

Management report -  
Extract from the ANNUAL REPORT 2020

# Management report

For the period from 1 January to 31 December 2020

## Principles of the EAA

### Operating activities of the EAA

The EAA operates as an asset manager pursuing a clear, public mandate that is enshrined in its charter: it is winding up the risk exposures and non-strategic business units (transferred assets) transferred from the former WestLB AG (now Portigon AG) and its domestic and foreign subsidiaries in a value-preserving and risk-minimising manner. This serves to stabilise the financial market.

It manages its business according to commercial and economic principles, in consideration of its winding-up objectives and the principle of minimising its losses. The EAA is not a credit or financial services institution within the meaning of the German Banking Act, an investment services firm as defined by the German Securities Trading Act or an insurance company pursuant to the German Insurance Supervision Act. In accordance with its charter, it does not conduct any transactions that require approval pursuant to Directive 2006/48/EC of the European Parliament and of the Council of 14 June 2006 or Directive 2004/39/EC of the European Parliament and of the Council of 21 April 2004, the amendment to Directives 85/611/EEC and 93/6/EEC of the Council and Directive 2000/12/EC of the European Parliament and of the Council and for the repeal of Directive 93/22/EEC of the Council, as amended.

The EAA is subject to regulation by the FMSA. The EAA is supervised by BaFin with regard to those provisions of banking law that are applicable to the EAA.

The EAA's work is principally carried out on the basis of section 8a StFG, its charter, the rules of procedure for the Supervisory Board and the Managing Board plus their committees, as well as its risk strategy and winding-up plan.

The winding-up plan describes the intended winding-up activities of the EAA by classifying its assets into sub-portfolios (clusters) and standard strategies, and contains a schedule for the winding up of assets. The standard strategies are oriented on an investor or disposal perspective, and take into consideration the "Self-monetisation", "Managed divestment" and "Hold" categories. The "Self-monetisation" strategy comprises assets that will be repaid in full by year-end 2020, while the "Managed divestment" strategy takes into account long-term assets for which active portfolio measures are possible from the EAA's perspective. The "Hold" strategy concerns positions that will probably be held until planned maturity owing to their specific features, although this does not preclude active portfolio management. The strategy for winding up the portfolio could include selling the assets prior to their maturity, holding them until maturity or restructuring the relevant items. The EAA reviews the winding-up plan at least once a quarter and makes adjustments when necessary, mainly in order to take account

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of changes in circumstances, for example current market developments. Changes or adjustments to the winding-up plan must be approved by the FMSA. The EAA regularly submits wind-up reports to inform the FMSA, its Supervisory Board and the EAA stakeholders about the progress of the winding-up and the implementation of the winding-up plan, and documents the success of the wind-up strategy. The annual wind-up report must be adopted by a resolution of the Supervisory Board before being submitted to the FMSA.

The following stakeholders participate in the EAA's share capital: the State of NRW, with a stake of around 48.2%; the Rheinische Sparkassen- und Giroverband and the Sparkassenverband Westfalen-Lippe, each with around 25.0%; and the Landschaftsverband Rheinland and the Landschaftsverband Westfalen-Lippe, each with around 0.9%.

The governing bodies of the EAA are the Managing Board, the Supervisory Board and the Stakeholders' Meeting.

The Managing Board of the EAA consists of at least two members. They are appointed by the Supervisory Board with the FMSA's approval for a maximum term of five years. Members of the Managing Board may be reappointed. The Managing Board manages the operations of the EAA and represents the EAA in and out of court.

The Supervisory Board consists of twelve members. Eleven members are appointed by the Stakeholders' Meeting. One member is delegated by the Bundesrepublik Deutschland - Finanzagentur GmbH, acting on behalf of the FMS. The members elect a Chairman and a Vice Chairman on the recommendation of the State of NRW. The Supervisory Board advises and consults with the EAA's Managing Board, monitors its activities and carries out additional duties set forth in the charter.

The Stakeholders' Meeting is composed of representatives who hold a stake in the EAA's share capital. It is responsible for adopting the annual financial statements of the EAA, among other things.

**Methods of transfer**

Several methods were used to transfer the risk exposures and non-strategic business units of the former WestLB to the EAA in the years 2009 and 2010 (first fill) as well as in 2012 (refill). The method that was chosen in each case was based on the respective domestic legal, supervisory and tax provisions.

In some cases, a spin-off process was used to transfer assets and liabilities in rem to the EAA, whereas in other cases, different transfer methods (sub-participation, guarantees) were used to create a synthetic transfer of the inherent risks and rewards contained in these portfolios.

When spin-offs, sub-participations, crossings (transfer of exchange-traded derivatives via the exchange) and risk assumption agreements are used to transfer the legal or beneficial ownership of derivatives, the portfolios are reported in the balance sheet based on the portfolio classification as stipulated under commercial law. When guarantees are used, the legal and economic ownership remains with Portigon, while the EAA assumes the economic risks of the portfolio. In this case, Portigon pays a guarantee fee to the EAA for the assumption of

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the risks. The risks assumed by the EAA are taken into account by recognising contingent liabilities or provisions.

**Equity base and liability**

The EAA's share capital amounted to EUR 500,000. The first fill created equity totalling around EUR 3.1 billion.

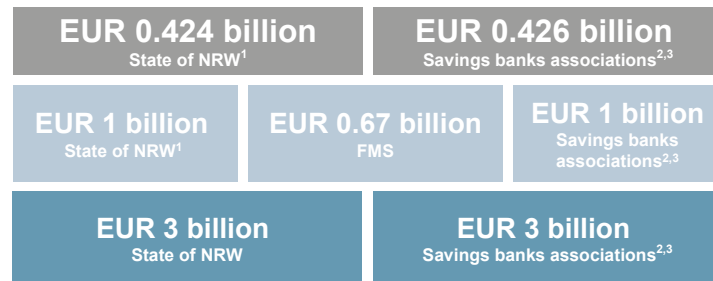
The refill provided the EAA with rights to draw on additional equity that will add EUR 480 million to the capital reserves. If necessary, the liable stakeholders of the EAA and the FMS will provide these funds in specified instalments in the event that the EAA's balance sheet equity should fall below EUR 50 million.

In addition to the EAA's equity base, a factor that is particularly important for the EAA's credit rating is the duty to offset the EAA's losses that the EAA's liable stakeholders and the FMS have assumed. They are individually liable to the EAA to offset all losses in accordance with section 7 of the EAA's charter. To that end, they must provide the EAA with such funds at such times as are necessary in order to ensure that it has sufficient cash and cash equivalents at all times to meet its liabilities as they become due, even after its equity capital has been used up. The EAA is obligated to assert this loss-offset claim against the liable stakeholders and the FMS in the appropriate volume and before any pending insolvency takes effect, in order to ensure it remains solvent at all times.

**Equity capital**

Equity capital drawing limit: EUR 0.480 billion

Levels 1-3 modified in August 2012



Level 4 unchanged since December 2009



**Special arrangement**

for the special-purpose entity Phoenix since 2008



<sup>1</sup> For purposes of simplification, the relatively low stake of the Landschaftsverbände (Landschaftsverband Rheintland and Landschaftsverband Westfalen-Lippe) is included in the figure shown for the State of NRW.

<sup>2</sup> Rheinischer Sparkassen- und Giroverband and Sparkassenverband Westfalen-Lippe, at 50% each.

<sup>3</sup> Default liability assumed by the State of NRW.

<sup>4</sup> The State of NRW and the FMS will reach an agreement on the apportionment of the associated financial burden on the basis of the StFG.

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**Funding**

The EAA was initially funded in the first fill through the nearly complete transfer of all issues and deposits of the former WestLB with guarantor liability. The EAA raised its own funds in the period thereafter. In the future, the EAA will continue to obtain funding primarily by issuing bearer bonds, by short-term borrowing and through repurchase transactions. The EAA's ratings correspond to those of the State of NRW. The risk weighting can therefore be set according to the weighting for the State of NRW. The EBA includes the EAA on the list of public-sector entities to which the borrower weighting of the relevant regional entity (in this case the State of NRW) may be applied pursuant to article 116 (4) CRR. The good ratings received from Moody's, Standard & Poor's and Fitch Ratings, as well as the duty to offset losses on the part of the liable stakeholders and the FMS, form the foundation for the EAA's successful presence on the capital market.

**Accounting**

The EAA prepares its annual financial statements in accordance with HGB. It is exempt from the requirement to prepare consolidated financial statements pursuant to section 8a (1a) sentence 3 StFG. However, the significant shareholdings, particularly EAA CBB, Erste EAA Anstalt öffentlichen Rechts & Co. KG and Dritte EAA Anstalt & Co. KG, are included in the wind-up success and risk planning, risk monitoring and risk reporting.

**Organisation**

Since it began its operating activities, the EAA has repeatedly adjusted its organisational structure to manage changes and challenges in the corporate environment. The gradual takeover of multi-billion portfolios presented it with enormous challenges in developing an adequate organisation and recruiting the required experts. The gradual reduction of the portfolio required capacity and costs to be reduced, without compromising the expertise required to successfully complete the wind-up.

Ongoing optimisation of organisational and cost structures is part of the EAA's responsibility in view of the progressive reduction of the portfolio.

Within the scope of its long-term service strategy, the EAA largely outsourced the provision of portfolio services to third parties, with the objective of maintaining continuity and stability on the one hand and enabling flexibility on the other. Besides the IT and operational services, which EFS provides via IBM as an external service provider, the EAA receives portfolio management services from MSPA, a former subsidiary of the EAA. The EAA will continue to optimise these structures in the future.

Due to the importance of the outsourced activities, the EAA has implemented a central function for an integrated service provider management system. Under this system, the service relationships between the EAA, EFS and MSPA, as well as the other external service providers, are systematically managed and monitored from a legal, substantive, processual and financial perspective.

## Control system

The EAA draws up a winding-up plan regularly (at least once a year) and evaluates as of the end of each quarter whether the plan needs to be adjusted. The winding-up plan details the intended unwinding measures, including a schedule for winding up the EAA portfolio and the resulting implications for EAA's equity capital and financial situation.

One of the EAA's key control metrics is the decline in the notional volume of the portfolio. Aside from volume reduction, other control metrics are also relevant. According to section 5 (3) of the EAA's charter, the primary requirements are to minimise losses and ensure that the EAA is solvent at all times. As a result, the earnings situation, the change in equity and ensuring solvency at all times are also major performance indicators for the EAA. Each of the EAA's decisions is made in consideration of the aforementioned control metrics, and their contribution to the wind-up success is assessed.

Administrative expenses are highly important, too. The costs of the planned reduction of portfolio volume are controlled within the scope of budget planning and ongoing cost controlling. Cost controlling plays a key role within the EAA because, due to legal provisions, it is not possible for winding-up agencies to offset operating costs through profitable new business.

Alongside planning, controlling is supported by ongoing monitoring. The reporting process provides the members of the Managing Board and the department heads with a regular summary of all portfolio measures taken, as well as all relevant data regarding the EAA's control metrics. Alongside reporting, actual-to-plan analyses are performed to identify deviations from the winding-up plan, to explain them in detail and derive corresponding recommendations for action.

## The EAA's locations

The EAA has its registered office in Düsseldorf. The EAA does not maintain any other locations. The EAA holds stakes in domestic and foreign subsidiaries, which have their own employees.

## Economic report

### Economic environment

#### **The pandemic dominated 2020 – will the recovery come in 2021?**

The global outbreak of the coronavirus was a turning point for the economy, politics and financial markets. The corona pandemic required a concerted effort by countries and their central banks to keep the effects on the economy, health care and financial markets at a manageable and acceptable level. Governments initially tried to deal with the virus outbreak by drastically restricting public life.

The curtailment of public life (company closures, working from home, suspension of travel and, in some cases, of the movement of goods) had noticeable consequences for the economy and the financial markets. The lockdowns burdened the profitability of companies both on the production side, due to a lack of deliveries and closed production facilities, and on the demand side, due to a lack of customer demand. This led to the collapse of share prices and valuations of many assets during spring of 2020. The DAX 30 reached a low (on a closing price basis) of 8,442 points on 18 March 2020, down 36.3% from the start of the year. The collapse in valuations on other stock markets were of a similar dimension. The S&P 500 plummeted by 30.7%, the FTSE 100 by 33.8% and the EURO STOXX 50 by 35.3%.

The easing of lockdowns in the early summer of 2020 and the prospect of effective vaccinations led to a sustained period of recovery in capital markets, which offset the losses of the corona crisis largely or even fully in part. The S&P 500, for example, ended 2020 with a gain of 16.3%, while the DAX 30 was able to improve by 3.5%.

The outlook for 2021 continues to be driven by the corona pandemic. The various vaccines now available could provide a path out of the harsh containment measures and open up into economic recovery. However, this is not certain at this stage.

#### **US economy: The long-term damage caused by the crisis is difficult to quantify**

Economic performance in the US declined by 1.25% and 8.4% respectively in the first two quarters of 2020 and rebounded by 8.4% and 1.0% in the third and fourth quarters of 2020. Overall, the crisis led to a 3.5% decline in US GDP in 2020. According to the National Bureau of Economic Research (NBER), the US has been in a recession since February 2020.

In many categories, this pandemic recession exceeds what was observed in previous recessions. The increase in US unemployment reached an all-time high of 13.1% in summer 2020. New ground was broken in other categories too. The viral shock resulted in an 8.3% drop in consumer spending in the second quarter of 2020 – much greater than in other recessions.

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The US Congress and the White House passed several fiscal packages to support US companies and households during the crisis. The budget deficit also increased in 2020; having fluctuated between 2.7% and 4.7% of US economic output from 2013 to 2019, it climbed to 15.8% in 2020. The Fed also played its part and cut the fed funds rate from a range of 1.5% to 1.75% to 0% to 0.25%. It also increased the volume of its quantitative easing purchases. At the December 2020 meeting of the Federal Open Market Committee, the Fed's most important committee decided to spend at least USD 120 billion every month on purchasing US government bonds and other assets until such time as the labour market situation and price developments were in line with the Federal Open Market Committee's expectations.

