DEPARTURE WITH A CAPITAL D

Capital Bank Group

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Annual Report 2019

LET'S TAKE OFF INTO THE FUTURE TOGETHER

Capital Bank 2019

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GRAWE Bankengruppe

It is 2020 and the world is now saying goodbye to reality as we knew it. With our masks on, we are looking a reality in the face that – unlike ourselves – is completely unmasked. We are left confronted with our own vulnerabilities and the fragility of a system that we all relied upon so much. Whatever the consequences are for us, one thing is quite clear: these events get under our skin. The catchword “skin” makes us think especially at this time of the prominent scientist, author and satisfied customer of Capital Bank, Nassim Nicholas Taleb. In his work Skin in the Game: Hidden Asymmetries in Daily Life he writes about the fact that there would be no life without risk. Taleb himself has a professional background as a trader and hedge fund manager, and is very familiar with the risks associated with these roles. Risk, as Taleb understands it, is characterised by a willingness to expose oneself to reality, directly and in such a way that you risk your own skin. We can only overcome false premises if we are willing to pay a price for our actions. This is a concept which Capital Bank already committed itself to years ago in a figurative sense when we turned the system of investment banking on its head. We are currently all in the same boat as our customers.

How we get this boat sailing again could perhaps be inspired by Christian Ortner’s guest article in this annual report, which is devoted to the deeper causes of the economic crisis in times of the coronavirus and attempts to outline some potential solutions.

CHRISTIAN JAUK

CEO

The concept of “responsibility” has rarely been as highly valued as it is these days during the Covid-19 crisis. Responsibility in our daily dealings with each other, and responsibility in business. Responsible management of our customers’ assets has always been a central concern of ours at Capital Bank. Our customers are very right to demand this now from us and fortunately they appreciate the steps we are taking to achieve this goal.

CONSTANTIN VEYDER-MALBERG

MEMBER OF THE MANAGEMENT BOARD

It has been weeks since things were “completely normal”. Fortunately, at Capital Bank things were never completely normal, and our innovations are now making what we have always intended them to make: the subtle difference. Seeing the bigger picture, having a clear and transparent remuneration model and a fair and honest payment system are just some of the main ideas that we have to guide you and us safely through the coronavirus era.

WOLFGANG DORNER

MEMBER OF THE MANAGEMENT BOARD

When reliability and the courage to do something new are positively intertwined, a new quality emerges. This is what it takes to change things. When you ask yourself at the right time “What if...”, you are much more likely to have thought ahead in times when things are not going as they usually do. That is exactly what we do in order to minimise our customers’ concerns: we think ahead and seek out preventive solutions – so that we can shape the future.

CONTENTS

Foreword 5

The problem is the bubble, not the pin 7

Capital Bank – GRAWE Gruppe AG

Performance and Key Figures 29
Management Report 30
Risk Report 54
Report by the Supervisory Board 82
Statement of Financial Position 83
Income Statement 87
Capital base 90
Statement of Changes in Equity 91
Notes 96
Company boards 134
Audit Certificate 136
Consolidated Statement of Financial Position 152

Imprint 158

FOREWORD

If you were to glance at the first sentence of last year's foreword, you could be forgiven for thinking that it had been written for 2020. The sentence went as follows: "Anyone who's been through tough times knows that when everything is running smoothly we can be lulled into a misguided sense of security." The coronavirus crisis has shown us in no uncertain terms just how true that is. In his writings, Nassim Nicholas Taleb, one of the most unconventional and provocative thinkers of our time and author of bestsellers like The Black Swan and Skin in the Game: Hidden Asymmetries in Daily Life – plus, incidentally, a longstanding client of Capital Bank – has made the point repeatedly that, even during period of success and constant, uninterrupted progress, we should also expect precisely that which we are not (keen on) expecting. This is the only way we can take preventive measures to shore up the weaknesses in our system and combat the fragility of our world.

The author of our guest essay, Christian Ortner, takes a similar angle when he writes that "the virus itself and the pandemic that it has triggered are not the cause of the resulting global economic crisis. Rather, they merely did exactly what other, completely different events would have done sooner or later: brought about the partial collapse of an economic architecture that, for various reasons, was roughly as stable as [a] house of cards after

you have removed the supports." His essay, entitled The problem is the bubble, not the pin, attempts to unlock the deeper causes of the economic crisis associated with Covid-19.

We hope you enjoy reading it.

THE PROBLEM IS THE BUBBLE, NOT THE PIN

By Christian Ortner

Part one: the virus and the house of cards

Anyone looking to understand what happened to most of the world's economies in spring 2020 in the wake of the "coronavirus crisis" and, perhaps more importantly, what else is highly likely to happen sooner or later essentially only needs a pack of standard playing cards, an hour to spare and passably sharp observation skills – and the courage to draw the right conclusions.

So let's take our playing cards and begin carefully to build a little tower. It's not difficult – after all, every child has had a go at some point. You take a pair of cards and lean them against each other in an upside-down "V", do the same again with a second pair, and lay another card on top, joining your pairs like a sort of flat roof. More of these simple five-card modules can then be added next to and on top of one another horizontally as well as vertically. With a bit of skill, nimble fingers and a sufficient appetite for risk, you can use this method to build houses of cards up to quite an impressive height.

Now this is where the exciting bit starts that children love so much. Carefully, ever so carefully, let's start to remove individual cards from our structure by plucking them out tentatively with our finger and

thumb, really slowly and concentrating hard. The house stays standing, for now. And now let's take out another card. And another. And the house is still standing. One more – it's a miracle of structural engineering

and a fascinating process. Ultimately, though, our instinct tells us how the whole thing usually ends. At some point, our house of cards will collapse.

Usually, this collapse is triggered by a tiny external impact that has nothing directly to do with how the house was built. A breeze from a window, an adult's plodding steps on the parquet floor, a car driving past outside – tiny vibrations that the now much-too-fragile structure is no longer able to withstand and that cause it to come falling down all around us.

Of course, nobody would ever think of holding the passing car responsible for the collapse of our intricate construction. Anyone with even a bit of common sense will know that the structure itself was the underlying problem, that the car outside merely lit the touchpaper, and that any one of hundreds of other random events would inevitably have led sooner or later to exactly the same implosion.

Even though the public and published opinion would tend to disagree, there is much to suggest that the "coronavirus crash" of 2020 is following a very similar pattern. And the virus itself and the pandemic that it has triggered are not the cause of the

resulting global economic crisis. Rather, they merely did exactly what other, completely different events would have done sooner or later: brought about the partial collapse of an economic architecture that, for various reasons, was roughly as stable as our house of cards after you have removed the supports.

Looked at this way, the crisis was not caused by the virus itself. Instead, it was down to the misguided policies and behaviour of key actors from the worlds of politics, economics and finance – but also of many consumers and voters – that had been going on for years if not decades.

They had all combined to blow up a balloon that was going to have to burst sooner or later. US economist Peter Schiff put it succinctly when he wrote: "The problem is the bubble, not the pin [...] If the US economy really were healthy, it could shake off a case of coronavirus. But because the Fed [the US central bank] has artificially stimulated so much during past recessions, I believe the economy is particularly vulnerable. By cutting past recessions short, the Fed prevented the resolution of the imbalances that caused those recessions in the first place. Instead, it made debt bubbles larger, so we will enter our next recession with unprecedented levels of debt. In such a vulnerable position, the slightest downturn might be catastrophic. Any interruption in corporate earnings or weekly paychecks might lead to unprecedented debt defaults, and a worse financial crisis than 2008. So, the Fed will be doing all it can to once

again delay the day of reckoning by making all the problems we need to reckon with larger."

Of course, something very similar applies to most other parts of the world too. Overindebtedness has become globalised, just like virtually every sector of the economy.

And the metaphor of the tower of debt that is bound to collapse at some point is not the brainchild of obscurantist conspiracy theorists or prophets of monetary doom: the image has even been used exhaustively by the respected German financial economist Isabel Schnabel, a member of the Executive Board of the European Central Bank (ECB), no less. Long before the coronavirus crisis struck, in fact, she had openly admitted that "low interest rates are essential to prevent the towers of debt from collapsing". The good lady is likely to know only too well what she is talking about.

To a greater or lesser extent, the situation applies to nearly all the world's economies and central banks. Coronavirus was not the cause of the exceptional problems now facing every one of us. Rather, it just brought many of them into rather sharp relief. It's only when the water level falls that you can tell who's been skinny-dipping.

This brief essay is intended as an attempt to uncover the real, deeper causes of the crisis and touch on what conclusions we will need to draw from what

has happened so far. (Spoiler alert: these conclusions may seem rather unpleasant to many people, but it remains the case – now more than ever before – that "there ain't no such thing as a free lunch").

Part two: two hundred and fifty trillion dollars

How much money is 250 trillion dollars anyway? Now, one measly trillion is a mere million million (1,000,000,000,000).

If you're struggling to get your head round all these zeroes, you're not alone, because even just the sheer scale of our economic problems at present and the "rescue packages" being launched against them are well beyond the realm of human comprehension.

250 trillion dollars – according to informed estimates, this is likely to be the current total global debt of all countries, companies and private individuals on the planet. And this is without even counting the hefty new debts that governments, in particular, have now piled on themselves in the wake of the pandemic. "The IMF's Fiscal Monitor has put the global costs of the additional health interventions and rescue measures necessitated by the pandemic at $3.3 trillion. This is in addition to public-sector bonds and injections of capital for companies ($1.8 trillion) plus guarantees and other contingent liabilities ($2.7 trillion). Public-sector debt is skyrocketing all over the world." (Neue Zürcher Zeitung, 20 April 2020)

This staggering amount is concerning mainly because it has grown at a much faster pace than global economic output over the past two decades: a debt bubble of unprecedented proportions has been inflated with great determination by piling new loans on top of old ones to prevent the individual players in this game from ever defaulting on their payments, if necessary also with money printed (or, as some printers would say, "counterfeited") by central banks for this very purpose.

And all this despite the fact that, as we all know, a major global financial crisis – essentially a debt crisis – erupted in 2007/2008: from the excessive US mortgages handed out to uncreditworthy borrowers to the overindebted countries of Europe's "Club Med", headed by Greece.

