	Male	Female	Total
Employees*	538	689	1,227
of whom: full-time employees	506	378	884
of whom: part-time employees	32	311	343

* Headcount; excluding vocational trainees and interns.

Directorships held by Board of Management members and employees of L-Bank sitting on statutory supervisory bodies of large corporations pursuant to Section 340a (4), Art. 1 HGB

DR. ULRICH THEILEIS, VICE-CHAIR OF THE BOARD OF MANAGEMENT	
Hypo Vorarlberg Bank AG, Bregenz, Austria	Member of the Supervisory Board
Sächsische Aufbaubank – Förderbank –, Dresden	Member of the Administrative Council

DR. IRIS REINELT, MEMBER OF THE BOARD OF MANAGEMENT	
Investitionsbank Berlin, Berlin	Member of the Supervisory Board

NOTES TO THE ANNUAL FINANCIAL STATEMENTS OF L-BANK AS AT 31 DECEMBER 2019

Boards of L-Bank

BOARD OF MANAGEMENT

Dr. Axel Nawrath
Chair
until 31.12.2019

Edith Weymayr
Chair
since 01.01.2020

Dr. Ulrich Theileis
Vice-Chair

Dr. Iris Reinelt

Johannes Heinloth

SUPERVISORY BOARD MEMBERS

Regular members

Edith Sitzmann MSP*
Minister of Finance for the State of Baden-Württemberg
Chair

Dr. Nicole Hoffmeister-Kraut MSP*
Minister of Economic Affairs, Labour and Housing, State of Baden-Württemberg
1st Vice Chair

Franz Untersteller MSP*
Minister of the Environment, Climate and Energy, State of Baden-Württemberg
2nd Vice-Chair

Dr. Jürgen Bufka
Managing Director, Amber Infrastructure GmbH

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

Martin Gross
Regional Manager, ver.di Baden-Württemberg

Manuel Hagel MSP*
Member of the CDU parliamentary group, Baden-Württemberg State Parliament
since 09.07.2019

Roger Kehle
President, Baden-Württemberg Association of Municipalities

Gabriele Kellermann
Member of the Board of Managing Directors, BBBank eG

Andrea Lindlohr MSP*
Vice-Chair, Alliance 90/The Greens parliamentary group, Baden-Württemberg State Parliament

Rainer Reichhold
President, Baden-Württembergischer Handwerkstag e. V.

Prof. Dr. Wolfgang Reinhart MSP*
Chair, CDU parliamentary group, Baden-Württemberg State Parliament

Dr. Florian Stegmann
Secretary of State, Baden-Württemberg Ministry of State

Thomas Strobl
Deputy State Premier and Minister of the Interior, Digitisation and Migration of the State of Baden-Württemberg
until 04.07.2019

Harald Unkelbach
President, Heilbronn-Franken Chamber of Industry and Commerce

Joachim Walter
President, Baden-Württemberg Association of District Councils

Consulting members

Clemens Meister
Chair, Central Staff Council of L-Bank, Karlsruhe

Barbara Bender-Wieland
Chair, Staff Council of L-Bank, Karlsruhe

Thomas Dörflinger
Chair, Staff Council of L-Bank, Stuttgart

*MSP = Member of the State Parliament of Baden-Württemberg.

Events after the balance sheet date

No incidents or events of particular significance occurred after the fiscal year-end on 31 December 2019.

Proposal by the Board of Management for the distribution of net profit

The Board of Management hereby proposes to the Supervisory Board that out of the net profit for fiscal year 2019, totalling EUR 50,959,453.24, an amount of EUR 50,000,000.00 should be allocated to other retained earnings and the remaining amount of EUR 959,453.24 carried forward to the current fiscal year.

Karlsruhe, 3 March 2020

L-Bank

Edith Weymayr Dr. Ulrich Theileis Dr. Iris Reinelt Johannes Heinloth

DECLARATION OF THE BOARD OF MANAGEMENT REGARDING THE FINANCIAL STATEMENTS OF L-BANK AS AT 31 DECEMBER 2019

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 financial position, cash flows and financial performance, and that the Management Report includes a true and fair review of the development and performance of the business and position of the Bank, together with a description of the principal opportunities and risks associated with the Bank's expected development.