**Forecast for the US: How robust is the recovery and how fast is it progressing?**

The stimulus package announced by the new US administration during the election campaign will hardly include the USD 1,900 billion that was hinted at. Market expectations are more in the range of USD 900 billion to USD 1,200 billion. However, with this package also giving US economic growth a noticeable boost, at least in the short term, the EAA expects US GDP to rise by 4.1% in 2021.

Government spending, private investment and private consumption are likely to be the central pillars of economic growth. Customer reticence in the past four quarters has led to pent-up demand among US consumers. Given that household finances are not burdened by excessive (new) debt, unlike in the 2001 or 2008 recessions, the EAA assumes that private consumer spending will increase by a good 5% in 2021. Private investment should increase even more, by +8%. An investment backlog needs to be cleared here too. In light of these developments, conditions in the US labour market should improve further in 2021. The unemployment rate is expected to fall from 8.1% in December 2020 to 6% in December 2021. Average job growth (non-farm payrolls) of 370,000 new jobs per month is expected. However, with some 750,000 jobs lost each month during 2020, it will take even longer to reduce the unemployment created in 2020.

The Fed's interest rate cuts and renewed massive purchases, together with the measures taken by the government, have improved the growth outlook. These concerted moves have fostered expectations of a rebound in inflation, which are reflected in the noticeable steepening of the US yield curve. The yield differential between the short (two-year term) and the long end (ten-year term) has increased from 35 basis points on 31 December 2019 to a current level of 103 basis points (11 February 2021). This expectation and the steepening of the yield curve has implications for the Fed's day-to-day operations. As much as it would like to see a sustained rise in inflation towards its implied inflation target of 2%, it is trying hard not to raise expectations of rapidly rising interest rates. Its current success in doing so is keeping interest rates and short-term yields unchanged for now.



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The rate of inflation will probably be at 2.2% at the end of 2021, with 2.0% to 2.1% expected for 2022, which is about in line with the target level of the economic policy. A further rise in US yield levels should therefore remain manageable. By the end of 2021, yields should be around 1.35% at the long end and roughly 0.3% at the short end, resulting in a noticeably steeper US yield curve compared to 2020.

**Eurozone: The pandemic hit the weaker eurozone states in particular**

The social and economic consequences of the corona pandemic were undoubtedly felt in all EU countries. At the same time, it became apparent that the countries that had suffered most from the euro debt crisis were also very negatively affected by the corona crisis. Italy and Spain struggled with high infection rates in the first corona wave in spring 2020, as well as in the second corona wave in autumn, and responded with widespread lockdowns.

The closure of companies and businesses had a corresponding negative impact on economic growth and tax revenues. Similarly, rising infection numbers led to additional expenditure in the healthcare sector, and in other areas of public administration and general public provisions.

Governments, the ECB and the EU responded to these burdens caused by the crisis with concerted action. Budgetary rules (a cap on debt) were suspended by the EU. In addition, the EU members states agreed on reconstruction assistance programme financed by the EU budget and EU borrowing. These measures are flanked by aid from the ECB, whereby it continued to buy euro government bonds and other securities at a monthly pace of EUR 20 billion. The ECB launched the pandemic emergency purchase programme. Under this programme, the ECB can purchase euro government bonds in a volume of up to EUR 1,850 billion, without being bound by the guidelines of the existing purchase programme. These purchases are assisted by additional long-term tenders offered at very favourable conditions (interest rate of -100 basis points) and higher allowances for banks on the negative deposit rate payments.

The containment measures imposed in Germany and among important trading partners have noticeably slowed down German economic growth in 2020. GDP fell by 5% in 2020. The economic slump could not be offset despite a partial easing of the measures in summer of 2020. Thanks to the short-time work programme, the situation on the labour market has not deteriorated dramatically. German unemployment increased by a comparatively moderate 1.1 percentage points to 6.1%.

The growth prospects for 2021 look good. If the containment measures are largely reversed from the summer onwards, German economic output is likely to rise again noticeably from the second quarter of 2021 onwards, more than compensating for the slight contraction in GDP in the first quarter. The EAA expects GDP to grow by a rate of 3.5% for the year 2021 as a whole.

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The corona pandemic also caused heavy losses in France. French economic output posted a 9% decline in 2020, driven mainly by the very long lockdown endured by the French in the second half of 2020. As in the rest of Europe, this has deferred consumer spending and private sector investment, which should open up the opportunity for a quick recovery in 2021 due to pent-up demand. In the core scenario, the EAA expects the French economy to grow by 5.8% this year. The easing of the lockdown in the second and third quarters of 2021 should prompt a growth spurt.

The past year has shown how susceptible Italy's economy is to problems. In 2020, the Italian economy contracted noticeably faster (-9%) than the average for the eurozone economy as a whole (-7.2%). The EAA expects the Italian economy to recover in 2021. With a quarterly gain of around 1.25%, the economic loss incurred in 2020 will not yet be fully recouped. The EAA expects GDP to increase by 4% to 5% in 2021 and by 4% in 2022.

Spain's economic performance in 2020 was severely affected by the corona crisis, with economic output contracting by 11%. The absence of tourist travel, high infection rates and harsh containment measures have contributed to this. The EAA expects the economic recovery to begin in 2021 and is forecasting a 5.9% increase in GDP.

**Financial markets and monetary policy: The ECB obeys the normative power of the facts ...**

... and has expanded the existing euro government bond purchase programme to include a special pandemic programme. The ECB wants to counter the problems of excessively low inflation rates and a shrinking economy with quantitative easing. At the same time, it is calling on the eurozone governments to use their spending powers and to stimulate the economy with additional spending. The ECB thus welcomes the EU reconstruction assistance. The ECB's very loose monetary policy and the reconstruction assistance should provide for fairly robust economic growth and higher inflation rates throughout Europe. However, at around 1% in 2021 and 1.2% in 2022, these still remain well below the ECB's inflation target of 2%. This means that for future monetary policy, very low yields and interest rates will be on the cards for quite some time. The ECB is likely to lower the deposit rate further.

Yields at the long end of the curve are expected to persist in negative territory at the end of 2021. The EAA expects yields to fluctuate within a range of -0.5% to -0.3%, with a yield of 0% expected for 2022. Yields at the short end will be driven by expectations of the ECB's monetary policy. The deposit rate is expected to be unchanged at -0.5% at the end of 2021. As a result of this measure, yields at the short end of the curve should be around -0.6% to -0.5% in December 2021. A yield of -0.4% is expected for 2022. With regard to the EUR/USD exchange rate, the EAA is expecting a price of USD 1.20 per EUR at the end of 2021.

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**Risks to the economic outlook – when will the lockdown end?**

In times of crisis such as these, the reliability of an economic forecast is significantly lower than in normal times, when one can orientate oneself on a reasonably well-established trend. This is due in particular to the difficulty of forecasting the further course of the pandemic.

If the current containment measures (lockdown) continue, there are concerns that 2021 will hardly differ from 2020. In this case, stagnation, low inflation rates and flight into safe government bonds would be expected.

**Overview of economic development**

In fiscal year 2020 the EAA's economic performance was largely determined by its wind-up mission.

The notional volume of the banking book fell 14.7% to EUR 12.7 billion. The notional volume of the trading portfolio declined by 30.9% to EUR 94.6 billion during the same period.

The results after taxes of EUR -1.9 million were defined in particular by general administrative expenses of EUR 125.0 million, the negative net fee and commission result of EUR -18.4 million and the negative balance of other expenses and income of EUR -17.2 million. These were largely offset by the positive net interest result of EUR 104.7 million, income from the reversal of loan loss provisions which, together with the results from financial assets and shareholdings, amounted to EUR 51.0 million, and the positive net trading result of EUR 3.2 million.

The EAA's total assets declined from EUR 37.8 billion in the previous year to EUR 32.2 billion. This is mainly due to the portfolio reduction, in particular the decline in trading assets and liabilities. The business volume, which also includes off-balance-sheet components, fell 14.2% to EUR 34.1 billion (previous year: EUR 39.8 billion).

**Wind-up report**

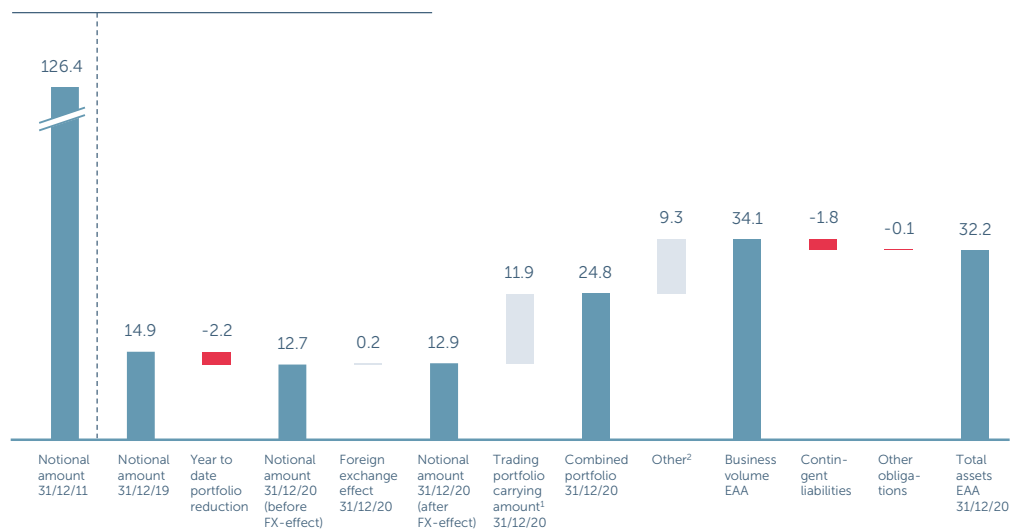
The figures and developments discussed in this section are regularly reported to the FMSA and to the EAA's governing bodies. They relate to the entire risk portfolio transferred to the EAA, regardless of whether these figures are recorded on- or off-balance-sheet in the EAA's separate financial statements or whether they are held via subsidiaries (look-through approach).

The following overview shows the changes in the portfolio's notional amounts since 1 January 2020 and the reconciliation to the EAA's total assets as of 31 December 2020.

## Reconciliation of the transferred notional volume to the balance sheet

in EUR billion

Notional values banking book



<sup>1</sup> Equates to the carrying amounts for trading portfolio assets.

<sup>2</sup> Contains the cash reserve, money market transactions, cash collateral and other assets not relevant for the wind-up portfolio.

Under the EAA's management strategy, the success of the winding-up plan is assessed on the basis of both the reduction in the notional volume before exchange rate effects (at constant exchange rates as of 31 December 2011 for the banking book and as of 30 June 2012 for the trading portfolio) as well as in terms of the effects on the winding-up plan. The latter takes into consideration the impact of sales proceeds, carrying amounts, expected losses, interest income and funding costs for the respective risk exposures, as well as transaction costs.

### Wind-up strategies

The banking book's risk exposures recorded in the winding-up plan for 2020 have been allocated in accordance with three stipulated standard strategies.

### Breakdown of the risk exposures of the banking book by standard strategy<sup>1</sup>

	31/12/2020 EUR billion	31/12/2019 EUR billion
Hold	10.7	8.0
Managed divestment	2.0	6.3
Self-monetisation	-	0.6
<b>Total</b>	<b>12.7</b>	<b>14.9</b>

<sup>1</sup> Excluding exchange rate effects (based on exchange rates as of 31 December 2011).

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The standard strategies for 2020 will thus be based on an investor or disposal perspective, and take into consideration the “Self-monetisation”, “Managed divestment” and “Hold” categories.

The “Self-monetisation” strategy comprises assets that will be repaid in full by year-end 2020, while the “Managed divestment” strategy takes into account long-term assets for which active portfolio measures are possible from the EAA’s perspective. The “Hold” strategy concerns positions that will probably be held until planned maturity owing to their specific features, although this does not preclude active portfolio management.

The winding-up plan for the trading portfolio makes no distinction based on the above strategies. The active management of the positions is modelled here. The portfolios are reduced via their normal maturities and active management.

**Wind-up success in the banking book**

From 1 January to 31 December 2020, the notional volume of the banking book was reduced from EUR 14.9 billion to EUR 12.7 billion (at exchange rates as of 31 December 2011, including the notional amounts of the guaranteed risk exposures and the risk exposures held by the EAA’s subsidiaries). That equates to a decline in notional volume of EUR 2.2 billion (14.7%). The volume at exchange rates as of 31 December 2020 is EUR 12.9 billion. The total banking book portfolio has decreased by EUR 113.7 billion or 90.0% since 1 January 2012.

Clusters	Notional volume (at exchange rates as of 31/12/2011)				Notional volume (at exchange rates as of 31/12/2020)	
	Notional 31/12/2020	Notional 31/12/2019	Change to 31/12/2019		Notional 31/12/2020	FX effect <sup>1</sup>
	EUR million	EUR million	EUR million	in %	EUR million	EUR million
Structured Securities	5,531.7	6,112.1	-580.4	-9.5	5,707.3	175.6
Public Finance & Financial Institutions	3,324.6	4,062.8	-738.2	-18.2	3,325.2	0.6
Real Assets	1,995.9	2,555.5	-559.6	-21.9	1,985.6	-10.3
Structured Products	1,213.6	1,336.4	-122.8	-9.2	1,279.7	66.1
Corporates	571.6	755.1	-183.5	-24.3	579.0	7.4
Equity/Mezzanine	61.4	60.0	1.4	2.3	61.9	0.5
<b>Total</b>	<b>12,698.7</b>	<b>14,882.0</b>	<b>-2,183.3</b>	<b>-14.7</b>	<b>12,938.7</b>	<b>239.9</b>

<sup>1</sup> Change in notional volume due to exchange rate effects.

Note: As of 31 December 2020, the total NPL portfolio amounted to EUR 1.7 billion at current exchange rates.

The portfolio reduction in the Structured Securities cluster is due in particular to partial repayments of the Phoenix A notes (USD/EUR).

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The notional reduction in the other clusters is distributed over the rest of the portfolio, with the changes here attributable in particular to repayments in the Public Finance & Financial Institutions and Real Assets clusters.