However, although history is known to be a great teacher, unfortunately nobody tends to take any notice. Almost as if the global financial crisis of 2008 and after had never happened, therefore, the world largely carried on unperturbed, cheerfully nurturing its burgeoning debt mountains. More than six months before the coronavirus crisis, the German journalist and commentator Gabor Steingart wrote: "The world is living a double life. By day, 'sustainability' is the word on every politician's and citizen's lips. By night, however, the bulwarks of economic sustainability are being deliberately dismantled. Out of fear of an economic slowdown. Out of concern for the possibility of a trade war. Out of a reluctance

to countenance any change to the status quo. Across the world, we are seeing a return to the politics of debt and cheap money, without any parliamentary debates ever being held on the matter."

And he would go on to predict: "A glut of money of a size never before seen is in the works. China, Japan, the USA, major developing countries and ECB President Mario Draghi and his team have become slaves to the greed of the moment. The peoples of the world, all lovers of the status quo – at least in the eyes of the political class – are to be anaesthetised.

Cheap money, not religion as Karl Marx believed, is the modern opium of the people. The world is now living out its double life in a hall of hallucinations. There could be many consequences – but sustainability can never be one of them." How right he was is something we will soon have to find out; the signs are not good.

The few isolated pockets of lingering resistance to this collective folly, such as Germany with its "black zero" policy (until April 2020), or Sweden, which had cut its national debt to a mere 30% of GDP by the time the coronavirus crisis hit, were regularly denounced by mainstream economists and political commentators as economic party-poopers whose policy of "saving till it hurts" would ruin the economy – an argument that, interestingly, seems more or less to have gone to ground since the coronavirus outbreak and the huge burden it has placed

on governments. Even as recently as 2019, however, the infamous Economics Nobel Prize winner Paul Krugman wrote in the New York Times that "[t]he world has a Germany problem", alleging that the German government had an "obsession" with debt that was slowly but surely jeopardising the global economy and accusing the country in all seriousness of "society-destroying spending cuts".

These days, Germany – and with it half of Europe – is happy that, thanks to its measured budgetary policy up until now, Berlin is able without major problems to prevent its own economy and thus ultimately those of its fellow EU members from collapsing, by taking on serious levels of new debt, even though this only means kicking the problems further down the road rather than solving them once and for all, of course.

In April 2020, when this essay was written, Germany and a handful of other eurozone countries, including Austria, were still mounting lingering resistance to the introduction of "eurobonds", i.e. the mutualisation of debt amongst members of the monetary union. Vocal supporters of the idea are chiefly Italy, which to all intents and purposes is already overindebted, but also Spain and France, because it would make Germany and the few other healthyish eurozone members jointly and severally liable guarantors alongside the principal debtor countries. As it happens, this is precisely something that the treaty establishing the eurozone had ruled out. As everyone

knows, however, needs must: an emergency can turn any breach of the law into a minor misdemeanour. It is not unduly reckless to predict that these eurobonds will come about sooner or later, whatever they end up being called. This is because, of course, Italy in particular is "too big to fail" in a way and will therefore (have to) be subsidised by its peers to the north.

And the Italians are being extremely creative when it comes to obtaining this solidarity. At the height of the coronavirus crisis, for instance, two dozen high-profile Italian politicians, including the mayors of Milan and Venice, called on the Germans to finally give eurobonds the green light, arguing that Germany had had some of its own debt cancelled in 1953(!) and that the new mutual debt was an essential weapon to combat the coronavirus.

They have some nerve. After all, Italy is not currently scarred by the consequences of the Second World War, like Germany was in 1953, but instead has lived through a substantial 75 years since the war ended – years that, however, the country failed to use to put itself in a position to survive without taking on any new debt, at least under normal circumstances.

Here too, the fact remains that, rather than being the cause of the crisis, the coronavirus has merely thrown it suddenly into sharp relief. Italy is virtually a textbook example.

German economist Hans-Werner Sinn sees bad times ahead if Italy has its way and "eurobonds", or "coronabonds", or whatever they may be disguised as do see the light of day: "They will destroy the European capital market because they will break the interest rate mechanism. And they will undermine Germany's creditworthiness, sacrificing our interest rate advantage over the USA. The narrowing transatlantic spreads are already showing this quite clearly. In the long term, they will inevitably lead to an avalanche of debt, which will leave nothing behind bar antagonism and hatred, just like when Alexander Hamilton mutualised debt in the USA. The wave of mass bankruptcies that hit individual states in the years after 1835 were the direct consequence of a policy of socialising debt that he started."

In some way, though, Italy is everywhere. One of the phenomena that the coronavirus has revealed all of a sudden is just how little financial resilience many private households, but also many companies, appear to possess. Surprisingly few of them have set aside the kind of adequate rainy-day fund that they could now really do with, either because they weren't able to, or because they didn't feel it was necessary and preferred to spend instead.

For instance, 60% of people in the USA wouldn't manage to cobble together 1,000 dollars from their savings if they had to make a sudden, unplanned payment, while 80% of industrial workers are living "from paycheck to paycheck", i.e. virtually from

one month to the next without any wriggle room. "Coronavirus reveals financial irresponsibility of Americans" says the title of The Hill magazine, hitting the nail bang on the head.

In Austria, too, it has become apparent that a great many sole traders and smaller businesses sail very close to the financial wind even in normal climes; if a crisis like the current one hits and sales plummet, often to zero, many risk defaulting on their debts after just one month, with only a small minority having reserves that can help to plug the gap for a few months. Die Presse had this to say on the subject on 5 April 2020: "It's clear we're going to have to talk about the level of capital resources and liquidity at Austria's small and medium-sized businesses. According to a survey by the SME researchers at "KMU Forschung Austria" a few days ago, 53% of SMEs only have enough liquid funds to cover their costs (staff costs, rent, loan payments, interest, energy bills, etc.) for a few weeks or a month at most if they don't get any extra help. This would be next week, then. We have a serious economic problem on our hands, at any rate. Not good."

It is patently clear that we are living in an economic environment that is much more precarious than previously assumed. The coronavirus did not cause this; it merely lifted the lid on it.

Part three: the firefighters turned arsonists

In her famous novel Atlas Shrugged, the author Ayn Rand (1905–1982) describes a fictional United States of America in which the government churns out one new law after another to protect its people against the impact of an economic crisis. Unfortunately, though, this merely serves to fan the flames of the crisis instead of extinguishing it – whereupon the government issues yet more new restrictions, bans and regulations, which once again have exactly the same effect. A downward spiral triggered by a desire to do good.

Sadly, it is not out of the question that we will be forced to go through something very similar in real life over the next few months if not years. This is because, in order to keep as much of a lid on the crisis as possible, governments are currently embarking on the most severe, comprehensive and sustained intervention into economic life since the end of the Second World War.

And, if the situation gets even worse, they will not even shy away from measures that used to be seen as taboo. The German Bundestag, for instance, has agreed to create an "Economic Stabilisation Fund", which now runs to €100 billion. Amongst other things, its role is to take direct stakes in companies struggling as a result of the coronavirus crisis. Or, put another way, the German taxpayer is stumping up €100 billion (with the prospect of much more

to come) for a nationalisation spree. The days of Angela Merkel styling herself as the heir to Margaret Thatcher are clearly long gone.

Some people in Germany are already weighing up creating a dedicated institution for this purpose à la "Treuhandanstalt" to pool and manage the state's new holdings. "If the coronavirus lingers for much longer, it will change our economic system beyond all recognition. The market economy as we know it will most likely be demolished bit by bit. Private ownership and competition will become less important as government influence is massively ramped up. It would be an unplanned systemic change, born not out of revolutionary zeal but out of the simple necessity to prevent an economic collapse brought on by the global lockdown," predicted the April issue of Manager-Magazin, a publication where a measure of calm composure is usually the order of the day.

The consequences would be severe. Companies that opt against an investment by the state and attempt to carry on under their own steam would fall behind as they would find it harder to raise finance. And governments and their politicians could well find that they quite enjoy having a direct say in large parts of the economy and never want to give it up. In Austria perhaps more than anywhere else, we know what happens next. And, where surplus capacity appears, it has to be eliminated. Capital markets are quite good at tackling this kind of streamlining, politicians much less so. It is not inconceivable that

we will end up with a large number of structurally loss-making zombie companies that are only just being kept afloat by cheap government loans." (Manager-Magazin).

You don't need a great deal of imagination to be worried that a renaissance in the state ownership of companies on this scale will cause much more damage in the long term than the crisis itself.

In fact, this applies just as much to the policies of the central banks, whom the economic shock has prompted to throw off all pretence of shame and indulge in everything that had previously – and for good reason – been off limits. For instance, the rule has been scrapped that says the ECB can hold no more than 33% of the bonds of an individual eurozone country; another rule being sidelined used to specify that government bonds could only be bought up once a certain time had passed since they were issued on the secondary market; and short-dated government bonds will be allowed on the bank's shopping list in the future too. "In short, everything that should prevent Europe's central bank from engaging in the extremely dangerous pursuit of direct state financing no longer applies." (Josef Urschitz, Die Presse, 27 March 2020).

You would have to be a diehard optimist to believe that a policy like this would not cause significant damage in the long term such as a sharp rise in inflation, which would erode the savings of the

middle classes, pension pots and ultimately trust in money itself – a most dangerous state of affairs.

Part four: why not take a sledgehammer to the source of your prosperity?

Capitalism and the system of the free-market economy and competition has been on the back foot for a number of years, at least since the global financial crisis of 2008. Hiding behind the smokescreen of "critiquing capitalism", the supporters of government intervention, statism and socialist ideology have been attacking the very system that has brought more people prosperity and opportunities in life than any of its alternatives.

This movement was given an initial extra boost by the climate hysteria of 2019, which has now faded into the background; nevertheless, the coronavirus crisis is now providing a lot more powerful ammunition to those looking to blow up the free-market economy.

For instance, left-wing Austrian economist Stephan Schulmeister is a happy man: "Never in the past 50 years have we had such a big opportunity to fundamentally rethink our view of the world. In this severe crisis, people are realising that neoliberalism, with its selfishness and competitive mindset, has its polar opposite in what is actually important for people: the welfare state and social cohesion. Politi-

cians who have tended to defend neoliberal ideas and developed neoliberal policies are feeling it too."

Now, it may be somewhat bold to talk of "neoliberal policies" with the government spending ratio hovering around 50%, but it is clear what he means: returning to a state that has a firm hold on the economy.