Karlsruhe, 3 March 2020

Edith Weymayr Dr. Ulrich Theileis Dr. Iris Reinelt Johannes Heinloth

INDEPENDENT AUDITOR'S REPORT

for Landeskreditbank Baden-Württemberg – Förderbank –, Karlsruhe

REPORT ON THE AUDIT OF THE ANNUAL FINANCIAL STATEMENTS AND THE MANAGEMENT REPORT

Audit opinions

We have audited the annual financial statements of Landeskreditbank Baden-Württemberg – Förderbank –, Karlsruhe comprising the balance sheet as at 31 December 2019, income statement, cash flow statement and statement of changes in equity for the fiscal year from 1 January to 31 December 2019, as well as the notes to the accounts, including the descriptions of the accounting and valuation methods applied. We have also audited the management report of Landeskreditbank Baden-Württemberg – Förderbank – for the fiscal year from 1 January to 31 December 2019. In accordance with German statutory provisions, we have not audited the contents of the separate non-financial report pursuant to Section 289b (3) of the German Commercial Code (Handelsgesetzbuch (HGB)).

In our opinion, based on the findings of the audit:

- the accompanying annual financial statements comply, in all material respects, with German commercial law and, in accordance with German accepted accounting principles, give a true and fair view of the net assets and financial position of the institution as at 31 December 2019, and of the results of its operations for the fiscal year from 1 January to 31 December 2019, and

- in all material respects, the accompanying management report conveys a true and fair view of the institution's position, is consistent with the annual financial statements, complies with German statutory provisions and suitably presents the opportunities and risks of future development. Our audit opinion on the management report does not cover the contents of the aforementioned separate non-financial report.

In accordance with Section 322 (3) sentence 1 HGB, we declare that our audit has not led to any reservations regarding the legal compliance of the annual financial statements and the management report.

Basis for the audit opinions

We conducted our audit of the annual financial statements and management report in accordance with Section 317 HGB and EU Audit Regulation 537/2014 (hereinafter 'EU Audit Regulation') and in compliance with German generally accepted standards for the audit of financial statements promulgated by the Institute of Public Auditors in Germany (Institut der Wirtschaftsprüfer (IDW)). Our responsibilities under those provisions and standards are further described in the 'Auditor's responsibilities for the audit of the annual financial statements and management report' section of our auditor's report. In accordance with European law as well as German commercial law and professional requirements, we are independent of the institution and have fulfilled our other German ethical and professional responsibilities in accordance with these requirements. In addition, in accordance with Article 10 (2) (f) of the EU Audit Regulation, we declare that we have not provided non-audit services prohibited under Article 5 (1) of the EU Audit Regulation. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinions on the annual financial statements and the management report.

Key audit matters in the audit of the annual financial statements

Key audit matters are those matters that, in our professional judgement, were of most significance in our audit of the annual financial statements for the fiscal year from 1 January to 31 December 2019. These matters were addressed in the context of our audit of the annual financial statements as a whole and in the preparation of our opinion thereon; we do not express a separate audit opinion on these matters.

In our view, the following was the matter of most significance in our audit:

1. Loan-loss provisions in client lending business

Our presentation of this key audit matter has been structured as follows:

1. Matter and issue

2. Auditing procedure and findings

3. Reference to further information

We present the key audit matter below:

1. Loan-loss provisions in client lending business

1. Landeskreditbank Baden-Württemberg – Förderbank – is the development bank of the German federal state of Baden-Württemberg. Its business activities are governed by its statutory remit, namely to support the state government of Baden-Württemberg in the fulfilment of its public duties, especially in terms of structural, economic and social policy, by implementing development initiatives in accordance with European Union (EU) rules on state aid. It provides this support mainly by issuing low-interest loans and grants. As at 31 December 2019, loan receivables in the amount of EUR 22,862 million (29.5% of total assets) were reported under the balance sheet item 'Receivables from clients' in the institution's annual financial statements.

The measurement of loan-loss provisions in client lending business is determined in particular by the legal representatives' assessment of future credit losses based on the structure and quality of the loan portfolio, as well as macroeconomic factors. Specific valuation adjustments for receivables from clients are equal in amount to the difference between the outstanding loan amount and its lower fair value at the reporting date. Portfolio and general valuation adjustments are also made. Valuation adjustments in client lending business are potentially of major significance for the institution's financial performance and also involve the legal representatives' discretionary use of judgement. In light of these facts, this matter was especially important in the context of our audit.