There was a EUR +23.6 million effect on the winding-up plan in fiscal year 2020 associated with sales and early repayments from the banking book portfolio. A winding-up plan effect of EUR -3.1 million was achieved from other measures. This effect arose mainly from the increase in risk provisions.

**Wind-up success in the trading portfolio**

The notional volume of the trading portfolio represents the business volume underlying the derivatives and not the exposure at risk.

The notional volume of the trading portfolio amounted to EUR 94.6 billion as of 31 December 2020. The notional volume of the trading portfolio decreased by a total of EUR 42.2 billion during the period from 1 January to 31 December 2020 (at exchange rates as of 30 June 2012). Since its transfer, the notional volume of the trading portfolio has been reduced by EUR 969.5 billion or 91.1%.

Clusters	Notional 31/12/2020 EUR million	Notional 31/12/2019 EUR million	Notional volume (at exchange rates as of 30/6/2012)		Notional volume (at exchange rates as of 31/12/2020)	
			Change to 31/12/2019 EUR million	Change to 31/12/2019 in %	Notional 31/12/2020 EUR million	FX effect <sup>1</sup> EUR million
Rates	92,647.9	134,324.9	-41,677.0	-31.0	91,281.4	-1,366.5
Other	1,917.5	2,470.3	-552.8	-22.4	1,517.9	-399.6
<b>Total</b>	<b>94,565.4</b>	<b>136,795.2</b>	<b>-42,229.7</b>	<b>-30.9</b>	<b>92,799.3</b>	<b>-1,766.1</b>

<sup>1</sup> Change in notional volume due to exchange rate effects.

The reduction in the Rates cluster with a total notional decrease of EUR 41.7 billion primarily resulted from active wind-up measures of EUR 28.7 billion, maturities totalling EUR 22.0 billion and contrary, portfolio-increasing hedging transactions in the amount of EUR 9.0 billion.

The notional volume of the Other cluster fell by EUR 0.6 billion due to maturities.

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EAA's overall situation

Earnings situation

The EAA's earnings situation was impacted by the net interest result of EUR 104.7 million, income from the reversal of loan loss provisions which, together with the results from financial assets and shareholdings, came to EUR 51.0 million, as well as by general administrative expenses of EUR 125.0 million, the negative balance of other expenses and income of EUR -17.2 million and the net fee and commission result of EUR -18.4 million. Personnel expenses totalled EUR 21.6 million. Other administrative expenses of EUR 103.4 million were comprised mainly of expenses for services rendered by EFS, as well as by IBM and MSPA.

The increase in the net interest result is mainly due to the profit transfer from a subsidiary. The results from financial assets and shareholdings developed positively. This was due in particular to the improved economic environment compared with when the corresponding assets were taken over. Risk provisions were reduced for the same reasons.

Fee and commission expenses as part of the net fee and commission result are attributable mainly to the commitment fee for the equity capital drawing limit. The net trading result of EUR 3.2 million was down on the same period of the previous year.

Overall, the results after taxes amounted to EUR -1.9 million (previous year: EUR -2.7 million).

Income statement

	1/1-31/12/2020	1/1-31/12/2019	Change	
	EUR million	EUR million	EUR million	in %
Net interest result	104.7	80.9	23.8	29.4
Net fee and commission result	-18.4	-17.7	-0.7	-4.0
Net trading result	3.2	6.5	-3.3	-50.8
Total other operating expenses/income	-17.2	-14.5	-2.7	-18.6
Personnel expenses	-21.6	-23.4	1.8	7.7
Other administrative expenses	-103.4	-112.3	8.9	7.9
Results from financial assets and shareholdings	21.9	29.7	-7.8	-26.3
<b>Results prior to risk provisioning</b>	<b>-30.8</b>	<b>-50.8</b>	<b>20.0</b>	<b>39.4</b>
Loan loss provisions	29.1	48.8	-19.7	-40.4
<b>Results before taxes</b>	<b>-1.7</b>	<b>-2.0</b>	<b>0.3</b>	<b>15.0</b>
Taxes	-0.2	-0.7	0.5	71.4
<b>Net result for the year</b>	<b>-1.9</b>	<b>-2.7</b>	<b>0.8</b>	<b>29.6</b>
Net retained losses brought forward	-2,360.7	-2,358.0	-2.7	-0.1
Net retained losses	-2,362.6	-2,360.7	-1.9	-0.1

**MANAGEMENT REPORT**

**Net interest result**

At EUR 104.7 million, the net interest result was up on the previous year (EUR 80.9 million).

In addition to net interest income (EUR 58.0 million [previous year: EUR 74.1 million]), the net interest result also included current income from equities, other non-fixed-income securities, long-term equity investments and shares in affiliates (EUR 4.9 million [previous year: EUR 2.6 million]) as well as income from profit pooling, profit transfer and partial profit transfer agreements (EUR 41.8 million [previous year: EUR 4.2 million]), in particular the EUR 40.1 million profit transfer of Erste EAA Anstalt öffentlichen Rechts & Co. KG.

The interest income arose from lending and money market transactions totalling EUR 300.7 million (previous year: EUR 414.7 million) and from fixed-income securities and debt register claims in the amount of EUR 96.2 million (previous year: EUR 135.5 million).

The interest income was offset by interest expenses of EUR 338.9 million (previous year: EUR 476.1 million).

**Net fee and commission result**

The net fee and commission result of EUR -18.4 million (previous year: EUR -17.7 million) is primarily due to the commitment fee payable for the equity capital drawing limit.

**Net trading result**

The net trading result amounted to EUR 3.2 million (previous year: EUR 6.5 million) and is composed of the interest, foreign exchange and valuation result in the amount of EUR -5.1 million (previous year: EUR 6.8 million) and the recognition in the income statement of the reversal of the model reserves totalling EUR 8.3 million (previous year: EUR -0.3 million).

**Total other operating expenses/income**

The balance of other operating expenses and income amounted to EUR -17.2 million (previous year: EUR -14.5 million), largely as a result of the creation of provisions.

**General administrative expenses**

General administrative expenses in the previous fiscal year totalled EUR 125.0 million (previous year: EUR 135.7 million). The EAA's personnel expenses accounted for EUR 21.6 million of this amount (previous year: EUR 23.4 million).

Of the other administrative expenses amounting to EUR 103.4 million (previous year: EUR 112.3 million), EUR 44.1 million (previous year: EUR 46.0 million) was due to the cooperation agreement with EFS and EUR 12.5 million (previous year: EUR 15.1 million) to the service agreement with MSPA to support the EAA with portfolio management and all associated activities. Additional costs of EUR 1.7 million (previous year: EUR 4.7 million) were incurred in connection with asset-sustaining measures. These include, in particular, expenses relating to the restructuring of exposures at risk of default.



**MANAGEMENT REPORT**

**Loan loss provisions**

There was a net release of EUR 29.1 million (previous year: EUR 48.8 million) from loan loss provisions in fiscal year 2020. The EAA has appropriately taken into account all recognisable risks.

**Results from financial assets and shareholdings**

Financial assets and shareholdings produced net income totalling EUR 21.9 million (previous year: EUR 29.7 million). This included net income in the amount of EUR 4.3 million from shareholdings in the financial investment portfolio and EUR 17.6 million from securities. The income from securities is mainly the result of reversals of write-offs.

The net result from shareholdings arose essentially from reversals of write-offs (EUR 3.1 million), payments above the respective carrying amounts (EUR 1.6 million) and selling shareholdings (EUR 0.8 million). This was offset mainly by expenses from write-offs of shareholdings (EUR 0.7 million) and expenses from loss assumptions (EUR 0.4 million).

**Taxes**

Taxes comprise taxes on income and earnings in the amount of EUR 0.2 million (previous year EUR 0.7 million), which mainly relate to foreign withholding taxes.

**Net result for the year**

The net result for the year amounted to EUR -1.9 million (previous year: EUR -2.7 million) and increased net retained losses carried forward to EUR 2,362.6 million.

**Financial position and issuing activity**

**Key tasks in the refinancing process**

The EAA is an issuer of securities and operates on the capital market as an independent legal entity with its own rating for the purposes of refinancing and winding-up activities. The EAA commissions financial institutions to distribute its issues to suitable investors.

The EAA's management and ALCO make strategic decisions regarding the issuing schedule, the issuing prospectus, markets and pricing, while the commissioned financial institutions act as advisors.

Prior to conducting an issuance, the EAA calculates its liquidity needs in preparation for the strategic and operational decision-making process. When doing so, it factors in the maturity structure of liabilities as well as the inflow of liquidity from the repayment of assets.

The EAA draws up a long-term issuing strategy, which is regularly reviewed – supported by consultations with banks and feedback from investors – and then modified if necessary. The documentation for the issuing prospectuses is prepared jointly with the commissioned financial institutions and external legal advisors.

MANAGEMENT REPORT

**Current funding volume**

The total notional amount of the portfolio of issued bearer bonds, promissory note loans and commercial paper was EUR 17.8 billion as of the reporting date. It included the global Commercial Paper Programme with a notional amount equivalent to EUR 7.9 billion.

During the reporting period, the notional volume of new issues for medium and long-term funding amounted to EUR 3.2 billion, of which EUR 2.2 billion (USD 2.8 billion) was accounted for by bonds denominated in US dollars.

New issues were launched during the reporting period under the global Commercial Paper Programme, of which a notional amount equivalent to EUR 7.9 billion was outstanding at the reporting date. These consisted of USD 6.5 billion (EUR 5.3 billion), GBP 1.4 billion (EUR 1.6 billion) and EUR 1.0 billion.

As of the reporting date, the portfolio contained securities issued by the EAA with a notional volume of EUR 30 million that were repurchased from the market for liquidity management purposes.

In the liquidity stress test, the EAA had net liquidity above the internal established threshold value at all times during the reporting period.

**Asset position**

The EAA's total assets as of the reporting date amounted to EUR 32.2 billion (previous year: EUR 37.8 billion), which, with the inclusion of off-balance-sheet components, amounted to a business volume of EUR 34.1 billion (previous year: EUR 39.8 billion).

**Assets**

	31/12/2020 EUR million	31/12/2019 EUR million	Change EUR million	in %
Cash reserve	3,450.7	1,768.9	1,681.8	95.1
Loans and advances to banks	3,188.4	5,662.4	-2,474.0	-43.7
Loans and advances to customers	7,172.9	8,292.0	-1,119.1	-13.5
Securities (no trading portfolio)	5,439.7	5,432.1	7.6	0.1
Trading portfolio	11,858.6	15,392.5	-3,533.9	-23.0
Long-term equity investments and shares in affiliates	970.6	1,063.1	-92.5	-8.7
Other assets	85.2	204.0	-118.8	-58.2
<b>Total assets</b>	<b>32,166.1</b>	<b>37,815.0</b>	<b>-5,648.9</b>	<b>-14.9</b>

MANAGEMENT REPORT

Liabilities and equity

	31/12/2020	31/12/2019	Change	
	EUR million	EUR million	EUR million	in %
Deposits from banks	1,733.1	2,119.0	-385.9	-18.2
Deposits from customers	1,720.2	1,953.1	-232.9	-11.9
Debt securities in issue	16,259.1	17,897.1	-1,638.0	-9.2
Trading portfolio	11,350.6	15,044.8	-3,694.2	-24.6
Provisions	114.5	105.6	8.9	8.4
Other liabilities	335.0	39.9	295.1	>100
Equity	653.6	655.5	-1.9	-0.3
<b>Total liabilities and equity</b>	<b>32,166.1</b>	<b>37,815.0</b>	<b>-5,648.9</b>	<b>-14.9</b>
Contingent liabilities	1,812.6	1,770.3	42.3	2.4
Other obligations/loan commitments	137.4	186.2	-48.8	-26.2
<b>Business volume</b>	<b>34,116.1</b>	<b>39,771.5</b>	<b>-5,655.4</b>	<b>-14.2</b>

**Cash reserve**

The cash reserve increased by EUR 1.7 billion compared with the end of the previous year, due to an increased holding of balance held with the Bundesbank to reduce liquidity risks and smooth the liquidity outflow profile as part of active liquidity management.

**Lending business**

The lending business comprises loans and advances, payment obligations arising from irrevocable loan commitments, sureties and other guarantees. Contingent liabilities also include Portigon risk exposures that were transferred using the "guarantee" alternative. Loans and advances also contain registered and other non-marketable debt instruments.

Lending business

	31/12/2020	31/12/2019	Change	
	EUR million	EUR million	EUR million	in %
Loans and advances to banks	3,188.4	5,662.4	-2,474.0	-43.7
Loans and advances to customers	7,172.9	8,292.0	-1,119.1	-13.5
Contingent liabilities	1,812.6	1,770.3	42.3	2.4
Other obligations/loan commitments	137.4	186.2	-48.8	-26.2
<b>Lending business</b>	<b>12,311.3</b>	<b>15,910.9</b>	<b>-3,599.6</b>	<b>-22.6</b>

Loans and advances to banks declined by EUR 2.5 billion as of the reporting date compared with the end of the previous year, with money market transactions and reverse repo transactions together accounting for EUR 1.7 billion, lower bank balances for EUR 0.5 billion and a lower volume of cash collateral for EUR 0.3 billion.

**MANAGEMENT REPORT**

The decline in loans and advances to customers (EUR 1.1 billion) is mainly due to repayments.

**Securities**

The securities portfolio remains unchanged year-on-year at EUR 5.4 billion. The repayments, of which EUR 0.4 billion are attributable to Phoenix notes, are offset by the assumption of EAA CBB's securities portfolio, so that the portfolio remains largely unchanged. EUR 31.0 million (previous year: EUR 31.0 million) was allocated to the liquidity reserve.

The EAA had not concluded any securities lending transactions, either in the fiscal or in the previous year.

**Trading portfolio**

Trading assets are recognised in the balance sheet at fair value less a risk discount, or, in the case of trading liabilities, plus a valuation premium. As of the reporting date, the EAA reported trading assets and liabilities with carrying amounts of EUR 11.9 billion (previous year: EUR 15.4 billion) and EUR 11.4 billion (previous year: EUR 15.0 billion) respectively. These relate almost entirely to derivative transactions.