And this sentiment is growing, especially in Germany. One German weekly newspaper straightfacedly called the coronavirus "a capitalist pandemic". And, undaunted, it blethered on: "It's not the virus that is killing people, it's capitalism."

Although this is clearly nonsense, more and more people are believing it – coronavirus or no coronavirus.

It's a pretty crazy state of affairs: although capitalism has ensured that more people than ever before are better off than ever before, it is growing increasingly unpopular. At least, this is what a study by the US communications agency Edelman in early 2020 suggests. Rather staggeringly, the study found that 56% of respondents, who were from 26 countries, believe that capitalism as it exists today "does more harm than good in the world". And 55% of Germans think this too. Only a minority recognise that, for all its inherent shortcomings, capitalism is the only economic system that has generated "prosperity for all" (Ludwig Erhard) and continues to do so.

Even in the USA, the mood is turning massively under pressure from the coronavirus crisis. In the New York Times, for instance, Martin Weiss, Austria's astute ambassador in Washington, observed recently that "Everyone's a Socialist in a Pandemic". The Philadelphia Inquirer, meanwhile, pondered whether the current crisis in the USA could usher in a form of "disaster socialism". Bear in mind that this is the country where President Ronald Reagan coined the famous phrase "The nine most terrifying words in the English language are: I'm from the Government and I'm here to help." (Wiener Zeitung, 3 April 2020).

By its very nature, Europe is in much more danger. For instance, the former Italian finance minister Giulio Tremonti – exhibiting the kind of pathos for which his country is not unknown – told an interviewer that the coronavirus was "the new Sarajevo". Just like the assassination of the Austrian heir to the throne Franz Ferdinand in 1914 and the subsequent world war had called an abrupt halt to the previous decades of internationalisation and the economic boom of the early 20th century, coronavirus would bring an end to the "golden thirty years of globalisation and the supremacy of the markets", he said.

And, at the moment, a fair few people would not be sorry to see them go. In an attempt to repackage the imminent loss of prosperity for broad swathes of the population, there are now increasingly frequent murmurs of a "systemic change" that is allegedly

required, of a "reflection on true values", of the urgent need to "slow down" – all of which we now apparently have the virus to thank for. For the most part, this is the vision of a deglobalised society in which everyone knits their own jumpers, travel is just something your grandparents tell you stories about and contemplative table talk is replacing the Internet.

There may be urban milieus in which this is seen as attractive, as long as you don't have to experience it first-hand. By contrast, the vast majority of people would view it as an imposition, because they would actually quite like to holiday on Majorca, drive a big car and buy smartphones made in somewhere like China. These people have as much interest in a "systemic change" as they do in getting tonsillitis, and they're fully entitled to feel that way. Why then should the coronavirus make any difference? It's not really clear.

Part five: the right way to live after the virus

Neither is it really clear yet what direction the crisis is going to take. It's quite conceivable that we will witness yet another successful example of what economists call "kicking the can down the road", just as we did in the years following 2008. In this case, this means: the ECB keeps on printing money, the debt bubble gets a fair bit bigger, the prices of material assets like houses or shares, gold or similar assets continue to rise, but the major crash does not

come. Politicians would have the perfect excuse for this approach in the shape of the coronavirus, which would appear to lend weight to the idea that there had been no other alternatives.

It would seem that this could work OK for a few years. At some point, however, the central banks will have no more bubbles left to blow up. As recently as March 2020, it became clear that even sizeable injections of new money by the Fed will no longer automatically mean that share prices will rise again straight away; in the short term, they can even fall further – a phenomenon never before witnessed. Something that the entire financial world had taken for a mighty bazooka turned out to be a rusty stovepipe.

What this points to is politicians potentially losing control over economic developments that have escalated uncontrollably. Once the house of cards starts to wobble, it will be nigh on impossible to stop it collapsing.

If it can be done at all, it will need the help of a radical paradigm shift in the world of politics. Shortly before his death in 2010, the libertarian economist Roland Baader got to the heart of this paradigm in some very vivid language that we can all relate to: "What we have packed our cheeks with in the credit-driven feeding frenzy of the past few decades, we'll have to starve ourselves of over the next few. It's going to get awful."

This is exactly what it's about. The political, economic and media elites will have to break the unpleasant news to the people that we have all been living above our collective means in some way. And that the debts piled up in the process will have to be brought down slowly but systematically, which will inevitably mean less prosperity. Greece has experienced what that feels like over the last ten years. But there will be no alternatives if our house of cards is to be prevented from collapsing at the eleventh hour. After all, there still ain't such thing as a free lunch.

At the same time, and the coronavirus shock would actually be an excellent place to start, we need a reset of government institutions. German author and commentator Markus Krall puts it nicely in his latest book Die bürgerliche Revolution ("The Bourgeois Revolution"). "There's an old rule in politics that says: if you need to cause pain, do so quickly and right at the start of a new government. If you act swiftly and resolutely, the self-healing powers of the market will work genuine wonders," he wrote, just before the outbreak of the pandemic in Europe. "It must consist of deregulation, savings, diverting spending from consumption to investments and repairing infrastructure, educational reform, defence reform, reform of internal security, pensions reform, immigration reform, a U-turn in energy policy, tax cuts, a drastic simplification of the tax system, a marked reduction in the government spending ratio, scrapping all subsidies, privatising the state's non-core tasks, cutting red tape, and a return to

freedom of contract in all industries, sectors and affairs."

That's it. However, many shrewd observers made exactly the same point after the 2008 financial crisis, although admittedly without all that much success. Of course, the constraints of political democracy make it extremely difficult to get a majority to hunger in an orderly fashion for what has already been wolfed down in advance. It's just that all the conceivable alternatives are even less attractive. Quite the opposite, in fact, as history has shown us. Now the choice is ours.

Christian Ortner
is a journalist, blogger and author ("Prolokratie").

He writes a weekly column in "Die Presse" and the "Wiener Zeitung", and runs "OrtnerOnline.at", the "central organ of neoliberalism".

Performance and Key Figures

PERFORMANCE AND KEY FIGURES OF CAPITAL BANK – GRAWE GRUPPE AG

	31.12.2019 TEUR	31.12.2018 TEUR	31.12.2017 TEUR
Total assets	985,386	964,741	935,480
Loans and advances to customers	413,146	336,928	316,520
Deposits from customers	497,409	476,493	370,669
Operating profit	12,041	14,746	14,910
Profit from ordinary activities	15,668	17,394	17,301
Total capital ratio pursuant to Art. 92 of EU Regulation No. 575/2013	23.0%	26.8%	22.6%
Volume of client custody accounts	12,456,168	11,621,560	11,612,897
Employees (excluding subsidiaries)	172	165	170

Management Report 2019 of CAPITAL BANK – GRAWE GRUPPE AG

Business performance and economic situation

Entrepreneurial activity and the investment of capital have one thing in common: both are associated with economic risk. Looking back on 2019, it is evident that the framework conditions for entrepreneurial activity and capital investment were more favourable than many indicators had predicted at the start of the year.

A review of the growth figures for the most significant economies in 2019 reveals consistently lower growth rates than in the previous year. However, solid growth was still achieved on average. Impending risks with the potential of weakening the global economy failed to materialise, including escalating trade conflicts – particularly between the USA and China, a resurgence of the euro crisis or a hard Brexit.

Global stock markets staged a remarkable rally against this background. The Dow Jones recorded an increase of 24.9%, while the DAX and the ATX rose by 25.5% and 16.1% respectively over the course of the year. The continued low levels for interest rates and the limited potential of bonds may also have contributed to this development.

CAPITAL BANK – GRAWE GRUPPE AG (referred to below as Capital Bank) has always managed to adapt well to the economic environment in the past and to bring innovation to the Austrian private banking market. The fact that we again lived up to our standards last year is highlighted by the result of the renowned Private Banking Comparison by the publisher Fuchsbriefe. We achieved an outstanding third place out of the 70 private banks tested in the German-speaking countries. Capital Bank set the benchmark for the industry, particularly in the categories of transparency and quality of advice and consultations.

Capital Bank specialises in providing advisory services in the field of asset management. The bank's core business is private banking, where the trust between client and advisor also forms the foundation for successful cooperation at all times. In addition to generating new client funds, assets under management increased by around 9.9%, partly as a result of positive price developments on the stock markets. Our customers' confidence in central asset management was in particular rewarded by the good performance of our products.

Capital Bank recorded significant growth of 22.1% in the unsecuritised lending business in the 2019 financial year. The volume was increased to €428.6 million in the last year. The focus in the financing area here has traditionally been on securities Lombard loans and selective real estate financing.

The fact that Capital Bank and its employees are recognised as a centre of excellence in the finance sector can be seen from their frequent appearances in the relevant financial and business media. We were able to increase our presence in the media even further with around 3.9 mentions per week on relevant professional topics (compared with 2.6 mentions per week in the previous year). Print media accounted for around 41.6%, online media for 48.2% and social media or radio/TV for 10.3%.

Several priorities were set in the 2019 financial year. Asset management was relaunched to make it even more attractive and to appeal to new customer groups. One crucial innovation was that stock selection with equities was made even more of an active process, while at the same time retaining the long-term portfolio direction. This has made future topics such as “digitisation”, “global ageing”, “automation & robotics” and other areas actively investable options.

Several events, podium discussions and presentations on current professional topics were also organised throughout Austria. Working with selected experts we were able to offer an attractive additional service to our customer with these events.

A change in customer behaviour became evident in the 2019 financial year as a result of new regulatory requirements. Directive 2004/39/EC on markets in financial instruments, better known as MiFID II, in particular led to a noticeable decline in individual

transactions and made the onboarding process more difficult due to increased documentary requirements. The clear objective here was to ensure that legal requirements are not implemented to the detriment of the customer experience.

The Family Office specialises in client relationship management for ultra-high-net- worth individuals, private charitable foundations and family businesses. Assets under management rose once again this year by 1.6%. The core competency of the Family Office is specific consideration of individual customer requirements on all financial matters. This may also include the implementation of specific topics, such as support with the acquisition or sale of a company or structuring a special financing deal.

In recent years the Family Office has established itself as a centre of expertise for absolute return deals and investments in private equity funds, providing an attractive earnings component for portfolio diversification.