2. In the course of our audit, we first assessed the appropriateness of the design of the controls in the institution's relevant internal control system and tested the effective functioning of the controls, taking into account the organisational procedures, IT systems and relevant valuation models. We also assessed the valuation of receivables from clients, including the appropriateness of estimates, by examining individual loan exposures on a random basis. In doing so, we assessed the documents available to the institution regarding financial circumstances and the recoverability of associated collateral, among other things. In the case of real-estate collateral for which the institution presented us with valuation reports, we obtained an understanding of the raw data underlying the reports, the valuation inputs used and assumptions made, critically appraised these and assessed whether they lie within a reasonable range. In addition, in order to evaluate the specific, portfolio and general valuation adjustments, we assessed the calculation methods as well as the underlying assumptions and parameters. Based on the audit procedures we performed, we were able to satisfy ourselves overall of the appropriateness of the assumptions made by the legal representatives in testing the loan portfolio for impairment and of the appropriateness and effectiveness of the processes implemented by the institution.

3. The institution's disclosures on loan-loss provisions in client lending business are contained in the notes to the annual financial statements, in the section entitled 'Financial assets and liabilities' under 'Accounting and valuation methods'.

Other information

The legal representatives are responsible for the other information provided. The other information includes the separate non-financial report pursuant to Section 289b (3) HGB.

The other information additionally includes the remaining parts of the annual report – excluding supplementary cross-references to external information – obtained by us prior to the date of this auditor's report, with the exception of the audited annual financial statements, the audited management report and our auditor's report. We anticipate that the Supervisory Board report will be made available to us after the date of this auditor's report.

Our audit opinions on the annual financial statements and management report do not cover the other information, and consequently we do not express an audit opinion or any other form of assurance conclusion thereon.

In connection with our audit, our responsibility is to read the other information and, in so doing, to consider whether the other information:

- is materially inconsistent with the annual financial statements, the management report or the findings we obtained in the course of the audit, or
- otherwise appears to be materially misstated.

Responsibilities of the legal representatives and Supervisory Board for the annual financial statements and management report

The legal representatives are responsible for preparing annual financial statements that comply, in all material respects, with German commercial law, and for ensuring that the annual financial statements give a true and fair view of the institution's net assets, financial position and financial performance in accordance with German accepted accounting principles. The legal representatives are also responsible for such internal controls as they, in accordance with German accepted accounting principles, determine are necessary to enable the preparation of annual financial statements that are free from material misstatement, whether due to fraud or error.

In preparing the annual financial statements, the legal representatives are responsible for assessing the institution's ability to continue as a going concern and disclosing, as applicable, matters related to the institution's viability as a going concern. In addition, they are responsible for financial reporting on the basis of the going-concern accounting principle, unless there is constructive or legal evidence to contradict this principle.

Furthermore, the legal representatives are responsible for preparing a management report that, as a whole, appropriately reflects the position of the institution and is in all material respects consistent with the annual financial statements, complies with German statutory provisions and suitably presents the opportunities and risks of future development. The legal representatives are also responsible for such arrangements and measures (systems) as they consider necessary to enable the preparation of a management report in accordance with the applicable German statutory provisions and to provide sufficient suitable evidence to support the assertions in the management report.

The Supervisory Board is responsible for overseeing the institution's financial reporting process for preparing the annual financial statements and the management report.

Auditor's responsibilities for the audit of the annual financial statements and management report

Our objectives are to obtain reasonable assurance about whether the annual financial statements as a whole are free from material misstatement, whether intentional or unintentional, and whether the management report on the whole appropriately reflects the position of the institution and is consistent, in all material respects, with the annual financial statements and the findings of the audit, complies with German statutory provisions and suitably presents the opportunities and risks of future development, as well as to issue an auditor's report that includes our opinions on the annual financial statements and the management report.

While reasonable assurance is a high level of assurance, it is not a guarantee that an audit conducted in accordance with Section 317 HGB and the EU Audit Regulation, and in compliance with German generally accepted standards for the audit of financial statements promulgated by the Institute of Public Auditors in Germany (IDW), will always reveal a material misstatement. Misstatements can arise from fraud or error and are considered material if, individually or in the aggregate, they could reasonably be expected to influence the economic or commercial decisions of users made on the basis of these annual financial statements and this management report.