The decline of EUR 3.5 billion and EUR 3.7 billion in trading assets and liabilities respectively was mainly the result of the portfolio reduction.

**Long-term equity investments and shares in affiliates**

The EAA has taken over shares of a large number of companies from the former WestLB. As of the reporting date, the carrying amount of long-term equity investments amounted to EUR 36.0 million (previous year: EUR 37.7 million) and shares in affiliates totalled EUR 934.6 million (previous year: EUR 1,025.4 million).

The carrying amounts of the long-term equity investments decreased mainly due to write-offs and capital reductions on several foreign shareholdings (EUR 1.2 million) and foreign exchange effects (EUR 0.7 million). This was offset by increases in book value due to capital injections of EUR 0.1 million.

The volume of shares in affiliates fell by EUR 90.8 million, mainly because of a capital withdrawal (EUR 93.3 million) at one domestic affiliate and a capital repatriation at another domestic affiliate (EUR 0.5 million). This was offset by reversals of write-offs (EUR 3.1 million) at domestic companies.

The balance sheet items long-term equity investments and shares in affiliates also include equity interests from loan restructuring (debt-to-equity swap).

**Deposits from banks and customers**

As of the reporting date, deposits from banks totalled EUR 1.7 billion (previous year: EUR 2.1 billion). Of this total, EUR 0.9 billion (previous year: EUR 1.7 billion) was accounted for by cash collateral received.

The deposits from customers in the amount of EUR 1.7 billion (previous year: EUR 2.0 billion) mainly consisted of issued registered bonds equalling EUR 1.5 billion (previous year: EUR 1.7 billion).

**MANAGEMENT REPORT**

**Issuing business**

The portfolio of debt securities in issue totalled EUR 16.3 billion (previous year: EUR 17.9 billion) as of the reporting date.

Please refer to the "Financial position and issuing activity" section for more information on issuing activities.

**Provisions**

Provisions amounted to EUR 114.5 million (previous year: EUR 105.6 million) as of the reporting date. The predominant part of the existing provisions is attributable to winding-up activities. A provision of EUR 11.2 million was established for legal risks. The EAA also created provisions of EUR 2.0 million for tax liabilities.

**Equity**

The EAA's subscribed capital remained unchanged at EUR 500,000 as of the reporting date. In addition, the first transfer of risk exposures and non-strategic business units of the former WestLB created a capital reserve in the amount of around EUR 3,013.2 million. Due to the refill in fiscal year 2012 the capital reserve was reduced by EUR 123.8 million (of which EUR 13.1 million in fiscal year 2013 was due to a contractual value adjustment clause) to its current level of EUR 3.0 billion. This reduction was essentially caused by the measures agreed in the content of the key point agreement dated 29 June 2011 and the binding protocol dated 18 June 2012.

As of the reporting date, the equity capital under HGB stood at EUR 653.6 million (previous year: EUR 655.5 million). Besides the net retained losses, this amount included other retained earnings of EUR 2.4 million resulting from the reversal of provisions whose values decreased due to revisions in the method to measure liabilities under BilMoG.

For further information about these changes, please refer to the section "Wind-up report".

**Summary of the business situation**

As planned, the EAA achieved a lower net interest result (excluding special effects from current income and income from profit pooling) due to the portfolio reduction. The fee and commission expenses, administrative expenses and other operating expenses incurred led to a negative operating result. The income from the reversal of risk provisions could not offset these as of 31 December 2020, so that a loss was reported for fiscal year 2020.

The EAA's assets are in good order. Its equity as of 31 December 2020 amounted to EUR 653.6 million. Adequate liquidity was available at all times.

Significant events after the reporting date are disclosed in the notes ("Subsequent events" section).

## Financial and non-financial performance indicators

### Financial performance indicators

As the EAA's aim is to wind up transferred assets in a manner that preserves value and minimises risk, the financial performance indicators used for the EAA's internal management purposes are not comparable with the performance indicators normally used by banks.

Return on equity, for instance, is not in the foreground of the EAA's business strategy. Instead, the EAA is managed by performance indicators that show the effects on its earnings situation or on its wind-up result. These performance indicators include the portfolio reduction in the banking book or the trading portfolio, as well as the net interest and net fee and commission result. These performance indicators are reported in the wind-up reports on a regular basis in both absolute and relative terms. The starting point for the analysis of the overall portfolio's wind-up success is 31 December 2011 for the banking book and 30 June 2012 for the trading portfolio (see also the "Wind-up report" section).

Moreover, there are further performance indicators in the "performance indicator cockpit" of the quarterly wind-up reports. These performance indicators include ratios for maturities for the banking book portfolio and income statement ratios in relation to total assets, from the risk provisioning ratio on the portfolio as a whole and on the sub-portfolios as well as the cost/income ratio. Both historical values and current values are used to analyse these performance indicators.

The specifics of the financial performance indicators are set out in the "Wind-up report" and "EAA's overall situation" sections.

### Non-financial performance indicators

#### Employees

Highly qualified, motivated, creative and loyal employees with a willingness to perform and personal responsibility are a major success factor of the EAA.

Thanks to their identification with the EAA and their commitment, these employees make a pivotal contribution to the fulfilment of the public mandate of the EAA. When doing so, their talent, skills and potential are supported and encouraged through a high level of individual responsibility as well as targeted training measures. The manager responsible for each employee conducts a structured personnel development meeting once a year, at the employee's request. This meeting aims to assess the performance of the past year on the one hand and to set the target agreement for the coming months on the other.

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Human resources work creates an environment in which the employees are able to develop and enhance their qualifications as best as possible based on their current phase of life. This is a key factor in employee loyalty and identification with the EAA. In winding up the portfolio, the EAA has taken on a complex public mandate and therefore has high standards when it comes to its employees. To secure this expertise, personnel management measures are offered, such as including multidisciplinary projects, job rotation and programmes for developing personal skills.

The EAA maintains a performance-oriented culture characterised by mutual respect.

As of 31 December 2020, the EAA employed 130 members of staff (excluding two Managing Board members). The number was reduced compared with the previous year (31 December 2019: 159 employees excluding three Managing Board members). The development of employee numbers represents a non-financial performance indicator for the EAA, which is reviewed annually as part of the winding-up planning and adjusted to present circumstances during the year, if necessary.

**Reputation and acceptance**

As a public institution, the EAA needs the acceptance and trust of governments and the general public in order to successfully fulfil its mandate. The EAA also attaches special importance to its public image since it impacts its funding options on the capital market. With this in mind, potential reputational risks are extremely important for the EAA.

The EAA mitigates these risks through media and public relations activities that are designed to deliver the greatest possible transparency. Aside from regular publications such as annual and interim reports or the latest information on the EAA's website, this also includes contact with representatives of business and financial publications as well as the public media.

Furthermore, the employees foster an understanding for the special features of the EAA's wind-up mandate by maintaining contact with multiplier groups, for example by taking part in conferences or holding talks with political and financial representatives and with investors.

The EAA also boosts awareness of the EAA and its local anchoring in the Düsseldorf region by encouraging its employees to get involved in their communities.

## Risk, opportunities and forecast report

### Risk report

A common objective of the liable stakeholders, the FMS and the EAA is to minimise its strategic wind-up risk, that is to say, the risk of a negative deviation from the economic targets in the winding-up plan and suffering higher-than-planned losses from winding up the portfolio. The EAA made further progress during the reporting period towards realising its wind-up mandate.

The figures and developments discussed in this section are regularly reported to the FMSA as part of its supervision of the EAA. They relate to the entire assets transferred to the EAA, regardless of whether these figures are recorded on- or off-balance-sheet in the EAA's separate financial statements, or whether they are held via subsidiaries (look-through approach).

#### Risk management organisation

The EAA is supervised by BaFin with regard to those provisions of banking law that are applicable to the EAA. MaRisk are almost entirely applied by the EAA.

The EAA is different from a commercial bank. This has a significant impact on its risk strategy. As the EAA does not acquire new business, but rather only increases lines of credit in exceptional instances in connection with restructuring measures and manages liquidity, the EAA does not have the same functions that are normally included in a bank's risk strategy for managing new business. Nor does the EAA have to apply capital adequacy rules. The requirement to fulfil the wind-up mandate based exclusively on the existing equity and not having to call upon any other equity instruments or the liable stakeholders' duty to offset losses is a significant challenge for the quality and capability of the risk management team.

The aim of the EAA's risk management is therefore to minimise strategic wind-up risk. The risk management team's responsibility is to map, analyse, manage and monitor the EAA's risks using a comprehensive risk reporting system.

The Managing Board determines the risk strategy. The Risk Committee of the Supervisory Board discusses the risk strategy and the risk policy principles set down therein with the Managing Board. On the recommendation of the Risk Committee, the Supervisory Board will decide on the principles relating to risk assumption contained in the risk strategy.



**MANAGEMENT REPORT**

The general risk management strategy forms the basis for the risk management framework. It contains the basic principles for risk management, defines the key risk categories and identifies the core elements of the risk management process. The general risk management strategy is supplemented by specific strategies for managing individual risks, including the related wind-up strategies. The key individual strategies relate to the risk categories of credit risks, market price risks, liquidity risks, longevity risks and operational risks (including reputational, legal and tax risks). The risk management strategies are reviewed at least once a year.

The Managing Board has implemented a structure of various interdisciplinary committees throughout the institution and its departments to aid it in fulfilling its responsibility to manage risk. As Managing Board committees, these committees are permanent institutions of the EAA. They serve as central decision-making, management and information-gathering bodies which assist in dealing with strategic issues related to portfolio management and the winding-up plan.

The committees which make decisions regarding risk management strategies and methods are the:

- △ RiskCo – covers portfolio management and in particular the management of credit risks
- △ ALCO – covers the optimisation of asset/liability management, monitoring and managing operational liquidity, funding, interest rate and foreign exchange risks, the trading portfolio as well as the operational risks (including reputational, legal and tax risks)

The Risk Controlling department is responsible for the independent monitoring and communication of the EAA's risks. Its tasks include in particular the following:

- △ Supporting management in connection with all risk policy issues, especially in the development and implementation of the risk strategy as well as in the organisation of a system for mitigating risks,
- △ Conducting a risk inventory and preparing the overall risk profile; and
- △ Assisting management with the establishment and development of risk management and risk controlling processes.

The Risk Controlling department is responsible for monitoring market price, counterparty, liquidity and operational risks. The Credit Risk Management department comprises the back-office function in the lending business as defined by MaRisk. In particular, this department functions as the lending authority. It is also responsible for credit risk steering and credit risk controlling. The Risk Controlling and Credit Risk Management departments monitor and analyse risk exposures as well as the utilisation of the limits. They also take measures to reduce risks if necessary.

The risk management system is regularly reviewed by the EAA's Internal Audit department.

**MANAGEMENT REPORT**

**Risk reporting**

Risks can be controlled and monitored in a sustainable manner only if they are transparent, and the underlying analysis results are prepared and communicated in a manner that is conducive to decision-making processes. For this reason, risk reporting is among the key tasks of the Risk Controlling department. The FMSA, the responsible committees, the Managing Board as well as the Supervisory Board and its committees are informed on a regular basis of any and all developments that might have an impact on the institution's risk or earnings situation. Risk reporting is a component of the monthly wind-up report and the quarterly risk report.

The Managing Board keeps the Supervisory Board and its committees regularly informed of the EAA's current wind-up status and the general risk situation, based on wind-up reports and a separate risk report that is adapted to fulfil the information requirements of the governing bodies.

**Risks from the corona pandemic**

**Financial risks**

The corona pandemic had no serious negative financial impact for the EAA.

Despite the initial turmoil in the financial markets, the EAA's liquidity situation remained good. Although the distortions resulted initially in rising risk premiums and therefore liquidity costs, the EAA was able to raise the required amount of liquidity at all times. The market has already returned to normal in the second quarter of 2020.

Market risk positions continued to be held within their tight limits. Despite very high market volatility in the beginning, the number of hedging transactions required was kept low, so that even a higher bid-ask spread had no particularly negative impact. Market volatility had already declined again in the second quarter of 2020.

Due to the structure of the EAA's remaining portfolio, the coronavirus has had little impact on credit risk to date. The EAA has reviewed all exposures for potential impact of the corona pandemic. In fiscal year 2020, rating downgrades reflected the deteriorating credit quality due to the corona crisis. In addition, exposures particularly affected by the corona crisis are presented separately as part of cluster and portfolio analyses.

In addition to rating downgrades of one or two notches, only a few restructurings or loan extensions were necessary up to now. Risk provisions had to be increased only relatively slightly so far (by less than EUR 10 million). However, the final effects cannot yet be quite accurately assessed as the pandemic continues develop.

The EAA portfolio holds no or hardly any sectors that are generally hard hit; these include the automotive industry, airlines, the hospitality industry, mechanical engineering, shipping, tourism and event management. Infrastructure project financing (in particular airports, toll roads and ports) represents an exception here. However, the total exposure of infrastructure project financing is low relative to the EAA's overall portfolio.

**MANAGEMENT REPORT**

According to information provided to the EAA, some countries have been granting borrowers payment deferrals through moratoriums for months now (including Germany until 31 March 2021). As a result, there were some additions and changes to the EAA GW (see also the "Problem loans and risk provision" section).

Banks with which the EAA concludes hedging operations, for example, have massively increased their risk provisions in 2020 and are already reporting losses in some cases, which has led to rating downgrades. However, the effects are significantly lower overall than those experienced in the financial crisis; moreover, the banks were generally better positioned when the corona crisis began.

**Non-financial risks**

Due to the corona pandemic, the EAA established a task force that has been in place since 26 February 2020. It originally met twice a week and since June 2020 once a week under the direction of the Managing Board. The task force directly informs the EAA's crisis unit of its decisions to protect the EAA's employees. Employees are given timely and practical guidance on conduct and hygiene. For this purpose, a webpage containing all the important information has been set up on the intranet, which is continuously adapted and supplemented. External employees and visitors receive information about the rules to be observed from their internal EAA contacts. In addition, opportunities for working-from-home capabilities, including teleconferencing and web conferencing, have been put in place since 12 March 2020. Since then, up to 80% of employees are working from home every week. The operational readiness of the EAA building is ensured by extended cleaning measures.