The Asset, Product & Quality Management (APQM) division occupies a central role at Capital Bank with various areas of responsibility. Its main role is central asset management of customer funds. The focus here is on achieving an attractive risk / earnings ratio in line with the different risk classes. APQM also provides capital market expertise to private banking, e.g. through preparation of investment proposals, event-driven formulation of stock and market

estimates and a newsletter which is published daily and is very popular with customers and business partners. In addition to topics specific to the capital market, the APQM deals with all questions relating to securities taxation. These services have also been provided for Bankhaus Schelhammer & Schattera Aktiengesellschaft since 2016 (referred to below as Bankhaus Schelhammer). Product Management within APQM structures and manages the in-house Performance Linked Notes. Quality Management is responsible for efficiency improvement measures and numerous projects within the private banking division at Capital Bank and Bankhaus Schelhammer. An additional group within the division manages custody accounts for third-party banks and insurance companies.

The issue of charitable and not-for-profit activities is also handled by APQM. Aside from the administration for the Philanthropy Austria Foundation, this also includes the provision of philanthropy advisory services. As such, Capital Bank is acting as a pioneer in Austria.

"Die Plattform" is a division of Capital Bank and the leading B2B investment fund platform in Austria. As an independent custodian bank, securities transactions are processed for clients of investment firms and investment service providers.

The positive trend continued over last year and market share was repeatedly expanded. Digitisation

and increasing the level of automation remains an ongoing priority. In addition to implementation of a modern customer portal, the interfaces to the platform's sales partners were also improved and expanded.

The Investment Banking division specialises in investing in high yield corporate bonds. The long-term collaboration with the Cardinal Point Fund located in San Francisco USA also continued successfully in 2019. Central bank policies have had a significant impact on the risk-return ratios of credit markets and the credit cycle already appears to be close to a turnaround. In light of this, corporate bonds would be particularly vulnerable in the event of a recession, which is why the fund focuses intensively on risk management and maintenance of capital. The level of investment was low last year for this reason, in order to enable us to take adequate advantage of any opportunities that arise in the event of turbulence.

Capital Bank belongs to the GRAWE Banking Group. The staff and service divisions of the banking group are mainly located within the parent company HYPO-Bank Burgenland Aktiengesellschaft (hereafter Bank Burgenland), where they provide their services to the banks in the GRAWE Banking Group. Significant quality and cost synergies have been realised in recent years as a result of this consolidation.

Successful migration of the core banking system was another important step towards increasing efficiency. Capital Bank and all other Austrian institutions in the GRAWE Banking Group have run on the General Data Processing Centre system (ARZ) since June 2019. This migration enabled numerous business processes to be harmonised and optimised throughout the Group. The shared data processing centre is also the basis required in order to be able to leverage development potential in the future. Particular attention was paid to minimising the impact on our customers during the migration process. Capital Bank constantly endeavours to ensure that the standard of training and professional development for its employees is maintained at a very high level. The advanced professional skills and qualifications of our employees, together with their commitment and our regular investment in training and development, all mean that we can look forward to the performance of our bank with a great deal of confidence, both in the coming financial year and over the longer term. Capital Bank had 172 employees as at 31 December 2019 (previous year: 168 employees).

Capital Bank is conscious of its social responsibility as a member of society. During the year under review, it offered a large number of presentations and lectures on economic issues free of charge. In the specialist lectures delivered at universities, the bank's primary aim in all cases was to provide students with expert knowledge and give them an insight into

day-to-day business practice in the banking industry. Capital Bank also provides financial support for numerous social and higher education institutions.

Essential equity investments

The investment firm Security Kapitalanlage Aktiengesellschaft (referred to as Security KAG below) has gained an outstanding reputation in its more than 30-year history. As the asset manager for the GRAWE Banking Group, it currently manages 60 funds with a value of around €5.7 billion as at 31 December 2019. Security KAG has been one of the fastest growing investment companies in Austria over the last 10 years, with institutional and private investors relying on its expertise, mainly from Austria but also increasingly from Germany. The asset manager is one of the pioneers of the Austrian sustainability scene and is one of the leading providers of sustainable mutual funds.

BK Immo Vorsorge GmbH which was established in 2009 specialises in the construction of residential property specifically aimed at buy-to-let investors, the purchase and renovation of older real estate and the design of "building contractor models" in which the investor is established as the principal construction or development contractor. The company has been able to maintain a good position in all existing market phases on the real estate market and has made an encouraging contribution to comprehensive income over the last few years. In addition, the acquisition of several properties in Vienna and Graz created a promising project pipeline for the coming years.

Österreichische Post AG (referred to below as ÖPAG) has had an 80% stake in Brüll Kallmus Bank AG (referred to below as Brüll Kallmus) since 25 October; Capital Bank has reduced its stake to 20%. ÖPAG acquired its stake in the company by way of a capital increase. Brüll Kallmus is therefore no longer within the scope of consolidation of the GRAWE Banking Group and is accounted for at equity at Group level.

The stake in Brüll Kallmus is accounted for in the individual financial statements of Capital Bank at the mitigated lower of cost or market principle. Despite initial losses, the valuation of Brüll Kallmus was maintained as of 31 December 2019 due to positive medium-term planning and forecasting. The value of the investment is subject to an annual review.

The Bank's future business model differs fundamentally from the existing one. The plans e.g. are for Brüll Kallmus to offer a focused range of products for the retail segment under a new name (the company was renamed bank99 AG in January 2020) from the second quarter of 2020 onwards, consisting of current accounts, payment transactions, credit cards, debit cards and savings products, both via the ÖPAG branch network throughout Austria as well as online. The company's registered office was relocated to Vienna.

The previous business model of Brüll Kallmus, which was operated until the 3rd quarter of 2019 (primarily

in the Fixed Income segment with institutional customers), will now be operated within the GRAWE Banking Group by the Capital Markets division in Bank Burgenland.

General economic environment

Global economic growth slowed to 2.9% in the 2019 reporting year according to the latest estimates from the International Monetary Fund (World Economic Outlook Update, January 2020). Growth was therefore below that of the previous year (+3.6%) as well as below the expectations prevailing at the beginning of 2019 (3.5%). It was also the lowest growth since 2009. The global economic downturn was in sync regionally and has various causes. The most significant of these include increased trade barriers and geopolitical uncertainties. There are also structural factors that apply in the industrialised countries, such as the shrinking share of people of working age and sustained low levels of productivity growth. Economic growth in the eurozone in 2019 fell from 1.9% to 1.2% according to the latest IMF estimates. The decline was particularly sharp in Germany, which saw economic growth of 0.5% in 2019, i.e. one percentage point below growth for the previous year. Private consumption in the eurozone continues to represent a pillar for growth. However, the global environment put pressure on investment activity and net exports, with the weakness of these particularly noticeable in Germany as an “export nation”. The labour market has so far proved to be resilient

despite the economic downturn. The unemployment rate in the eurozone was 7.4% in December, 0.4% lower than in the same month the previous year. This is the lowest rate recorded in the eurozone since May 2008. Germany and the Netherlands had the lowest unemployment rates among the Member States at 3.2% each. The highest unemployment rates were recorded in Greece (16.6% in October 2019) and Spain (13.7%). Despite the improved situation on the labour market, inflationary pressure has so far failed to materialise in the eurozone. The annual rate of inflation in the eurozone was 1.3% in December 2019, compared with 1.5% in the previous year. The lowest rates of inflation were in Portugal (0.4%) and Italy (0.5%). The highest rate was recorded in the Netherlands at 2.8%. The lack of inflation dynamics prompted the European Central Bank (ECB) to relax monetary policy again over the course of the year. The monetary policy stance was agreed at the June meeting of the Governing Council by means of forward guidance on the key ECB interest rates. ECB President Mario Draghi spoke in the July meeting about the symmetry of the ECB's inflation target and about adjusting the Central Bank's monetary policy instruments as necessary in order to achieve the inflation target. At the penultimate Council meeting under Mario Draghi, the Governing Council decided on 12 September 2019 to reduce the interest rate for the deposit facility by 10 basis points to -0.50%. The interest rate on the main refinancing transactions and the interest rate on the marginal lending facility were left unchanged at 0.00% and

0.25% respectively. The Council also decided to include new net purchases under the ECB's asset purchase programme for a monthly amount of €20 billion from 1 November. Mario Draghi ended his eight-year term as President of the ECB on 31 October. He was succeeded as President of the European Central Bank on 1st November by Christine Lagarde, the former Managing Director of the International Monetary Fund. She was appointed by the European Council on 18 October 2019 for a term of eight years. Lagarde announced a review of the ECB's monetary policy strategy for 2020.

Economic growth in the United Kingdom in 2019 will be at the previous year's level of 1.3% according to the latest estimates. Growth was driven strongly by net exports in the second and third quarters of 2019, contrary to developments in the eurozone. Investment had a negative effect on the other hand. The rate of inflation was 1.5% in November, below the Bank of England's target of 2%. The unemployment rate is low at 3.8%. Boris Johnson's position in the negotiations on exiting the European Union was significantly strengthened by the clear result of the early elections in December 2019. Nevertheless, the United Kingdom and European Union are faced with some difficult negotiations in 2020 on reaching a trade agreement.

Economic growth in the USA in 2019 slowed by 0.6 percentage points to 2.3% on the previous year. Both investments and net exports declined

significantly over the course of the year. By contrast, the strong labour market supported consumption growth as a mainstay of the US economy. The lowest unemployment rate since 1969 was 3.5% as recorded in December. Real wage growth slowed despite the low unemployment figures and stood at just 0.6% in December 2019. The rate of inflation rose during the year from 1.9% to 2.3% and was therefore around the range of the FED's inflation target of 2%. The slowdown in the growth dynamic and the absence of inflationary pressure prompted the FED's monetary policy decision-making body, the Federal Open Market Committee (FOMC), to cut the US key interest rate in three steps over the course of the year from 0.25% in each case to a range between 1.5–1.75%.