We exercise our professional judgement and maintain professional scepticism throughout the audit. We also:

- identify and assess the risks of material misstatement in the annual financial statements and the management report, whether due to fraud or error; plan and perform audit procedures in response to those risks; and obtain audit evidence that is sufficient and appropriate to provide a basis for our audit opinions. The risk of not detecting a material misstatement resulting from fraud is higher than for one resulting from error, as fraud may involve collusion, falsification, intentional omission, misrepresentation or the overriding of internal controls.

- obtain an understanding of the internal control system relevant to the audit of the annual financial statements and of the arrangements and measures relevant to the audit of the management report, in order to design audit procedures that are appropriate in the circumstances, albeit not for the purpose of expressing an audit opinion on the effectiveness of these systems at the institution.

- evaluate the appropriateness of the accounting and financial reporting methods used by the institution's legal representatives, as well as the reasonableness of estimates and related disclosures made by the legal representatives.

- draw conclusions on the appropriateness of the legal representatives' use of the going-concern principle of accounting and, based on the audit evidence obtained, on whether a material uncertainty exists in connection with events or circumstances that could cast significant doubt on the institution's ability to continue as a going concern. If we conclude that a material uncertainty exists, we are required to draw attention in the auditor's report to the related disclosures in the annual financial statements and in the management report or, if such disclosures are inadequate, to modify our audit opinion. Our conclusions are based on the audit evidence obtained up to the date of our auditor's report. However, future events or conditions may cause the institution to be unable to continue as a going concern.

- evaluate the overall presentation, structure and content of the annual financial statements, including the disclosures, and whether the annual financial statements present the underlying business transactions and events in such a way that the annual financial statements give a true and fair view of the net assets, financial position and financial performance of the institution in accordance with German accepted accounting principles.

- evaluate the consistency of the management report with the annual financial statements, its conformity with the law and the extent to which it accurately reflects the institution's position.

- perform audit procedures on the forward-looking statements presented by the legal representatives in the management report. On the basis of sufficient appropriate audit evidence, we evaluate, in particular, the significant assumptions on which the forward-looking statements by the legal representatives are based and assess whether the forward-looking statements were properly derived from those assumptions. We do not express a separate audit opinion on the forward-looking statements or the assumptions underlying them. There is a significant unavoidable risk that future events will differ materially from the forward-looking statements.

We communicate with those charged with governance regarding, among other matters, the planned scope and timing of the audit, as well as significant audit findings, including any deficiencies in the internal control system that we identify during our audit.

We provide those charged with governance with a declaration stating that we have complied with the relevant requirements for professional independence, and discuss with them all relationships and other matters that may reasonably be thought to bear on our independence, as well as the relevant safeguards that have been put in place.

From the matters discussed with those charged with governance, we identify those matters that were of greatest significance in the audit of the annual financial statements for the current reporting period and are therefore the key audit matters. We describe these matters in the auditor's report unless law or regulation precludes public disclosure of such matters.

OTHER LEGAL AND REGULATORY REQUIREMENTS

Further information pursuant to Article 10 of the EU Audit Regulation

We were appointed statutory auditor by the Supervisory Board on 16 April 2019. We were engaged by the Supervisory Board on 17 October 2019. We have been the statutory auditor of Landeskreditbank Baden-Württemberg – Förderbank –, Karlsruhe, for an uninterrupted period of engagement since fiscal year 2015.

We declare that the audit opinions contained in this auditor's report are consistent with the additional report to the audit committee referred to in Article 11 of the EU Audit Regulation (long-form audit report).

INDEPENDENT AUDITOR RESPONSIBLE

The German public auditor responsible for the engagement is Stefan Palm.

Stuttgart, 3 March 2020
PricewaterhouseCoopers GmbH
Wirtschaftsprüfungsgesellschaft

Stefan Palm	Peter Schüz
Public Auditor	Public Auditor

INDEPENDENT AUDITOR'S REPORT ON A LIMITED-ASSURANCE ENGAGEMENT RELATED TO THE BANK'S NON-FINANCIAL REPORTING

for Landeskreditbank Baden-Württemberg – Förderbank –, independent public-law institution, Karlsruhe.