In addition, IBM and MSPA, as the EAA's primary service providers, have provided their services, without being impaired in any way by the corona pandemic.

The absence of any cases of coronavirus in the EAA demonstrates the success of the measures implemented. The EAA's operations were stable during fiscal year 2020.

**Credit risks**

Under credit risks, the EAA distinguishes between default risks, migration risks, counterparty risks, issuer risks, participation risks and country risks:

- △ Default risk comprises potential losses incurred if a borrower is unable or unwilling to comply, in part or in full, with his contractual obligations, specifically the obligation to repay his loan.
- △ Migration risk comprises potential losses calculated mathematically if the amount of the expected loss on interest and principal payments increases as a result of a deterioration in a borrower's creditworthiness.
- △ Counterparty risk comprises potential losses from the default of counterparties of derivatives transactions or where their creditworthiness deteriorates. Counterparty risk also includes settlement risk. Counterparty risk is determined for both the banking book and the trading portfolio.

**MANAGEMENT REPORT**

- △ Issuer risk comprises potential losses that arise if issuers of securities held in the portfolio fail to perform or if their creditworthiness deteriorates.
- △ Participation risk includes potential losses due to omission of dividends, impairments, losses on disposals and a reduction in hidden reserves from the EAA's shareholdings.
- △ Country risk comprises the inability of a borrower to meet its obligations, essentially due to sovereign acts.

**Analysis and assessment of credit risks**

The EAA's Risk Controlling department in conjunction with the Credit Risk Management department continuously analyses and monitors the loan portfolio and its default and migration risks. In order to assess the potential consequences of systemic crises, stress tests are performed regularly to monitor how a portfolio-wide rating downgrade of several rating categories would impact the expected loss. The amount of loan loss provisions and changes to that amount are estimated at the general portfolio level. Two stress scenarios for default risks as well as one inverse stress test for the exposure of the eurozone periphery are applied when preparing the winding-up plan. Moreover, the portfolio is monitored for concentration risks in individual sub-portfolios, asset classes and regions.

The EAA assesses credit risk in terms of both the overall portfolio and individual exposures. Credit quality and default probabilities are regularly assessed on the basis of balance sheet analyses and ratings. A clearly defined process facilitates the analysis of problematic exposures and the determination of alternative options, which are presented to the relevant competent individuals or bodies of the EAA for approval. The ratings of the performing loans are also reviewed promptly and adjusted if necessary. The effects of the corona crisis are also taken into account in this way in the rating of individual borrowers, if they are affected by it. As of 31 December 2020, all ratings of the banking book had already been reviewed. Additional cluster and portfolio analyses are performed separately for significant individual exposures. This also includes portfolio analysis and reporting of the exposures affected by the corona crisis.

A central focus of portfolio analysis also includes problem loans. These are intensively monitored and actively managed. The EAA GW provides a mechanism for monitoring problem loans and exposures under intensive supervision. Additional details are provided in the "Problem loans and risk provision" section. The appropriateness of risk provisioning is determined by analysing the recoverable value of the loan/advance, the expected cash flow and the existing collateral.

**MANAGEMENT REPORT**

**Management of credit risks**

The most important tools used to manage credit risk are the restructuring or sale of loans, taking into account the effect of the winding-up plan. Additionally, the EAA can enter into credit default swaps and other credit derivatives to hedge individual exposures.

Default risks are generally limited to the amount of the credit lines that Portigon had provided prior to the date the portfolio was transferred. Increases are permitted exceptionally only in connection with restructuring measures, provided they contribute to the loss reduction. When borrowers repay portions of their loans, the committed credit lines and the limits are reduced by a corresponding amount.

Migration risks and rating distributions within the portfolio are monitored regularly and reported to the EAA's relevant supervisory bodies. Deteriorating credit quality – also insofar as it is caused by the corona crisis – is reflected by rating downgrades. Rating downgrades for individual exposures are assessed as part of the credit process and the exposures concerned are reviewed to check for alternative courses of action; these options may include restructuring or sale. The approach towards the borrower is then approved by the relevant individuals with the appropriate level of authority according to the authority rules.

The EAA analyses counterparty risks by monitoring and assessing the exposures using internal calculations. The method used to determine the exposure for OTC derivatives takes collateral and netting into account. Master agreements with netting and symmetrical collateralisations are used to mitigate counterparty risks.

Issuer risks from the trading portfolio are limited to the amount of the transferred exposures towards individual issuers as part of the refill. Issuer risks are monitored and managed in the same manner as default risks.

**Credit risks – banking book**

The credit risk of the EAA and its subsidiaries is regularly analysed so as to identify, analyse, evaluate and manage all default risks within the portfolio. The EAA uses a variety of parameters – such as risk type, rating categories, maturities and regions – to identify risk concentrations.

The notional volume of the banking book portfolio (which primarily consists of loans and securities) declined by EUR 2.2 billion during fiscal year 2020 to EUR 12.7 billion (at constant exchange rates as of 31 December 2011). Please refer to the section "Wind-up report" for more detailed information on the wind-up success.

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Breakdown of notional volume by internal rating category<sup>1</sup>

	31/12/2020 EUR billion	31/12/2019 EUR billion
A0-A2	0.3	0.8
A3-A5	1.9	3.8
B1-B3	0.5	0.6
B4-B5	4.1	1.8
C1-C2	2.4	3.3
C3-C5	1.2	1.4
D1-D3	0.3	0.6
D4-E	0.5	0.6
S.R.	1.3	1.4
N.R.	0.2	0.5
<b>Total</b>	<b>12.7</b>	<b>14.9</b>

<sup>1</sup> Excluding exchange rate effects (based on exchange rates as of 31 December 2011).  
Note: Where possible, the internal rating categories are based on the guarantor's rating.

The quality of the banking book portfolio was reflected in an investment grade rating share (rating categories A0-C2) of around 72% (31 December 2019: 69%). About 17% (31 December 2019: 31%) of the notional volume had a very good rating (A0-A5) and around 55% (31 December 2019: 39%) is assigned to the mid-rating categories B1-C2. The rating category S.R. included the opening clauses of the rating process and has a share of around 10% of the total portfolio (31 December 2019: 9%).

The EAA continued to aim for a portfolio reduction across all rating categories.

One rating procedure was discontinued in fiscal year 2020. As a result, new non-rating reasons were introduced to classify assets according to their fundamental value. This resulted in shifts mainly in the rating category B4-B5 from the rating categories A0-A2, A3-A5 and C1-C2.

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The following table shows the reconciliation of the EAA's internal ratings to external ratings.

INTERNAL EAA	EXTERNAL			
	Moody's	S&P	Fitch	
A0	Aaa	AAA	AAA	
A1	Aaa	AAA	AAA	
A2	Aa1	AA+	AA+	
A3	Aa2	AA	AA	
A4	Aa3	AA-	AA-	
A5	Aa3	AA-	AA-	
B1	A1	A+	A+	Investment grade
B2	A2	A	A	
B3	A3	A-	A-	
B4	Baa1	BBB+	BBB+	
B5	Baa2	BBB	BBB	
C1	Baa2	BBB	BBB	
C2	Baa3	BBB-	BBB-	
C3	Ba1	BB+	BB+	
C4	Ba2	BB	BB	
C5	Ba3	BB-	BB-	
D1	B1	B+	B+	Non-investment grade
D2	B2	B	B	
D3	B3	B-	B-	
D4	B3	B-	B-	
D5	Caa1 to C	CCC+ to C	CCC+ to C	
E	C	C	C	

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**Breakdown of notional volume by clusters<sup>1,2</sup>**

	<b>31/12/2020</b> in %	<b>31/12/2019</b> in %
Structured Securities	43.6	41.0
Public Finance & Financial Institutions	26.2	27.3
Real Assets	15.7	17.2
Structured Products	9.5	9.0
Corporates	4.5	5.1
Equity/Mezzanine	0.5	0.4
<b>Total</b>	<b>100.0</b>	<b>100.0</b>

<sup>1</sup> 31 December 2020 = EUR 12.7 billion; 31 December 2019 = EUR 14.9 billion.

<sup>2</sup> Excluding exchange rate effects (based on exchange rates as of 31 December 2011).

The EAA's banking book portfolio consists of six clusters. The largest cluster, Structured Securities, with a total share of 43.6%, consists of three sub-portfolios: Phoenix (59.8% – please refer to the section "Phoenix" for further details), ABS (31.3%) and Dritte EAA (8.9%).

**Breakdown of notional volume by maturities<sup>1,2</sup>**

	<b>31/12/2020</b> EUR billion	<b>31/12/2019</b> EUR billion
<= 6 M	0.2	0.5
> 6 M <= 1 Y	0.1	0.5
> 1 Y <= 5 Y	1.3	1.6
> 5 Y <= 10 Y	2.9	3.6
> 10 Y <= 20 Y	5.1	5.1
> 20 Y	3.1	3.6
<b>Total</b>	<b>12.7</b>	<b>14.9</b>

<sup>1</sup> For assets with no fixed or with very long maturities: expected repayment profile.

<sup>2</sup> Excluding exchange rate effects (based on exchange rates as of 31 December 2011).

The reduction in the maturity range of up to six months was mainly due to a repayment of the Phoenix A3 note (EUR 0.1 billion).

The other changes within the maturity ranges reflect the portfolio management measures undertaken and amortisation during fiscal year 2020.



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**Breakdown of notional volume by region<sup>1</sup>**

	<b>31/12/2020</b> EUR billion	<b>31/12/2019</b> EUR billion
Americas <sup>2</sup>	6.8	7.3
EMEA	4.6	6.0
Germany	1.1	1.4
APAC	0.2	0.2
<b>Total</b>	<b>12.7</b>	<b>14.9</b>

<sup>1</sup> Excluding exchange rate effects (based on exchange rates as of 31 December 2011). The regional breakdown by borrowers or for securitisations is based on the main risk country of the asset pool.

<sup>2</sup> Contains EUR 1.8 billion for the Phoenix B note guaranteed by the State of NRW.

The regional breakdown of the notional volume hardly changed compared with 31 December 2019. Approximately 53% of the notional volume was attributable to America (31 December 2019: 49%). Repayments were the main reason for a decline of EUR 0.5 billion in the Americas region, particularly in the Structured Securities cluster (largely Phoenix).

About 37% of the notional volume (31 December 2019: 40%) was attributable to the EMEA region.

The share of German borrowers and guarantors (share of portfolio: about 9%; 31 December 2019: 9%) is almost unchanged.

The APAC region represents around 1% (31 December 2019: 2%) and is also almost unchanged.

The EAA's banking book portfolio was backed by the following collateral:

**Breakdown of types of collateral of the banking book**

	<b>31/12/2020</b> EUR billion	<b>31/12/2019</b> EUR billion
Guarantees	2.4	2.9
Aircraft/Ships	0.0	0.1
Financial collateral	0.0	0.1
Real estate	0.0	0.0
Other collateral <sup>1</sup>	1.6	2.1
<b>Total</b>	<b>4.1</b>	<b>5.2</b>

<sup>1</sup> Including market values for Phoenix tranches.

**Problem loans and risk provision**

Problem loan exposures are subject to special risk monitoring pursuant to MaRisk. Loan exposures with notable risk profiles are subject to intensive monitoring. Loan exposures with increased risk profiles or which have already experienced actual defaults as well as non-performing loans are transferred to the Problem Loans Processing function.

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Problem loan exposures are recorded centrally in the EAA GW. It serves as a core basis for risk control and risk management of credit risks. The EAA GW is defined as an early warning system in accordance with MaRisk. It serves to record, monitor and report on individual loan exposures that have a notable or heightened risk profile, expected or actual defaults, or for which a specific risk provision has been recognised.

Exposures are included in the EAA GW in different categories based on defined risk indicators. The information and data recorded in the EAA GW are managed, monitored and regularly reported to facilitate tight control. The EAA GW also forms the basis for regular reporting to the EAA's governing bodies and to the FMSA on the current risk situation with regard to these loans and to the corresponding risk provisioning.

The recoverability of loans and advances is reviewed by ad hoc and regular performances of an impairment test (a test to determine whether a loan or advance is non-performing or at risk of non-performance, therefore resulting in a risk provisioning requirement). The assessment of a possible need for a risk provision takes into account collateral values, company valuations, discounted cash flow analysis or observable market prices. It is reviewed on a regular basis.

The EAA forms general loan loss provisions based on the expected one-year loss for the deferred credit risk in the portfolio of receivables and contingent assets. The computation is performed using individual company-specific loss rates and conversion factors as well as ratings, after taking into account the transfer-stop risk of the funding. This means that a separate model for country risk is not necessary. The general allowance for the derivatives of the banking book is calculated through the computation of the CVA of this sub-portfolio.

This method is also being maintained in view of the corona crisis.

Result of risk provisions

	Provisions for loan losses EUR million	Charge-offs EUR million	Net change in loan loss provision EUR million	Other exp./inc. due to risk EUR million	Total allow. losses EUR million
<b>Acute counterparty default risk</b>	<b>53.8</b>	<b>62.5</b>	<b>8.7</b>	<b>23.6</b>	<b>32.3</b>
Credit risk	53.8	62.5	8.7	25.1	33.8
Other risk	-	-	-	-1.5	-1.5
<b>Contingent counterparty default risk</b>	<b>3.2</b>	<b>-</b>	<b>-3.2</b>	<b>-</b>	<b>-3.2</b>
<b>Total</b>	<b>57.0</b>	<b>62.5</b>	<b>5.5</b>	<b>23.6</b>	<b>29.1</b>

Other risk expenditure/income primarily include recoveries from written-off receivables.

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**Special banking book issues**

**Phoenix**

The tranches of the Phoenix Light SF DAC securitisation constitute a major portion of the EAA's structured loan portfolio.