Economic growth in China slowed during the year from 6.4% in the first quarter to 6% in the fourth quarter. The IMF expects growth of 6.1% for the year as a whole. China's real GDP growth in 2019 was therefore half a percentage point below the level of the previous year and 0.1 percentage point below the IMF forecasts at the start of 2019. While the contributions to growth from exports and private consumption declined, investment activity by Chinese companies increased significantly. The measures taken by the Chinese central bank to stimulate lending in the banking sector have therefore proven to be successful. The Chinese central bank has lowered the minimum reserve ratios for bank deposits on several occasions in recent years in order to achieve this effect. Although the "Phase One" deal in

the trade dispute with the USA has recently brought positive developments for the Chinese economy, risks continue to build domestically as levels of private and public sector debt rise.

Austria's economy was unable to escape the global slowdown in growth. Following an improvement of 0.5% in the first quarter of 2019, growth in GDP fell to 0.1% in each of the second and third quarters. This means that growth in 2019 will be significantly below the 2.7% in the previous year. Private and public consumer spending remains strong in line with the European trend, despite the economic slowdown. However, significant declines in growth rates can be observed for investments and exports. The unemployment rate fell to 7.3% for 2019 from 7.7% in 2018 according to national calculations. Unemployment was 4.2% in December according to Eurostat calculations, i.e. half a percentage point below the previous year's figure and well below the eurozone average of 7.4%. The HICP inflation rate fell over the course of the year from a baseline of 1.7% on 31 December 2018 to 1.0% by October, although this rose to 1.8% by December, i.e. 0.5 percentage points above the average for the eurozone. Following a weak start for the Austrian economy in 2020, the Austrian National Bank (OeNB) forecasts a gradual acceleration in economic development from the second quarter of 2020 onwards in its latest economic report ("Konjunktur aktuell"). The IMF expects growth in GDP of 1.1% for 2020 as a whole. The growth forecast is therefore

significantly below the average of 1.5% over the past ten years.

Capital market

Following the sharp rise in volatility in 2018, volatility gradually declined again until April 2019, remaining at moderate levels for the rest of the year. The SPX Volatility Index ("VIX") published by the Chicago Board Options Exchange fell from 25.4% at the start of 2019 to around 12% by the beginning of April. Over the course of the entire year, the volatility index failed to reach the historically low levels of 2017 when the VIX repeatedly posted levels below 10%. The index stood at 13.8% at the end of 2019. The stock markets performed strongly in this calm environment. The US S&P 500 Index rose by 723.9 points to 3,230.78 points over the course of the year, representing a gain of 28.9%. Although the European stock markets also performed strongly, average gains were once again below those of the USA. The broad-based Stoxx 600 Index ended 2019 with a gain of 78.2 points (+23.2%) to 415.84 points. Germany's leading index DAX gained 2,690.05 points (25.5%) and ended 2019 at an index level of 13,249.01. Austrian stocks were in less demand from investors. The ATX Index rose by 441.16 points (16.1%) to 3,186.94 points. The Stoxx 600 Bank Index even reached a 10-year low on 15 August. The index had only traded at lower levels in March 2009 as a consequence of the Great Financial Crisis. Nevertheless, the index rose by 8.22% over the course of the year. Brazil was once again one

of the strongest markets from among the emerging countries in 2019. The Bovespa index rose 31.58% to 115,645.30 points. By contrast, Hong Kong's leading share index (Hang Seng Index) recorded a gain of 9.1%. The thirty largest companies on the Mumbai Stock Exchange, which are consolidated in the BSE Sensex Index, gained an average of 14.4%. Stocks in emerging countries gained an average of 10.0% in 2019 measured against the MSCI Emerging Markets Index.

The bond markets were again dominated by the central banks. Three key interest rate cuts by the FOMC totalling 0.75% caused yields on 10-year US government bonds to fall by 0.81 percentage points to 1.88%. The yield on 2-year US government bonds fell by 0.92 percentage points to 1.57 % over the course of the year. The yield curve therefore remains very flat with a yield differential between two and ten-year government bonds of 0.31%. Yields on 10-year government bonds in Germany fell in the summer to a new record low. The 10-year German federal bond was trading with a yield of -0.71% on 28 August. This had risen again to -0.19% by the end of the year. This meant that the yield was 0.43 percentage points below the level for the previous year. By contrast, the yield on 2-year German government bonds remained virtually unchanged over the course of the year at -0.6%. As such the yield curve flattened to a yield differential between two-year and ten-year federal bonds of 0.42%. The performance for Greek government bonds was also remarkable in

2019. The yield on 10-year securities fell from 4.35% to 1.43% over the course of the year. As a result, the yield on Greek government bonds was only two basis points above Italian securities by the end of 2019, with the yield from these falling from 2.74% to 1.41% in 2019.

The euro was trading at 1.12 to the US dollar at the end of the year, slightly below the level of 1.15 at the start of the year. The common currency also fell slightly in value against the British pound and Japanese yen. As of the end of the year, the euro was trading at 121.77 against the Japanese yen and at 0.85 against the British pound.

BUSINESS DEVELOPMENT AND FINANCIAL PERFORMANCE INDICATORS

Statement of financial position

Capital Bank's total assets rose moderately in 2019 by around 2.1% from €964.7 million to €985.4 million. In particular the increase in loans and advances to customers, which rose by €76.2 million to €413.1 million, had the effect of increasing the total assets. On the liabilities side, deposits from customers increased slightly by €20.9 million to €497.4 million. At the same time, the volume of own issues fell slightly to €224.7 million compared with €228.8 million in the previous year.

Own funds pursuant to Part 2 of the CRR were increased by 4.6% from €162.9 million to €170.3 million in the 2019 financial year. The own funds requirements increased significantly by 29.2% to €77.9 million. The resulting surplus of own funds is €92.4 million. The own funds surplus fell on the previous year by €10.2 million or 9.9%. The Common equity Tier 1 capital ratio fell to 22.4% from 25.7% in 2018. However, this remains extremely high compared with the rest of the industry. The total capital ratio also fell over the course of the year by 3.7 percentage points and stood at a healthy 23.0% at year-end. The quotas shown are calculated on the basis of the minimum own funds requirement. Of the own funds reported of €170.3 million, 97.0% was accounted for by Tier 1 capital.

The return on equity, which is the ratio of profit for the year before taxes to equity excluding distributable profit before changes in reserves, (ROE: 2019: 12.5%; 2018: 13.9%) declined slightly compared with the previous year's level. The return on assets, i.e. the ratio of the profit from ordinary activities to average total assets, barely changed in the period from 1.8% to 1.6%. The return on capital employed fell from 28.8% to 20.1% over the course of the year. The return on capital employed is calculated from the ratio of profit from ordinary activities to the own funds requirements.

As the focus at Capital Bank is on fee and commission business, the changes in total assets and the comparison with traditional retail banking are less important in an analysis of the bank's performance. The long-term objective of the bank is to generate returns commensurate with the risks involved in the interests of the owner and thereby to continue to increase the profitability of the business in the future.

Income statement

Capital Bank generated a profit on ordinary activities in the 2019 financial year of €15.7 million, which is therefore around €1.7 million below the previous year's level of €17.4 million. The picture in the operating business is mixed. At €25.3 million, the net fee and commission income and net financial income is around 7.9% down on the previous year. This decline in earnings was partly offset by growth in the lending business. Net interest income increased by €816 thousand to €11.4 million in the reporting period.

Personnel expenses increased by 1.9% to €16.7 million in line with expectations. The increase in operating expenses was much higher at €1.1 million. These amounted to approximately €11.7 million as at 31 December 2019. Costs incurred in connection with migration of the core banking system and higher IT expenditure are the main factors behind this increase.

Capital Bank generated an operating profit of €12.0 million for 2019. This equates to a fall of 18.3% compared with the operating profit of €14.7 million in 2018. The cost income ratio rose on the previous year from 65.6% to 70.9%.

Volume of client custody accounts

Capital Bank also continued to focus in the 2019 financial year on gaining market share and therefore expanding its volume of client custody accounts. Compared with the previous year, the volume of client custody accounts increased by 7.2%following momentum from the financial markets. Capital Bank managed client custody accounts valued at €12.5 billion as at the balance sheet date.

Our subsidiary Security KAG recorded a strong 14.8% increase in the volume of securities accounts to €5.7 billion. At the same time, assets under management including own issues of the Capital Bank sub-group also increased in the year by 9.1% to €18.6 billion.

Proposed dividend

The profit from ordinary activities generated in the 2019 financial year amounted to €15.7 million. Capital Bank will pay a dividend of €5.0 million to its shareholder Bank Burgenland following the resolution passed at the Annual General Meeting. The remainder of the annual profit will be allocated to equity in order to strengthen the own funds base even further.

OUTLOOK

The IMF expects growth rates to increase again in 2020 and 2021 following the global economic downturn in 2019. However, it was forced to revise these rates downwards by 0.1 percentage points for 2020 to 3.3% and by 0.2 percentage points to 3.4% for 2021. The IMF points to some surprise negative factors in its downward revision affecting some emerging countries, especially in India. It had not yet taken into account the potential effects of the coronavirus on the Chinese economy in particular and the global economy in general. On the positive side, the IMF refers to the bottoming out in the manufacturing sector and in global trade in its latest update. The expansionary global monetary policy, recent easing in the trade dispute between the US and China ("Phase One" deal) and diminishing risks from the UK's exit from the EU also support the economic outlook. While the IMF was forced to revise growth expectations downwards for 2020 and 2021, it points to a reduction in downward risks for the baseline scenario.

Banks should therefore prepare themselves for a sustained low interest rate environment with continuing economic uncertainty. Costs in the industry are also expected to rise at the same time due to regulatory issues. We expect pressure to increase further on the commission business, particularly in private banking.

Capital Bank's clear objective against this background is to expand business volumes even further in order to compensate for the negative effects of rising regulatory costs and declining margins. Cost-saving measures can be expected if this objective is not achieved. Market momentum was harnessed effectively in 2019. However, it would be wrong to expect similar support from the capital markets for 2020.

We are convinced that we will be able to continue operating successfully on the market in future with the backing of a traditional insurance group, the strength of a broad-based banking group, our sophisticated business model and the quality and commitment of Capital Bank's employees.

Risk Report CAPITAL BANK – GRAWE GRUPPE AG

At Capital Bank, risk management is defined as a process (based on a division of labour) for identifying, measuring, monitoring and managing risks defined in the GRAWE Banking Group. A risk management system with an appropriate level of quality is seen as a significant factor if the required growth of the business is to be successfully sustained over the long term. The risk-policy principles, responsibilities as well as control principles are enshrined in the GRAWE Banking Group's risk management. The responsibilities are clearly regulated in terms of content and function.