We have performed a limited-assurance engagement on the separate non-financial report pursuant to Section 340a (1a) in conjunction with Section 289b (3) HGB for the period from 1 January to 31 December 2019 (hereinafter the 'non-financial report') published by Landeskreditbank Baden-Württemberg – Förderbank –, independent public-law institution, Karlsruhe (hereinafter the 'institution').

RESPONSIBILITIES OF THE LEGAL REPRESENTATIVES

The institution's legal representatives are responsible for preparing the non-financial report in accordance with Sections 289c to 289e HGB.

This responsibility on the part of the institution's legal representatives includes selecting and applying appropriate methods of non-financial reporting, as well as making assumptions and formulating estimates related to individual non-financial disclosures that are appropriate in the given circumstances. The legal representatives are also responsible for such internal controls as they determine are necessary to enable the preparation of a non-financial report that is free from material misstatement, whether intended or unintended.

AUDIT FIRM INDEPENDENCE AND QUALITY CONTROL

We have complied with German statutory provisions regarding independence and other requirements for professional conduct.

Our audit firm applies national statutory requirements and the German profession's pronouncements, in particular the professional statues for German public auditors and sworn auditors (Berufssatzung für Wirtschaftsprüfer und vereidigte Buchprüfer (BS WP/vBP)) as well as the IDW Quality Assurance Standard 1: Requirements for Quality Assurance in Auditing Practice (IDW Qualitätssicherungsstandard 'Anforderungen an die Qualitätssicherung in der Wirtschaftsprüferpraxis' (IDW QS 1)) and accordingly maintains a comprehensive quality assurance system which includes documented policies and procedures regarding compliance with professional conduct requirements, professional standards and applicable legal and regulatory requirements.

INDEPENDENT AUDITOR'S RESPONSIBILITIES

Our responsibility is to express a limited-assurance conclusion on the disclosures in the non-financial report based on the limited-assurance engagement we have performed.

It is not within the scope of our engagement to assess external documentation sources or expert opinions referred to in the non-financial report.

We conducted our limited-assurance engagement in accordance with the International Standard on Assurance Engagements (ISAE) 3000 (Revised) 'Assurance Engagements other than Audits or Reviews of Historical Financial Information' issued by the IAASB. This Standard requires that we plan and perform the assurance engagement in order to obtain limited assurance about whether any matters have come to our attention that cause us to believe that the institution's non-financial report for the period from 1 January 2019 to 31 December 2019 has not been prepared, in all material respects, in accordance with Sections 289c to 289e HGB.

In a limited-assurance engagement, the assurance procedures performed are less extensive than in a reasonable assurance engagement, and therefore a substantially lower level of assurance is obtained. The selection of assurance procedures depends on the public auditor's professional judgement.

In the course of our audit, we performed the following assurance procedures and other activities, including:

- obtaining an understanding of the structure of the sustainability organisation
- making inquiries of the legal representatives and relevant personnel involved in the preparation of the non-financial report concerning the preparation process, the internal control system relating to this process and disclosures in the non-financial report
- identifying likely risks of material misstatement in the non-financial report
- performing an analytical evaluation of disclosures in the non-financial report
- comparing disclosures with corresponding data in the annual financial statements and management report
- evaluating the presentation of the disclosures

ASSURANCE CONCLUSION

Based on the assurance procedures performed and assurance evidence obtained, nothing has come to our attention that causes us to believe that the institution's non-financial report for the period from 1 January to 31 December 2019 has not been prepared, in all material respects, in accordance with Sections 289c to 289e HGB.

INTENDED USE OF THE ASSURANCE REPORT

We issue this report on the basis of the engagement agreed with the institution. The assurance engagement was performed for the purposes of the institution and the report is solely intended to inform the institution of the results of the assurance engagement.

The report is not intended for use by third parties as a basis for making (asset-related) decisions. Our responsibility is solely towards the institution. We do not assume any responsibility towards third parties.

Frankfurt am Main, 3 March 2020

PricewaterhouseCoopers GmbH
Wirtschaftsprüfungsgesellschaft

Nicolette Behncke
Certified Public Accountant

pp. Urata Biqkaj
Certified Public Accountant

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