The majority of the securitised Phoenix portfolio is denominated in US dollars and represents US risks, primarily in the property market there.

**Phoenix notes capital structure**

Tranche	Amount as of 31/12/2020 in million		S&P rating	Legal maturity
Class A4	1,793.0	USD	B-	9/2/2091
	130.8	EUR	B-	9/2/2091
Class B	1,770.4	EUR	N.R.	9/2/2091

Repayments of EUR 0.2 billion and a guarantee drawdown of EUR 0.1 billion resulted in a decrease of the notional volume reported in euros in the reporting period to EUR 3.3 billion as of 31 December 2020 (at constant exchange rates as of 31 December 2011).

**Rating breakdown by internal rating category for Phoenix notes<sup>1</sup>**

	31/12/2020 EUR billion	31/12/2019 EUR billion
A0-A2	-	-
A3-A5	1.8	2.0
B1-B3	-	-
B4-B5	1.5	0.1
C1-C2	-	1.5
C3-C5	-	-
D1-D3	-	-
D4-E	-	-
S.R./N.R.	-	-
<b>Total</b>	<b>3.3</b>	<b>3.6</b>

<sup>1</sup> Excluding exchange rate effects (based on exchange rates as of 31 December 2011).

Note: The presentation by internal rating category considers the rating (A3) of the guarantor, the State of NRW, for the Phoenix B note.

All of the Phoenix notes have an investment grade rating (rating categories A0-C2), taking into account the rating of the State of NRW (the guarantor for the Phoenix B note). About EUR 3.2 billion of this guarantee had been utilised up to 31 December 2020.

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The rating distribution has changed compared to the beginning of the year due to a change in methodology. The classification is based on the quarterly valuation of the underlying assets. This led to a shift of Phoenix A notes from rating category C1-C2 to rating category B4-B5. The Phoenix B note is not affected by this because of the guarantee of the State of NRW.

In addition to the ongoing sale of parts of the portfolio by taking advantage of market opportunities, the EAA continues to work with the parties involved in Phoenix to optimise the portfolio. These measures include both legal measures in relation to individual portfolio securities and the restructuring of non-performing securities.

**Public Finance**

The exposure to the public sector (including the liquidity portfolio) as of 31 December 2020 totals a notional amount of EUR 3.2 billion (excluding exchange rate effects, based on exchange rates as of 31 December 2011). EUR 2.3 billion of this amount was attributable to the UK, Italy, Portugal and Spain. Further information can be found in the section "Exposures to selected EU member states and the UK".

Securities account for 81% of the total public-sector exposure (including regional and municipal borrowers). Lending transactions involving federal, municipal or other public-law institutions account for a share of 17%, with derivatives accounting for 2% of the portfolio.

The largest part of the overall exposure, at 82%, is attributable to borrowers or issuers from the eurozone, with the remaining volume coming from EMEA countries outside the eurozone (8%), America (8%) and APAC countries (2%).

**Credit risks – trading portfolio**

Trading portfolio credit risks are divided into counterparty risk (pre-settlement risk and settlement risk) from derivatives and issuer risk from securities.

Issuer risks from securities in the trading portfolio are calculated using market values, while those in the banking book are determined on the basis of carrying amounts. A distinction is drawn between collateralised and non-collateralised counterparties in order to determine the replacement risks (pre-settlement risks) from derivatives. The market value plus a regulatory premium is used as the replacement risk for non-collateralised counterparties. For collateralised counterparties, the market value, collateral and a premium based on VaR are calculated as the replacement risk. Settlement risks are determined using the payment due per value date. Credit risks from trading transactions are compared with the corresponding credit limits on a daily basis. Risk-mitigating measures, such as close-out netting (offsetting) and collateral in the OTC derivatives business, are used whenever possible. Active hedging of risk exposures takes place only with counterparties with whom corresponding master agreements are in place.

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OTC derivative counterparty default risks are assessed independently from the front office using CVA. When doing so, externally traded credit spreads, where available, are used to determine the probability of default. The expected loss can be calculated as CVA based on expected future exposures and a statistically determined recovery rate. The CVA in the trading portfolio amounted to EUR 3.8 million as of 31 December 2020 (31 December 2019: EUR 3.0 million). The EUR 0.8 million increase in CVA is attributable to changes in LGD and ratings (EUR +1.0 million) and market fluctuations (EUR -0.2 million).

**Counterparty and issuer risks**

**Direct counterparty risks**

As the EAA concludes OTC derivatives both from the trading portfolio as well as the banking book, and as counterparty risks are measured and controlled per counterparty, the explanations and figures below relate to both the trading portfolio and the banking book. In accordance with an established management process, risks are managed by the Treasury/Capital Markets department, a front-office function, and the Credit Risk Management and Risk Controlling departments, which are back-office functions.

The following table shows direct risks with active strategic counterparties. Direct risks are counterparty risks from those transactions which the EAA accounts for directly in its balance sheet and not those that have been transferred to it synthetically.

	<b>31/12/2020</b>	<b>31/12/2020</b>	<b>31/12/2019</b>	<b>31/12/2019</b>
	<b>Exposure</b>	<b>Limit</b>	<b>Exposure</b>	<b>Limit</b>
	<b>EUR million</b>	<b>EUR million</b>	<b>EUR million</b>	<b>EUR million</b>
Credit risk – money market positions <sup>1</sup>	199.9	4,151.5	1,549.8	5,183.5
Counterparty risk – OTC derivatives (pre-settlement risk)	348.1	2,310.0	372.2	2,358.0
Counterparty risk – repos	-	224.0	-	564.0

<sup>1</sup> All money market transactions with counterparties outside the EAA Group have a maximum maturity of up to six months.

Compared with year-end 2019, the changes in the credit risk for money market positions as of 31 December 2020 were driven primarily by active liquidity management for the purpose of reducing liquidity risks. Counterparty risks from OTC derivatives are driven by transactions for liquidity steering (foreign exchange swaps) and interest rate hedging instruments (interest rate swaps).

When evaluated by risk country, the country concentrations for money market positions, OTC derivatives and repos are as follows.

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Money market positions

Risk country	31/12/2020 Exposure EUR million	31/12/2020 Limit EUR million
Germany	199.9	1,825.0
France	-	835.0
Switzerland	-	500.0
Other countries	-	991.5
<b>Total</b>	<b>199.9</b>	<b>4,151.5</b>

OTC derivatives

Risk country	31/12/2020 Exposure EUR million	31/12/2020 Limit EUR million
UK	156.3	1,045.0
Germany	115.1	595.0
France	66.5	545.0
Other countries	10.2	125.0
<b>Total</b>	<b>348.1</b>	<b>2,310.0</b>

Repos

Risk country	31/12/2020 Exposure EUR million	31/12/2020 Limit EUR million
Germany	-	119.0
France	-	65.0
UK	-	40.0
<b>Total</b>	<b>-</b>	<b>224.0</b>

Issuer risks

Issuer risks are managed by the Treasury/Capital Markets department, a front-office function, and the Credit Risk Management and Risk Controlling departments, which are back-office functions.

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The following table shows the issuer risks of the banking book, broken down by sub-portfolios.

	<b>&lt; 1 Y</b>	<b>1-4 Y</b>	<b>4-8 Y</b>	<b>8-15 Y</b>	<b>&gt; 15 Y</b>	<b>Total exposure</b>
	<b>EUR million</b>	<b>EUR million</b>	<b>EUR million</b>	<b>EUR million</b>	<b>EUR million</b>	<b>EUR million</b>
Public Finance	140.9	375.2	829.6	1,055.5	578.5	2,979.7
Financial Institutions	-	-	18.0	-	-	18.0
Other securities	1.4	13.6	99.3	84.1	2,328.2	2,526.6
<b>Total 31/12/2020</b>	<b>142.3</b>	<b>388.8</b>	<b>946.9</b>	<b>1,139.6</b>	<b>2,906.7</b>	<b>5,524.3</b>
Total 31/12/2019	557.5	345.0	1,185.9	1,308.9	3,299.5	6,696.8

Other securities comprise mainly US student loans.

**Participation risks**

Participation risks result from the provision of subordinated capital and equity. Managing participations is mainly the responsibility of the participation management in the Legal & Compliance department. The Finance & Tax department supports the participation controlling process.

Of the total portfolio of the EAA Group, a notional volume of EUR 1.6 billion (12.4%) was held by subsidiaries, mainly consisting of Erste EAA Anstalt öffentlichen Rechts & Co. KG with EUR 1.1 billion (68.6%) and Dritte EAA Anstalt & Co. KG with EUR 0.5 billion (31.4%).

Erste EAA Anstalt öffentlichen Rechts & Co. KG holds a portfolio of US life insurance contracts through partnerships under US law. This company is fully funded by the EAA (EUR 1.1 billion).

Dritte EAA Anstalt & Co. KG holds a portfolio of structured securities. The EAA manages the transactions of Dritte EAA Anstalt & Co. KG as its general partner. As the securities continue to fall within the EAA's scope of risk management, on the basis of the look-through approach, the internal reporting has remained virtually unchanged.

EAA CBB was included in the risk management and business management of the EAA. The subsidiary is subject to monitoring by the EAA and the EAA's approved internal limit system. A representative of the EAA exercises non-managerial control functions as a member of the governing bodies and committees of EAA CBB. The EAA CBB is in an accelerated winding-up process. Following the transfer of assets to the EAA in the second half of 2020, EAA CBB essentially only reports one receivable from the EAA as an asset in addition to bank balances. The return of the full banking licence and the licence as a designated credit institution – comparable to a covered bond bank licence – which was applied for in October 2020, was approved in March 2021.

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In some situations, the EAA will enter into new participations via restructuring if such an approach is deemed beneficial to preserve the value of the assets (for example with debt-to-equity swaps).

**Exposures to selected EU member states and the UK**

The banking book exposure of the EAA and its subsidiaries to the UK, Ireland, Italy, Portugal, Spain and Cyprus of around EUR 3.2 billion as of 31 December 2020 is shown in the table below.

Country <sup>1</sup>	Debtor group	31/12/2020 Notional in EUR million <sup>2</sup>	31/12/2019 Notional in EUR million <sup>2</sup>
Greece	Corporates	-	0.0
<b>Greece</b>		<b>-</b>	<b>0.0</b>
UK	Corporates	406.2	510.9
	Public Finance	130.1	137.5
<b>UK</b>		<b>536.4</b>	<b>648.5</b>
Ireland	Corporates	12.5	15.2
	Financial Institutions	0.0	0.0
<b>Ireland</b>		<b>12.5</b>	<b>15.2</b>
Italy	Corporates	138.5	233.6
	Public Finance	1,457.5	1,476.6
<b>Italy</b>		<b>1,596.1</b>	<b>1,710.2</b>
Portugal	Financial Institutions	15.4	15.4
	Public Finance	502.9	709.1
<b>Portugal</b>		<b>518.2</b>	<b>724.4</b>
Spain	Corporates	273.9	383.1
	Public Finance	213.0	238.0
<b>Spain</b>		<b>486.9</b>	<b>621.1</b>
Cyprus	Corporates	45.0	49.1
<b>Cyprus</b>		<b>45.0</b>	<b>49.1</b>
<b>Total<sup>3</sup></b>		<b>3,195.0</b>	<b>3,768.5</b>
of which	Corporates	876.1	1,191.9
of which	Financial Institutions	15.4	15.4
of which	Public Finance	2,303.5	2,561.2

<sup>1</sup> Economic view; may differ from the borrower's legal country of residence (for Corporates and Financial Institutions).

<sup>2</sup> Based on current exchange rates. Presentation of the notional volume, including hedges (net).

<sup>3</sup> Of which EAA subsidiaries: EUR 291.8 million (31 December 2019: EUR 1,090.0 million).

This exposure has fallen by EUR 573.5 million from the beginning of 2020. The change was mainly attributable to Portugal (EUR -206.2 million), Spain (EUR -134.2 million), Italy (EUR -114.1 million) and the UK (EUR -112.1 million).



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The total trading portfolio and ALM exposure of the EAA and its subsidiaries to banks, companies and governments in the UK, Italy, Spain and Ireland is shown in the table below.

Product <sup>1</sup>	Value	Country <sup>2</sup>	31/12/2020 EUR million <sup>3</sup>	31/12/2019 EUR million <sup>3</sup>
Other derivatives and ALM	MtM	UK	183.2	222.8
		Italy	14.3	274.3
		Spain	5.6	5.9
<b>Other derivatives and ALM</b>			<b>203.1</b>	<b>503.0</b>
Other	Notional	UK	12.7	344.4
		Ireland	18.5	-
<b>Other<sup>4</sup></b>			<b>31.2</b>	<b>344.4</b>

<sup>1</sup> ALM = cluster ALM as part of the banking book is identified here as in the internal view and not as a banking book exposure; derivatives = replacement risks from OTC derivatives.

<sup>2</sup> Economic view; may differ from the borrower's legal country of residence (for Corporates and Financial Institutions).

<sup>3</sup> Based on current exchange rates. Presentation of the notional volume, including hedges (net).

<sup>4</sup> Includes mainly the HSBC nostro balances and the Central Bank of Ireland central bank balances.

During fiscal year 2020, the EAA analysed potential risks arising from the UK's withdrawal from the EU on 31 January 2020 (Brexit). Existing regulations from when the UK was an EU member continued to apply until the end of 2020. Thereafter, there was a risk that strategic counterparties for financial market transactions (derivative transactions in particular) for hedging market price risks will no longer be available. This could happen, for example, if counterparties previously domiciled in the UK which were operating in Germany via pass-porting would no longer be allowed to conclude transactions in Germany. In these cases, the EAA plans to transfer the business to counterparties domiciled in the EU, where it aims to transfer the business relationship as well as the existing legacy business to the new entity. The precondition was that the EAA's credit risks would not deteriorate as a result of the move, which is why existing counterparty guarantees were or are to be replicated in the same or at least equivalent form to the new EU entities. In order to reduce the transition risk for the EAA, it also started to convert business relationships affected by Brexit to their new EU entities, insofar as permitted by the progress of negotiations. This process was completed with half of the counterparties in 2020. In addition, the EAA had sufficient not utilised limits with counterparties domiciled in the EU to compensate for the loss of limits. The same applies to the trade repository selected by the EAA for reporting under EMIR and for the clearing broker for exchange-traded derivative business. The EAA sees no need for action at present as regards further business relationships (brokers, clearing, market data and outsourcing), as these business partners are either located outside of the UK or the EAA has confirmations for corresponding transfers to hand.