The objectives in the risk management unit are to identify, quantify and actively manage all the risks arising in connection with banking operations (credit risk, market risk, interest-rate risk, liquidity risk and operational risk). Pursuant to the statutory provisions set out in section 30 (7) of the Austrian Banking Act (BWG), Bank Burgenland, as the parent bank, is therefore responsible for satisfying the Internal Capital Adequacy Assessment Process (ICAAP) requirements at consolidated level. The entities included in the ICAAP consolidation for Bank Burgenland include Bankhaus Schelhammer and its subsidiaries, Capital Bank, BB Leasing and Sopron Bank as a downstream credit institution in other EU countries. The risk strategy in the GRAWE Banking Group is to take on standard banking risks within a defined framework and to

exploit the resulting potential returns. To this end, a risk management system has been set up in the GRAWE Banking Group. This system forms the foundation for strategic bank management based on risk and returns, and therefore promotes selective growth.

At Capital Bank, risk management is a central function that takes into account the regulatory framework based on the Austrian Banking Act (BWG), the CRR, as well as various policies and guidelines, along with the nature, scope and complexity of the transactions specific to the bank and the resulting risks to which the bank is exposed. The risk management system at Capital Bank is integrated into the risk management cycle managed by the GRAWE Banking Group.

The basis for risk management in the GRAWE Banking Group is a strict segregation between front office and back office functions. The various risk management functions are brought together under the member of the Management Board responsible for risk management. The activities of the risk management units are conducted in accordance with the risk policy guidelines laid down by the Management Board. These guidelines specify how risks are to be managed and how they are to be monitored competently and in a timely manner in conjunction with the individual corporate units and the independent risk function. In application of the principle of proportionality, the organisation of

risk management reflects – both qualitatively and quantitatively – internal requirements, the business activities involved, the bank's strategy and the risk situation. Organisationally, the risk management system is located at the GRAWE Banking Group level and is also implemented for the subsidiaries under the responsibility of Bank Burgenland. The responsibilities of the risk management unit at Capital Bank include the control of market risk, liquidity risk, credit risk and operational risks, risk management for the subsidiaries of Capital Bank as well as overall control over the bank. The operational management of credit risk is carried out by the credit risk management department. The implementation of risk management for the Group involves close cooperation between the risk management unit at Bank Burgenland and Capital Bank.

Basic principles of risk management

Risks at Capital Bank are controlled and managed through a system of risk principles, risk measurement procedures, limit structures and monitoring processes.

A key underlying component of the risk management process is the risk policy. The risk policy forms part of the corporate strategy, specifies the bank's risk appetite and risk focus, and sets out the framework within which the operational risk policy targets are to be pursued. The risk policy at Capital Bank is determined by the Management Board taking into

account Group developments and guidelines. It covers the planned development of the business as a whole from a number of different dimensions, specifies limits for relevant risks and restricts concentration risk.

The risk policy principles represent a further component of the basic principles of risk management. The following risk policy principles have been specified as applicable throughout the Group:

- The Management Board and all employees must act in accordance with the risk policy principles and must make decisions in compliance with these guidelines.

- In order to achieve the desired balance of risks and returns, the individual business divisions must be limited by means of risk and/or volume specifications taking into account the risk-bearing capacity of the bank.

- The methods used for assessing and measuring risk must be structured and applied according to the scope, complexity and risk content of the transactions involved in each case. The systems must cover not only the risk arising from trading business but also any risk arising from an analysis of the bank's activities as a whole. The selection of methods should be flexible to permit sensible further development in the future.

- To ensure a consistent and coherent risk management process, standardised methods must be used for assessing and limiting risk.

- As part of the risk management system, a suitable system of limits must be implemented and continuously monitored. The overall bank limits must be used to derive and specify limit systems both for the individual sub-risks and also for the individual subsidiaries. The specified risk limits must be based on the potential risk cover. However, the entire potential risk cover must not be used up in connection with the measured risks; a proportion must be held in reserve for exceptional circumstances and other risks that have not been measured.

- Risk management and control processes reflect the statutory requirements currently applicable and will be adjusted in line with changing conditions. The risk management performance indicators are also included in a system for strategic bank management.

- In the case of significant types of risk that may jeopardise the bank as a going concern, the bank will endeavour to put in place a risk management system that is at least similar to that in comparable banks in terms of structure and volumes (best practice principle).

- Responsibility for risk management lies at GRAWE Banking Group level. In addition, every

employee is encouraged to identify potential risk and initiate appropriate corrective action.

- The organisation of risk management is subject to the principle of segregation of functions between front office and back office and must ensure that conflicts of interest are prevented at all decision-making levels.

- For the purposes of ongoing risk management, regular reports on the risk situation must be submitted to the Management Board and to the decision-making committees at Group and individual bank levels. The relevant organisational units are responsible for risk documentation and reporting.

Another key component of the risk management system is the product approval process, which is applied when the bank launches new products or ventures into new markets. Capital Bank generally only takes on exposures in those areas of business in which it has appropriate professional knowledge or relevant experts and in which it can assess the specific risks involved and carry out suitable monitoring. When moving into new business areas or products, a key prerequisite is therefore a suitable analysis of the risks specific to the business concerned. To this end, Capital Bank has set up a product approval process, which comprises defined rules and regulations for the organisation of the procedures involved. The process determines the procedures to be followed for issues, investments in new products and entry

into new markets or areas of business. When the process is implemented, it identifies the main opportunities and risks, which then serve as a basis for decision-making.

Risk management

In order to ensure there is a comprehensive, coordinated risk management system, the bank has drawn up an overall bank risk strategy and uses an overall bank risk manual together with service and work instructions as a documentation basis; it has also specified risk limits.

The overall bank risk strategy first defines general principles for risk management (basic principles, risk management process, organisation, etc.) and then set out risk strategies for each risk category. The objective of the risk manual is to meet the statutory and the business management requirements in respect of risk management. It provides support in the systematic handling of risk and enables employees and managers to systematically address the individual components of risk management. The service and work instructions, like the risk manual, have the objective of informing employees about special (risk) topics and their management in greater detail. In contrast to the risk manual, they are extremely detailed and are mostly restricted to specific individual topics.

The risk limits are defined at least once a year on the basis of the risk-bearing capacity calculation. Compliance with risk limits is continuously monitored and regularly reported to senior managers. If a limit is exceeded, limitation measures are to be decided upon in cooperation with the management board and the respective area head in accordance with the respective risk.

The main tool used for risk management at Capital Bank is the calculation of risk-bearing capacity. In this calculation, the key risk figures from the individual types of risk are aggregated into an overall potential loss from the assumption of risk and in the same process compared against the cover assets (earnings, reserves, equity) available to be set against these potential losses. The aim of this comparison is to determine the extent to which the bank is able to sustain any unexpected losses (risk-bearing capacity). According to the risk-bearing capacity calculation, the goal is to ensure the certainty of the bank's continued existence. The Management Board decides on the overall risk strategy, which includes the allocation of the potential risk cover to the individual risk categories. The calculation of the risk-bearing capacity acts as a brake on all risky activities within the GRAWE Banking Group. The risk-bearing capacity is calculated quarterly at Group level and on an individual basis for all banks in the GRAWE Banking Group. Risk positions are also constantly monitored in order to be able to take

ad-hoc risk-minimising steps when discrepancies arise.

Risk-bearing capacity is calculated using two methods: the gone concern approach, which focuses on protection for creditors, and the going-concern approach, which takes as its basis the need to ensure the problem-free continuation of the bank as a going concern.

Under the gone concern approach, the capital available to the GRAWE Banking Group for dealing with risks is the equity composed of the tier 1 capital, reserves and the supplementary capital, including from the profit already generated by the key date. Under the going concern approach the forecast value is taken into account in determining the risk coverage potential instead of the results already achieved. The methodology used for calculating the risks varies depending on the risk category and the selected analysis method. Credit risk (incl. consideration of risks from loans in foreign currencies and country risks), market risks in the banking book (incl. credit spread risks), operational risk, liquidity risk, investment risk, real estate risk and other types of risk as well as the macroeconomic risk are all taken into account with this. To determine the overall risk, the individual types of risk are aggregated without factoring in any adjustment for the effects of correlation between the types of risk.

The Bank took into account the mandatory reconciliation process between the quantified potential risk and the risk coverage potential available to the bank at all times during 2019. Calculations based on stress scenarios are also applied in order to assess the risks that could arise from extreme market volatility.

Management of special types of risk

All risks in the GRAWE Banking Group are considered as part of the overall bank risk management for Capital Bank. Given the bank's direction, material risk arises primarily in the areas of operational risk, investment risk, legal risk and market risk. Particular attention is given to these risks in the monitoring and management process.

Market risk

Market risk refers to potential losses that could arise from adverse changes in the market value of exposures as a result of changes in exchange rates (currency risk), share prices, indices and fund prices (equity risk), credit spreads (spread risk) and volatility (volatility risk). Risk exposures affected by market risk arise either in connection with client transactions or as a result of the conscious inclusion of such exposures in the bank's own portfolio. The main risk factors within the scope of market risk include interest-rate risk, currency risk, price risk related to variable-yield securities and price risk related to interest-bearing securities caused by credit spread.

Market risk is managed by Group Treasury, the assets and liabilities committee, the capital markets committee and by the risk management unit, which is responsible for identifying, measuring, monitoring and managing market risk in the trading book and banking book. A key feature of the organisation of treasury activities is the segregation of front office and back office functions. The bank may only take on market risk within existing limits and only in respect of authorised products. These limits are specified annually by the Management Board and the Supervisory Board taking into account the risk-bearing capacity of the bank and the limits specified for the Group. Key factors used in developing the limit structure are the desired degree

of diversification in the portfolio and the trading strategy. The limits include country limits in addition to volume and exposure limits.

The bank may only conduct investments on its own account within defined limits. These limits are monitored continuously in accordance with the risk management guidelines for treasury investments. To all intents and purposes, currency risk is effectively eliminated at Capital Bank by means of currency-matched funding and the use of foreign exchange derivatives. Tight limits are imposed if foreign exchange exposures are left open.