The EAA sees no need to take action on existing agreements, in particular loan and derivative agreements with customers and non-strategic counterparties.

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**Market price risks**

The EAA pursues a strategy of lowering market price risks to the greatest extent possible. Market price risk is controlled via a system of limits. Market price risks in the trading portfolio and the banking book are limited separately. Market price risk exposures are controlled on a daily basis by the Treasury/Capital Markets department and are monitored and analysed by the Risk Controlling department.

In terms of market price risks, the EAA distinguishes between interest rate risks, foreign exchange risks, equity risks, and credit spread risks:

- △ Interest rate risk describes the risk to the portfolio's net interest result or present value from changes in market interest rates.
- △ Foreign exchange risk describes the risk of losses from changes in exchange rates.
- △ Equity risk describes the risk of losses from changes in prices on the stock market.
- △ Credit spread risk describes the fluctuation in the value of securities resulting from a change in credit risk premiums (for example, on foreign government bonds in the Public Finance portfolio).

**Market price risks – banking book**

As a result of the portfolio structure, there are interest rate and foreign exchange risks (particularly in relation to the US dollar) that are largely hedged. In accordance with the risk profile, the EAA's hedging activities are mainly focused on the hedging of interest rate and foreign exchange risks.

These risks are hedged by refinancing with analogous currencies and matching maturities or by concluding derivatives transactions.

**Interest rate risk (EAA Group)**

	31/12/2020 EUR thousand	31/12/2019 EUR thousand
< 1 Y	-24.2	-16.5
1-4 Y	-16.1	-1.1
4-8 Y	83.9	60.3
8-15 Y	-16.6	-22.8
> 15 Y	-53.3	-52.6
<b>Total</b>	<b>-26.3</b>	<b>-32.7</b>

Interest rate risk in the banking book is measured as the change in the present value when the yield rises by one basis point (interest rate sensitivity PV01).

**MANAGEMENT REPORT**

The interest rate sensitivity PV01 was EUR -26.3 thousand (31 December 2019: EUR -32.7 thousand), due to management and maturity effects. The utilisation is within the limits.

**Foreign exchange risk (EAA Group)**

	<b>31/12/2020</b> EUR thousand	<b>31/12/2019</b> EUR thousand
AUD	1,257.4	852.4
CAD	884.3	718.7
CHF	91.1	240.4
GBP	679.1	1,049.2
JPY	1,131.9	578.3
PLN	667.3	27.7
SGD	461.7	469.6
USD	-3,234.9	7,675.3
Other	11.2	516.3
<b>Total</b>	<b>1,949.1</b>	<b>12,127.9</b>

Note: The presentation of the previous year's currencies has been restated.

The EAA's currency position is determined based on the principle of special cover in accordance with section 340h HGB. The positions in the various currencies are within the limits. They change as a result of market fluctuations and in the course of normal business operations.

The wind-up strategy aims to realise the intrinsic value of the exposure. The EAA does not take into account short-term capital market fluctuations and associated credit-spread changes when managing its exposures. The exposures are monitored and, if required, decisions are made to exit specific exposures. Therefore, no limits for credit spread risks are in place.

**Market price risks – trading portfolio**

The trading portfolio is exposed not only to interest rate and foreign exchange risks but also to a limited amount of credit spread risks. The trading portfolio predominantly includes derivatives as well as non-linear option risks. In line with market practice, risks in the trading portfolio are hedged at the portfolio level. This entails residual risks which change due to market movements and developments in the portfolio, and are hedged dynamically (dynamic hedging strategy).

The EAA applies both a VaR model and risk sensitivities to monitor and limit risks. A variety of stress scenarios is also used for risk management purposes. The VaR model calculates interest rate risks, equity risks and foreign exchange risks for the trading portfolio, including the respective volatility risks, on a daily basis. A confidence level of 99% and a one-day holding period are assumed when calculating the VaR.

**MANAGEMENT REPORT**

Historical and parametric stress tests are calculated on a daily basis. These also simulate the effects of market price risks not covered by the VaR, independently of statistically observed probabilities of occurrence.

The relevant market price risk exposures are continuously subjected to backtesting. This involves comparing the actual market value changes (hypothetical income statement) with the potential market value changes forecast by the VaR model on a daily basis. For the periods from the first quarter of 2020 to the fourth quarter of 2020, there were five backtesting breaches at the highest level of the portfolio structure of the trading portfolio. From a statistical perspective, two to three instances of exceeded limits must be expected per year for a VaR with a holding period of one trading day and a confidence level of 99%. The EAA believes that the backtesting process continues to confirm the VaR model. VaR plays only a minor role in EAA's management. Its effective risk management is based on risk sensitivities.

**Value at Risk by clusters**

	<b>31/12/2020</b> EUR thousand	<b>31/12/2019</b> EUR thousand
EAA Trading	647.6	669.8
Rates	647.6	595.8
Other	0.1	127.7

Note: The presentation of the previous year's clusters has been restated.

As of 31 December 2020, the VaR for the trading portfolio fell to EUR 647.6 thousand (31 December 2019: EUR 669.8 thousand) due to the winding up of the Muni GIC portfolio (Other cluster). The changes in the Rates cluster were due to market movements and hedging activities.

**Liquidity risks**

The EAA distinguishes between tactical and strategic liquidity risks.

△ Tactical liquidity risk is the risk of not being able to generate sufficient liquidity over the short term (time horizon of up to one year) to meet contractual payment obligations.

△ Strategic liquidity risk is the risk of not being able to implement funding measures set out in the funding plan on the market, in whole or in part.

The EAA's affiliates are included in the liquidity planning and management process so as to ensure optimal access to liquidity. Due to the duty of the liable stakeholders and the FMS to offset losses incurred, as well as because of their creditworthiness, the EAA is perceived positively in the capital markets. As a result, there is less risk concerning the EAA's specific funding options than there is with regard to systemic market illiquidity.

**MANAGEMENT REPORT**

In order to assess its liquidity, the EAA analyses in detail its funding position, liquidity reserve and funding needs. On the liabilities side, liquidity is assessed by type, volume and time horizon of the funding instruments. The EAA creates a monthly capital commitment balance by comparing the expected cash flows used for liabilities with those arising from assets, taking into account the use of derivatives. This provides information on its need for net funding. To this end, the EAA considers both tactical and long-term strategic liquidity. The tactical liquidity risk is regularly assessed using stress tests.

In order to manage and monitor its liquidity risks, the EAA has implemented a system to closely monitor the implementation of the funding plan. It also maintains a liquidity reserve. Securities with short terms and the best possible credit ratings may be purchased (subject to strict limits) in order to maintain the necessary volume of the liquidity reserve. A significant portion of the EAA's assets are invested in foreign currencies (particularly the US dollar) for longer terms. Foreign currency assets are refinanced using a mixture of foreign currency liabilities, which are issued via the Commercial Paper and Debt Issuance Programme, and using liabilities in euros in combination with long and medium-term cross-currency swaps and short-term foreign exchange swaps.

The limited stress scenarios ("liquidity crisis and downgrade", "liquidity crisis and downgrade USD") demonstrated a viable net liquidity situation as of 31 December 2020 (defined as the total of cumulated cash flows and the liquidity reserve). The liquidity reserve comprises highly liquid securities that are very likely to be eligible for repo transactions to generate new liquidity. The liquidity reserve was around EUR 2.3 billion when the stress test was performed.

Owing to the good ratings of its liable stakeholders and the FMS, the EAA does not consider it necessary to limit the strategic liquidity risk.

**Longevity risks**

The EAA funds premium payments for US life insurance policies, which are known as life settlement engagements. The payouts from these policies flow to the EAA when the insured individual dies. These policies are bundled in subsidiaries of Erste EAA Anstalt öffentlichen Rechts & Co. KG.

Longevity risk is the risk that insured individuals live longer than originally calculated. In this respect, the insurance premiums must be paid longer than forecast. Changes to the assessment of the expenses to be borne by the EAA from longevity risks are due to higher premiums demanded by the insurance companies. The EAA believes the increases are legally inadmissible. Several lawsuits are currently pending against insurance groups.

Longevity risk is limited to the acquired portfolio. Due to the large number of policies, coupled with a correspondingly high financing volume and long maturities, longevity risk is a major risk for the EAA.

**MANAGEMENT REPORT**

The actuaries and service providers engaged by the EAA provide monthly analyses on the life settlement exposure. Based on these analyses the EAA constantly monitors the relevant cash flows and thus the longevity risk so that deviations from the original forecast can be identified and taken into account in the valuation.

The EAA regularly monitors not only the present value of the expected cash flows (premiums, death benefits and service fees) from the policies but also the net present value of Erste EAA Anstalt öffentlichen Rechts & Co. KG. Besides the present value of the expected cash flows, this indicator takes into account the outstanding funding and cash on hand, making it possible to measure the performance over time of the entire life settlement portfolio.

**Operational risks**

The EAA differentiates between operational risks within the EAA Group (including its subsidiaries) and risks from the outsourcing of activities to service providers.

Operational risks in the EAA comprise all risks arising from inappropriate reactions or from the failure of internal processes, systems, and individuals, as well as risks resulting from external events.

Outsourcing risks in respect to the service providers encompass possible losses from procuring services from third-parties. These include, in particular, the risk that contractually agreed services are not provided or do not meet the stipulated quality.

Operational risks arise from errors made by employees or service providers in processing the business or through fraud. Alternatively, they may arise from the surrounding environment, such as cybercrime. The management of operational risks is therefore the direct responsibility of the individual departments under the leadership of the respective department heads. The EAA's Risk Controlling department monitors this effort.

**Operational risks within the EAA**

The EAA's management has established a sustainable risk management culture within the organisation in order to avoid operational risks. The EAA's Risk Controlling department is responsible for developing and introducing methods for identifying, measuring, analysing, monitoring and reporting on operational and other risks.

Operational risks are managed in the EAA and its subsidiaries using uniform methods and procedures. The operational risks of other service providers are managed using consistent methods. They are aggregated into an overview of overall risk.

Its activity focuses on the regular analysis and identification of weaknesses, and on ways to optimise all business procedures and processes. The EAA focuses on managing or mitigating material individual risks. To that end, it has established an internal system – depending on the type and scope of the operational risks – to record and measure the operational risks for the EAA as a whole. The recording of operational risk incidents and the annual risk inventory are key elements to measure operational risks. Based on the findings obtained, appropriate measures are decided upon and implemented.

**MANAGEMENT REPORT**

On the one hand, losses and near losses are recorded and evaluated, and potential or actual losses are quantified. In addition to documenting operational losses and near losses, an extensive ex-post analysis of operational risk incidents offers information on weaknesses and facilitates the initiation of risk-reducing measures on the basis of this information.

On the other hand, an annual risk inventory is performed to identify risks and assess their significance for the EAA. Appropriate risk-mitigating measures are decided upon and implemented based on the findings obtained. The Risk Controlling department gathers the information on the operational risk incidents and performs the risk inventory for the EAA. The processes at the service providers which are relevant to the EAA are also subjected to an annual risk inventory by the relevant Operational Risk Management department, which then reports the results to the EAA. If an operational risk incident occurs in these processes, it will also be reported to the EAA, including the associated risk-reducing measures and their status.

The EAA's last risk inventory from 2020 revealed five assessment objects with high risks in the availability of personnel category due to employee departures. This risk will be absorbed by using external employees if required. Of the assessment objects, 14% are medium risks and 84% low risk. The overall risk situation remains largely unchanged.

The aforementioned risk inventory of the EAA from 2020 was carried out together with the EFS and EAA CBB subsidiaries, and the key service providers IBM and MSPA. Owing to the outsourcing of key functions to IBM and the ongoing process of dismantling EFS, the risk situation at EFS continued to be assessed as low. IBM reported a slightly improved risk situation. The risk situation of MSPA remained largely unchanged. However, within the scope of this year's MSPA risk inventory, a high risk was reported in the category of staff motivation, due to the uncertain outcome of the ongoing tender of the EAA for the MSPA.

**Service provider management**

The outsourcing of key business processes requires that the EAA controls and monitors the operating infrastructure in order to ensure proper business operations. The monitoring requirements for the EAA are far-reaching and result from both the EAA's original task and its accountability to the liable stakeholders and the FMSA as well as from supervisory and statutory requirements in terms of transparency, correctness and the adequacy of control systems.

The EAA is also subject to the legal and supervisory regulations pursuant to section 25a KWG and applies MaRisk AT 9 (outsourcing) and AT 4.3.1 note 2, which require the management and monitoring of outsourced activities.

**MANAGEMENT REPORT**

As a result, an adequate monitoring system is a key success factor for the EAA. The EAA has selected a needs-based approach to structure its service provider management in order to create a structure that fulfils the requirements, reflects its business model, meets its supervisory and reporting obligations, and minimises the operational risks associated with outsourcing. The selected approach is also innovative because it brings together the unusually broad coverage of highly different services and assessment criteria using a simple analysis matrix. The EAA's concept combines a flexible technical solution with a holistic, integrated, multidimensional and pragmatic management approach that focuses on business processes and the end product.

The EAA has established a service provider management to monitor the interface between the subsidiaries and other service providers and the EAA, as the recipient of services, in terms of the content, form and quality of the services. Using a continuous and timely monitoring process, the EAA accordingly ensures that its requirements, which are defined in service level agreements, are fulfilled by the service providers in the agreed form. In this process, the EAA records the outsourcing risks and assesses them by applying a traffic light system. The monitoring and assessment process is supported by an online assessment system. Any necessary service and process adjustments are additionally taken into account in a process of continuous improvements.

The EAA has agreed protective measures for data and IT security, including the data centres, with its service providers. These measures are continuously reviewed and adjusted if necessary.