At Capital Bank, interest-rate risk is defined as the risk of fluctuations in the price of interest-bearing securities, arising in turn from changes in capital market interest rates. Interest-rate risk is managed for the whole of the Group by Group Treasury and the assets and liabilities committee, which manage the interest-rate structure taking into account the risk involved. On the basis of interest-rate risk statistics from the Austrian National Bank (OeNB), it is possible to state that interest-rate risk at CAPITAL BANK – GRAWE GRUPPE AG is at a low level compared with the regulatory threshold.

A particular aspect of market risk that affects Capital Bank is the risk arising from guarantees given in connection with the securities business. Capital Bank has given capital guarantees for certain products that it has designed and sold itself, and for products

that are sold by insurance companies. The PZV (prämienbegünstigte Zukunftsvorsorge) product, a special pension plan product offered in Austria with a government subsidy, is especially important in this context because Capital Bank assumes responsibility for the capital guarantee in connection with this investment product in accordance with statutory requirements (section 108 (1) no. 3 of the Austrian Income Tax Act (EStG)). The Bank has also assumed guarantees for unit-linked life insurance. Under this capital guarantee, the bank guarantees with the PZV (prämienbegünstigte Zukunftsvorsorge) product, a special pension plan product offered in Austria with a government subsidy, that the client will receive a payout that is at least equivalent to the amounts paid in plus the government subsidy. Capital guarantees and maximum level guarantees are also provided in unit-linked life insurance. The risk associated with capital guarantees is subject to greater monitoring in the risk management system. Even before the bank took over responsibility for this guarantee, the product was subject to an authorisation process in which, both within the bank itself and also with third parties, the product process was discussed in detail, various problems were addressed and solutions drawn up. Within the capital guarantee management process at Capital Bank, trends regarding the guarantees are monitored, as are the investment criteria and the performance of the underlying funds. Stress tests are also regularly carried out for the capital guarantees in order to highlight the impact of market trends on any payment that may have to be made

under the guarantee. In addition, the bank holds regular guarantee meetings in which it discusses material changes concerning the capital guarantee portfolios and the underlying funds with Security KAG and Grazer Wechselseitige Versicherung AG. Guarantees with a total guaranteed sum of around €165.5 million (2018: around €156.8 million) were outstanding at Capital Bank as at the reporting date. Guarantees with a total guaranteed sum of around €341.5 million (2018: around €332.8 million) were outstanding in the GRAWE Banking Group as a whole. The guarantees are matched by corresponding recoverable investments.

Operational risk

At Capital Bank, operational risk is defined in the same way as in the statutory provisions as the risk of unexpected losses caused by the inadequacies or failure of internal procedures, people or systems, or by external events, and includes legal risk. A more detailed and then aggregated measurement and management of risk should therefore be applied, for example, to breakdowns in IT systems, damage to property, processing failures, fraud, natural or other disasters and changes in the external environment. Operational risk also includes cyber risks. The term cyber risk essentially describes the risk that arises when navigating in a digital and connected world (cyberspace). On the one hand, cyber risks exist due to the possibility of deliberate, targeted IT-supported attacks on data and IT systems. These

attacks are likely to have the following consequences: violation of the confidentiality of data (e.g. loss of data, spying on data), violation of the integrity of the system or data (e.g. data corruption, possibly by means of malware), fast, massive, inexpensive and far-reaching dissemination (e.g. e-mail campaigns against companies, calls for boycotts via social media) and through "social hacking".

Such risks must be classified according to the cause of the risk so that operational risk can be identified and analysed with precision. The purpose of risk categories is to help the bank to analyse the size, cause and impact of operational events that occur. Self-assessments are also used to support the process of ascertaining the potential risk. Loss events are recorded in a separate database on an ongoing basis. Additional risk information can be obtained from various risk indicators, such as the number and duration of system breakdowns, findings from internal audits (process risks) and the frequency of complaints and claims against the bank. The principal concern of risk management is to find an answer to the question as to whether and how an existing risk can be mitigated. The task of risk management is therefore to search for solution options and possible corrective action. The task is carried out by the department responsible for the risk, generally in collaboration with the Internal Audit and Organisation units.

The management of operational risk at Capital Bank is the responsibility of the risk management unit. The duties of the unit include classifying the risks, drawing up standard guidelines for use throughout the Group, managing the operational risk database, analysing loss events and preparing reports for the Management Board and various committees. Based on the standards applicable throughout the Group, loss events related to operational risk are assembled in one database. This database can then be used as a basis for identifying weaknesses in systems and processes and then for initiating appropriate corrective action.

The systems and structures used by Capital Bank to minimise operational risk also include internal control systems (including control systems managed by Internal Audit), clearly documented internal guidelines (work instructions), segregation of functions, the principle of double-checking by a second person, allocation and limitation of decision-making authority, together with an ongoing process of training and professional development (personnel development) to ensure that employees have the requisite skills and qualifications, which they then continue to enhance. These internal management and control measures integrated into the business processes are intended to ensure that there is an appropriate, acceptable level of risk within the bank.

In the context of operational risk, Capital Bank pays special attention to the risk associated with the provision of advice, a risk that arises particularly in the private banking business. To manage this risk, the bank has developed special risk management procedures that have now been used for a number of years in the private banking business and have been refined over the course of time. The main focus of the risk strategy in this case is to discover any possible errors in advice or undesirable developments at an early stage and identify associated advisory or reputational risks. Regular meetings also take place with the market divisions and the Management Board as part of these risk management activities.

Capital Bank uses the Basic Indicator Approach to determine its capital adequacy for operational risk in accordance with Basel III.

Credit risk

At Capital Bank, credit risk is defined as the default risk that arises in connection with loans and advances not evidenced by certificates and loans and advances evidenced by certificates (securities) to third parties. The risk is that these loans and advances may not be repaid in full or on time to Capital Bank. The situation may arise from developments at individual counterparties or from general problems affecting a large number of counterparties. Credit risk may also arise from particular types of product design or types of business. Expert manage-

ment of all credit risks is the responsibility of the credit management unit. This unit carries out the banking operations on the assets side of the balance sheet at an operational level. The tasks include checking all finance applications from the perspectives of risk and credit quality in accordance with the relevant guidelines, reviewing compliance with measurement and assessment guidelines and identifying any early warning indicators. At Capital Bank, risk in the lending business is managed in accordance with the principles agreed by the Management Board and specified in the credit risk manual. These guidelines meet the minimum standards for lending business issued by the Austrian Financial Market Authority (FMA) and are updated if there are any legal or other changes affecting this type of business. The basic principles of lending business at Capital Bank include a clear credit and associated risk policy. The detailed risk assessment for each loan commitment, in particular the customer's creditworthiness rating, is very important as part of the process for approving loans. Each loan decision is based on a thorough analysis of the loan commitment, including an assessment of all relevant influencing factors. Following the initial loan application the Bank's loan commitments are generally monitored once per year.

The risk management unit is responsible for identifying, measuring, assembling, planning, managing and monitoring the overall credit risk portfolio. The total lending exposure (loans and advances to clients including securities) and the breakdown of the risk

volume by currency, risk category and country is regularly reported to the Management Board. Stress scenarios are also defined for the credit exposure which inter alia simulate a deterioration in the collateral situation. In addition, concentrations in the securities furnished as collateral are continuously analysed in order to highlight any resulting cluster or concentration risk. Credit risk data from Capital Bank is also fed into the analysis and assessment of the credit risk for the whole of the Group.

To manage country risk, country limits have been set both at Group and individual bank levels. Capital Bank has laid down guidelines for the approval of counterparties with the aim of minimising counterparty risk. The risk management unit is responsible for vetting new trading partners. The unit carries out checks on new partners and approves them using internal criteria.

Investment and real estate risk

The investment risk represents a special form of credit risk and includes the risk of a need for depreciation or write down of the carrying amount of the equity investments. It describes the risk that the investments made may result in potential losses (as a result of a lack of a dividend, partial depreciation, losses made on sales or a reduction in undisclosed reserves) from equity provided, from profit-transfer agreements (assumption of losses) or from liability risks (e.g. letters of comfort). The term investment risk at Capital Bank covers risks from equity investments similar to loans on the one hand and risks from the investment in bank99 AG on the other. Risks from stocks, investment fund units and other investment securities on the other hand are stated under market risks. The real estate risk arises from fluctuations in market prices for real estate.

Capital Bank's investment commitment consists primarily of the investment in Security KAG, BK IMMO GmbH and the investment in bank99 AG. The real estate risk is a subordinate risk category. The GRAWE Banking Group has set up its own department for managing equity investments and real estate.

Liquidity risk

Liquidity risk encompasses both insolvency risk and liquidity maturity transformation risk. The aim of managing liquidity risk is to ensure that the bank can meet its payment obligations by the due date at all times without having to incur unacceptably high costs.

The group treasury function together with cash pooling for the entire banking group is the responsibility of Group Treasury at Bank Burgenland. Liquidity risk is managed centrally for the whole of the banking group under the auspices of the assets and liabilities committee, which meets regularly.

Making provision for an unforeseeable increased need for liquidity is guaranteed through maintaining a sufficient portfolio of liquid assets which can be used for liquidity procurement at short notice. The amount of the liquidity buffer is determined based on the liquidity simulations for various scenarios which are regularly reported to the Management Board. Capital Bank had sufficient liquidity at its disposal at all times in 2019 and was above the key figures required under supervisory law at all times.

Macroeconomic risk

Macroeconomic risk arises from an economic deterioration as part of the traditional economic cycle and a potential increase in the accompanying risk parameters. Macroeconomic risk is factored into the bank's risk calculations so that it would have sufficient aggregate risk cover even after such a period of deterioration without the need for massive intervention and corrective measures. The quantification of the risk assumes a contraction in GDP which is then reflected in a deterioration in default rates. Credit risk is recalculated using these modified parameters and the difference compared with the original credit risk represents the macroeconomic risk.

Other risks

The main risks included within other risks are business risk, strategic risk and also reputational risk. These risks are factored into the calculation of risk-bearing capacity in the form of a capital buffer. Business risk is defined as the risk of a loss from a negative trend in the economic environment and in the bank's business relationships. Business risk may arise primarily from a significant deterioration in market conditions, from changes in the competitive position or from changes in client behaviour. This can lead to a sustained fall in earnings and thus a decrease in enterprise value. Responsibility for strategic corporate management lies with the Management Board of Capital Bank. The management of

business risk is the responsibility of those business units that focus particularly on increasing the volume of assets under management and thus on enhancing earnings capacity. Decisions on the fundamental direction and development of the Bank's business activities harbour a risk that the consequences in terms of attaining long-term corporate objectives may include a range of problems from undesirable developments to a complete failure to achieve objectives.