There were no elevated risks during fiscal year 2020, and the quality of the services rendered during the period was fundamentally stable in accordance with the service agreement.

**Other risks**

**Reputational risks**

Reputational risks express the risk that public reporting on the EAA or the transactions in which it engages will result in damage to its reputation.

Given the public interest in the EAA, reputational risks are especially relevant. The EAA also attaches special importance to its public image, since it impacts its funding options on the capital market.

The EAA has established behavioural rules for its employees in its "Code of Conduct". The EAA monitors all public media coverage intensely to further minimise reputational risks. This also includes public media coverage about its subsidiaries in the wind-up portfolio. Coordinated and active communication and public relations activities support the EAA's reputation.



**MANAGEMENT REPORT**

**Legal risks**

Legal risks comprise risks arising from contractual agreements or statutory conditions which harbour the risk of negative effects within and outside the EAA.

The EAA is subject to legal supervision by the FMSA, which, in turn, is subject to legal and technical supervision by the German Ministry of Finance. The FMSA ensures in particular that the EAA complies with the requirements of statutory provisions and its charter.

Since April 2010 the authorities in the US and in the EU (particularly BaFin) had been investigating possible misconduct in the trading departments of several banks. In connection with the quotations of reference interest rates, the results of the investigation have not produced any evidence of wrongdoing at the former WestLB; the investigations by BaFin and the US supervisory authorities were terminated without any measures being undertaken against Portigon. In addition, Portigon, together with a large number of banks active in the US, was sued in this context in various class action lawsuits in the US for alleged manipulative actions with regard to reference interest rates. Certain aspects of these class actions were repeatedly rejected in the court of first instance also with respect to Portigon. Some plaintiffs launched an appeal against this, which led in part to a referral back to the court of first instance and in part to an uncertain outcome as things currently stand. It is currently impossible to predict when an appeal decision will be issued and whether it will confirm the previous first-instance decisions. The court of first instance has yet to make a final ruling. However, Portigon remains convinced that, in line with the results of the investigations by the supervisory authorities, it cannot be accused of misconduct. The EAA has no reason to doubt Portigon's claims.

In connection with dividend arbitrage transactions in the years 2005 to 2008, Portigon paid capital gains tax and interest to the competent tax authorities which may have been unjustifiably credited, but appealed against the corresponding recovery orders. Portigon has also written to the EAA requesting reimbursement of or release from these expenses, and has filed a corresponding action against the EAA with the Frankfurt am Main Regional Court for the assessment periods 2005 to 2011, as it believes that, on the basis of the transfer agreements concluded in 2012 by the liable stakeholders within the scope of the refill, the EAA would assume the risk in this respect. Following a detailed assessment of the asserted claim, the EAA considers this claim to be unfounded on the basis of the information available to it and with the assistance of external legal advisors. In its statement of defence, the EAA requested that the action be dismissed and, in line with the legal opinion of its legal advisors, did not create any provisions in the matter. It will continue to defend itself against a claim by Portigon.

When necessary, the EAA has established sufficient financial reserves and initiated other measures to cover judicial and extra-judicial disputes.

**MANAGEMENT REPORT**

**Tax risks**

Tax risks may arise from changes in tax legislation, case law or errors in the application of the law as well as the special tax regulations for winding-up agencies.

The EAA uses clearly defined governance structures and processes to analyse and manage tax risks. Tax risks are clarified through active communication with tax authorities and other government institutions. Where necessary, external specialists are engaged to consult on legal and tax issues.

**Summary of the risk situation**

The EAA was established to assume the risk exposures and non-strategic business units of the former WestLB and its domestic and foreign subsidiaries, and to wind these up in a value-preserving and risk-minimising manner, pursuant to a winding-up plan. Value fluctuations in the interim are of less significance.

For that purpose, in particular, winding-up agencies in accordance with section 8a StFG are exempt from capital requirements, the obligation to prepare consolidated financial statements and other statutory provisions that apply to commercial banks.

The EAA strives in its risk management activities to reduce the risks resulting from the winding-up of the portfolio. To that end, the wind-up success and any deviations from the winding-up plan are continually monitored and compared against the plan (please refer to the section "Wind-up report").

Due to its good rating, the EAA has a stable funding situation. The stress scenarios demonstrated reasonable net liquidity as of 31 December 2020.

Market price risks are largely limited.

The EAA has a tight service provider management system and an internal control system in order to manage operational risks.

Longevity risk is the risk that insured individuals live longer than originally calculated or the insurance companies increase the premiums. They are limited to the acquired portfolio. The longevity risks in the portfolio are regularly analysed.

Risks resulting from the sovereign debt crisis, particularly for exposures in periphery euro-zone countries, and equally the risks resulting from the corona crisis, are being monitored closely and in a timely fashion.

The EAA has made sufficient provision for all known risks. Its equity – before the equity instruments and the loss-offset obligation – is initially available as aggregate risk cover for risks that are not yet foreseeable at present.

**MANAGEMENT REPORT**

The requirements for risk-bearing capacity pursuant to section AT 4.1 MaRisk are not relevant for the EAA. Instead, the EAA performs a quarterly analysis of the changes in its equity to the end of the planning period using the winding-up plan as well as updated variables and market parameters. This involves, in particular, analysing the effects of changed framework conditions on equity in fiscal year 2027. The winding-up plan shows positive equity capital as of the end of the planning period. This means that the only possibility of a loss occurring that would require the EAA's liability mechanism to be utilised in the period to the end of the planning horizon for the winding-up plan would be if adverse scenarios were to materialise which, from today's perspective, are unlikely to occur.

In summary, the EAA perceives the risks it has assumed to be adequately covered, given its capital resources as well as the existing guarantee, equity instruments and loss-offset obligations of the liable stakeholders and the FMS.

The EAA will continue to place a special focus on sustainable and consistent risk management.

### Opportunities report

Economic growth in the eurozone is currently being restricted by the corona pandemic. The containment measures have slowed growth on both the demand side (lack of consumption and less private investment) and the supply side.

2021 and 2022 should mark the start of the economic recovery for all eurozone countries. This will be facilitated by aid from the ECB and the EU. The ECB has remained true to its "whatever-it-takes" approach and has created various instruments to support euro member states and their banks and companies (government bond purchases under its pandemic emergency purchase programme, targeted long-term pandemic loans and rebates on negative interest rates).

The ECB's monetary policy will therefore support the valuations of euro government bonds in 2021 and 2022. With its current purchase programmes for euro government bonds and other purchases, it will continue to have a positive influence on valuations, which should limit price and spread volatility. The combination of very loose monetary policy and robust economic growth, and the EU's reconstruction assistance, will allow the eurozone states and the companies and project financing based there to service their debt at much better terms. The process will not be limited to listed products only; it will also affect other segments of the euro credit market such as promissory note loans, traditional loans and project financing.

Besides exposures to the euro periphery, the EAA also has significant commitments in the US. The corona crisis had no negative impact on US property prices; only the rise in prices slowed somewhat in the spring. As of November 2020, property prices are again increasing at a rate of 9.1% per year and are nearly 10% above the last peak of July 2006. This was already taken into account in the valuation of the exposures, so the positive effect of the continued economic recovery in the US should be limited.

**MANAGEMENT REPORT**

The EAA anticipates these developments will have a beneficial effect on the portfolio (see also the "Forecast report" section).

## Forecast report

Active measures and contractual maturities are expected to reduce the notional volume of the banking book by around 10% compared with the previous year to less than EUR 12 billion in fiscal year 2021.

The EAA's objective is to have wound up around 93% of the banking book as of 31 December 2011 (including the exposures held by subsidiaries and the exposures from the refill) by the end of 2022. As in previous years, the winding-up activities will focus on advance portfolio-reducing measures and active participation management.

For fiscal year 2021, the notional volume of the trading portfolio is expected to decline significantly by more than 20% compared with the previous year, to a mid-double-digit billion value. Since the transfer in 2012, the EAA has continued to target a reduction in the notional volume of around 95% by the end of 2022. The EAA will continue to analyse how the trading portfolios can be effectively and cost efficiently reduced at an accelerated pace.

With regard to the change in notional volumes in the banking book and the trading portfolio, in the previous year the EAA anticipated that these would be reduced to EUR 13 billion in the banking book and below EUR 100 billion in the trading portfolio in fiscal year 2020. Thanks to active measures in particular, this forecast was surpassed by a substantial margin.

The EAA expects to generate a total of EUR -9 million (including dividend income) from the net interest result, net fee and commission result, and the results from financial assets and shareholdings for 2021, which is therefore below the previous year's level. This is due to the accelerated reduction in the portfolio. A forecast for the net trading and risk provision result is difficult due to the imponderables with respect to developments on the global financial markets and other markets. The EAA is sticking with its strategy of winding up in a value-preserving manner. Losses cannot be ruled out in the next few fiscal years either because of the now substantial reduction of the portfolio and the associated decline in income from ongoing operations. This possibility is taken into account in the EAA's winding-up planning.

In the previous year, the EAA anticipated that its net interest result, net fee and commission result and the results from financial assets and shareholdings would decline slightly in fiscal year 2020. A clearly positive one-off effect (from the profit transfer of a subsidiary), led to the forecast being clearly exceeded and an increase achieved. The increase over the previous year was EUR 15 million and therefore exceeded forecasts. No forecast for the net trading and risk provision result was made the year before due to the imponderables with respect to developments on the global financial markets and other markets.

**MANAGEMENT REPORT**

Further forecasts regarding earnings in the next few fiscal years on the basis of the indicators described are subject to uncertainty and are reliable only to a limited extent. Based on its winding-up planning, however, the EAA does not currently foresee the need to utilise the equity capital drawing limit or the assumed loss-offset obligations.

The EAA fundamentally pursues an opportunistic approach by conducting regular analyses of market conditions and exit opportunities in order to assess early and profitable wind-up opportunities for the portfolio. To this end, an agreement was reached for example at the end of 2019 to reduce substantial portions of the derivatives portfolio, which has been implemented since then in several steps.

The recession triggered by the corona crisis has only triggered temporary increases in the risk premiums so far. The ECB's euro government bond buying programme and the new pandemic programme have impacted positively on the EAA's portfolios. The ECB measures and the EU's reconstruction aid of EUR 1,850 billion appear to be reassuring market participants. Further easing by the ECB in the form of a boost to the pandemic programme or of relief for banks suffering from the costs of negative interest rates are not ruled out. The ECB will therefore continue to exert a significant influence on the market performance of euro government bonds in the years ahead. Because of the low interest rate environment, investors' will remain hungry for yield, which should support the EAA's sales activities and encourage investors to redeem holdings ahead of schedule.

Even if the various measures taken by central banks and governments are helping, one cannot turn a blind eye to the fact that the sharp economic downturn will cause the number of corporate insolvencies to rise. A study by Euler Hermes dated 16 July 2020 expects a 35% increase in insolvencies worldwide by the end of 2021. In Europe, the authors expect insolvencies to peak in 2021. Only then should the situation improve again. The EAA is very aware of this threat. Exposures that could be negatively affected by the crisis and recession are closely monitored.

The tasks of the EAA include securing the acquired expertise for the ongoing successful winding-up activities. However, in parallel with winding up the portfolio, the EAA must also reduce costs and save on staff. It is a challenge for the management to deal with these conflicting priorities while retaining specialists for the work that remains. The EAA will optimise its structures on an ongoing basis in the coming years.

## Accounting-based internal control and risk management system

The objective of an accounting-based internal control and risk management system (ICS/RMS) is to ensure compliance with financial reporting standards and regulations and to guarantee the integrity of the financial reporting.

Within the framework of the service agreements concluded, the EAA, the MSPA and EFS (together with IBM since December 2017) have implemented an ICS and an RMS that are appropriate for the financial reporting processes and business activities of the EAA. The accounting-related ICS/RMS consists primarily of guidelines and processes which offer reasonable assurance that business transactions are fully, promptly and accurately measured and recorded on an accrual basis in accordance with statutory and other provisions so that

- △ public financial reporting provides a true and fair view of the EAA's financial standing (integrity and reliability of financial reporting);
- △ decision-makers and governing bodies are regularly and promptly informed of financial reporting data relevant to the management of the institution (internal reporting);
- △ appropriate control procedures are in place so that unauthorised purchases, use or sales of assets having a material impact on the financial reporting can be prevented or identified early on;
- △ an appropriate control and documentation environment is created (such as the segregation of functions, compliance with established approval or authority levels, dual control principle when recording business transactions, orderly documentation); and
- △ the archiving and storage of documents and accounting-relevant data is regulated concerning information that provides accurate, sufficiently detailed and appropriate data on business transactions and the use of assets.

The EAA monitors the entire accounting-based ICS/RMS on an ongoing basis. Existing professional and technical controls are examined regularly by the Internal Audit department of the EAA (with the support of its external service provider) and the auditor of the EAA as well as, in cases pertaining to outsourcing to EFS, the MSPA and IBM, by their Internal Audit departments and their auditors.

The EAA's Internal Audit department also monitors audit activities at IBM and the MSPA for effectiveness and appropriateness, and can also perform audits there.

**MANAGEMENT REPORT**

Moreover, the financial reporting processes are included in EAA's general risk management process with regard to operational risks. This is intended to prevent errors or misstatements to the greatest extent possible, or to uncover them early on. All processes are documented in the EAA's written rules of procedure, which are available to all employees.

The accounting policies are documented in electronic manuals. Annual, quarterly and monthly financial statements are prepared in accordance with a coordinated schedule.

New statutory and supervisory requirements are implemented and communicated promptly, depending on their respective scope and significance to the EAA. This is carried out in projects and via written instructions. All relevant business units and management levels are involved in accordance with internal project guidelines.

Employees of the Finance & Tax department participate in the meetings of the relevant risk and management committees. This participation helps ensure that strategic and risk-related developments are included promptly in the financial accounting and reporting. Transactions with new products or in new markets, which the EAA may carry out only within the scope of the portfolio wind-up and not to operate new businesses, are handled through the new product process intended for that purpose, in which the Finance & Tax department is also integrated.