Summary and outlook

At Capital Bank, suitable action is taken to limit and minimise all material risks. An analysis of risk-bearing capacity is carried out in which all the measurable risks throughout the whole of the bank are aggregated. The measures to limit risk also include a suitable limit system and the calculation of different key risk indicators.

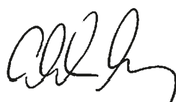
The Capital Bank Group will also continue its business activities during 2020 in line with its chosen risk strategy. One of the key areas of focus in risk management activities will be the ongoing further development of risk methods, systems and management in the GRAWE Banking Group. Given the special nature of the business model at Capital Bank, risk monitoring in the private banking business will also continue to be a focus of risk management activities. In addition to this focal area, the ongoing ICAAP and ILAAP processes, capital

guarantees, the extension of documentation requirements, the internal control system and continuous improvements to existing risk management activities will all represent further tasks for risk management. Another priority in 2020 will be the preparatory work for the implementation of Basel IV in the form of a joint project in the shared data centre. Developing management tools, supporting the professional training of employees and ensuring continuous development in internal risk quantification methods will also remain priorities for 2020.

Graz, 02 March 2020

The Management Board

Christian Jauk, MBA MAS
CEO



Mag. Constantin Veyder-Malberg
Member of the Management Board

Wolfgang Dorner, CIA,
Member of the Management Board

01. PROFIT FROM ORDINARY ACTIVITIES IN € THOUSANDS

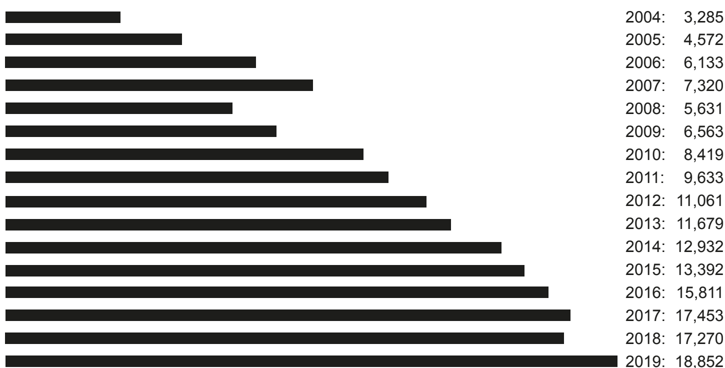
Year	Value
2004	14,830
2005	15,961
2006	16,840
2007	17,663
2008	175
2009	5,451
2010	7,088
2011	6,905
2012	7,181
2013	7,661
2014	29,551
2015	10,845
2016	11,110
2017	17,301
2018	17,394
2019	15,668

02. TOTAL ASSETS IN € '000

Year	Value
2004	225,975
2005	389,054
2006	563,684
2007	735,829
2008	731,082
2009	653,309
2010	679,772
2011	704,449
2012	833,990
2013	920,513
2014	933,233
2015	882,830
2016	847,896
2017	935,480
2018	964,741
2019	985,386

03. OPERATING PROFIT IN € THOUSANDS

04. ASSETS UNDER MANAGEMENT (INCL. SECURITY KAG) IN € MILLIONS



05. OPERATING INCOME IN € MILLIONS

Year	Value
2004:	42.9
2005:	46.1
2006:	45.5
2007:	47.4
2008:	33.2
2009:	32.2
2010:	31.4
2011:	34.5
2012:	34.9
2013:	36.0
2014:	43.9
2015:	40.8
2016:	40.6
2017:	41.0
2018:	42.8
2019:	41.4

06. NET INTEREST INCOME IN € THOUSANDS

Year	Value
2004:	4,462
2005:	4,931
2006:	7,440
2007:	10,641
2008:	9,426
2009:	5,710
2010:	5,031
2011:	7,973
2012:	7,292
2013:	6,991
2014:	7,949
2015:	9,854
2016:	9,855
2017:	9,179
2018:	10,550
2019:	11,365

07. PERSONNEL EXPENSES IN € MILLIONS

Year	€ millions
2004:	11.2
2005:	13.2
2006:	16.3
2007:	15.5
2008:	11.1
2009:	11.0
2010:	12.0
2011:	12.8
2012:	13.3
2013:	13.6
2014:	14.8
2015:	14.7
2016:	15.6
2017:	15.9
2018:	16.4
2019:	16.7

Report by the Supervisory Board

The Supervisory Board monitored the Management Board in 2019 and endorsed its activities on the basis of four meetings of the Supervisory Board to which the Management Board submitted reports and documents as well as on the basis of repeated contact between the two boards.

The annual financial statements for 2019 and the annual report, to the extent that it provides explanations for the annual financial statements, were audited by KPMG Wirtschaftsprüfungs- und Steuerberatungs GmbH, 1090 Vienna. This audit did not give cause for any reservations and the auditors issued an unqualified audit certificate.

The Supervisory Board has acknowledged the report and proposal for the appropriation of profits submitted by the Management Board and has reviewed and approved the annual financial statements for the year ended 31 December 2019. These annual financial statements have therefore been formally adopted pursuant to section 96 (4) of the Austrian Stock Corporation Act (AktG).

The Supervisory Board would like to take this opportunity to thank all clients for their confidence in Capital Bank – GRAWE Gruppe AG and to express its gratitude to the Management Board and all employees for their contributions in 2019.

Graz, April 2020

Dr. Othmar Ederer
Chairman of the Supervisory Board

STATEMENT OF FINANCIAL POSITION OF CAPITAL BANK – GRAWE GRUPPE AG

08. STATEMENT OF FINANCIAL POSITION OF CAPITAL BANK – GRAWE GRUPPE AG AS AT 31 DECEMBER 2019

ASSETS		31 Dec. 2019 €	31. Dec.2018 € '000
1. **Cash on hand and balances at central banks**		77,756,115.21	101,189
2. **Public-sector debt instruments eligible as collateral for central bank funding**			
Public-sector debt instruments and similar securities		17,682,967.35	16,419
3. **Loans and advances to banks**		198,008,075.52	229,124
a) Repayable on demand	65,492,486.40		185,895
b) Other loans and advances	132,515,589.12		43,229
4. **Loans and advances to customers**		413,146,107.28	336,928
5. **Bonds and other fixed-income securities**		50,971,062.21	42,304
6. **Shares and other variable-yield securities**		79,815,732.06	96,968
7. **Equity investments**		12,678,998.18	665
of which: in banks	12,004,215.01		4
8. **Shares in affiliated companies**		11,707,255.30	23,707
of which: in banks	10,900,925.13		22,901
9. **Intangible fixed assets**		147,194.26	323
10. **Property and equipment**		997,562.07	1,043
11. **Other assets**		111,773,598.68	105,884
12. **Prepaid expenses**		595,163.12	717
13. **Deferred tax assets**		10,105,872.66	9,471
TOTAL ASSETS		985,385,703.90	964,741
Below-the-line items			
1. **Foreign assets**		371,980,194.86	361,272

EQUITY AND LIABILITIES		31 Dec. 2019 €	31 Dec. 2018 € '000
1. Deposits from banks		16,395,889.27	22,307
a) Repayable on demand	5,731,882.77		12,307
b) With agreed maturity or notice period	10,664,006.50		10,000
2. Deposits from customers		497,408,828.96	476,493
a) Savings deposits	2,410,539.07		4,997
aa) Repayable on demand	2,238,084.29		3,908
bb) With agreed maturity or notice period	172,454.78		1,088
b) Other deposits	494,998,289.89		471,496
aa) Repayable on demand	414,577,447.63		396,138
bb) With agreed maturity or notice period	80,420,842.26		75,358
3. Liabilities evidenced by certificates		224,668,660.92	228,761
Other liabilities evidenced by certificates	224,668,660.92		228,761
4. Other liabilities		33,620,170.55	30,061
5. Prepaid expenses		2,519,562.12	3,649
6. Provisions		32,899,315.74	33,103
a) Provisions for severance payments	8,426,203.27		7,326
b) Provisions for pensions	668,022.00		640
c) Tax provisions	0.00		0
d) Other	23,805,090.47		25,137
7. Subscribed capital		10,000,000.00	10,000
Nominal amount	10,000,000.00		10,000
8. Capital reserves		55,915,661.65	55,916
a) Non-distributable (share premium)	35,082,987.22		35,083
b) Distributable	20,832,674.43		20,833
9. Retained income		48,096,218.77	48,096
a) Legal reserve	1,504,504.45		1,505
b) Other reserves	46,591,714.32		46,592
10. Liability reserve pursuant to section 57 (5) BWG		11,127,000.00	11,127
11. Distributable profit		52,734,395.92	45,229
a) Profit brought forward	40,229,087.89		31,294
b) Net profit for the year	12,505,308.03		13,935
TOTAL EQUITY AND LIABILITIES		985,385,703.90	964,741

	31 Dec. 2019 €	31 Dec. 2018 € '000
Below-the-line items		
1. Contingent liabilities		
Liabilities from guarantees and liabilities from the provision of collateral	15,881,018.31	13,444
2. Credit risks	53,416,846.50	67,487
3. Liabilities from trust transactions	24,282,776.94	63,823
4. Eligible capital pursuant to part 2 of EU Regulation no. 575/2013	170,299,774.05	162,883
f which: supplementary capital pursuant to part 2 title I chapter 4 of EU Regulation no. 575/2013: € 5.079.000,00 (previous year: € 6.772 thousand)		
5. Capital requirements pursuant to Art. 92 of EU Regulation no. 575/2013 (Total risk amount)	739,048,679.68	608,139
of which: capital requirements pursuant to 92 (1a-c) of EU Regulation no. 575/2013:		
a) Common equity tier 1 capital ratio	22.36%	25.67%
b) Tier 1 capital ratio	22.36%	25.67%
c) Total capital ratio	23.04%	26.78%
6. Foreign liabilities	88,580,120.75	92.378

INCOME STATEMENT
OF CAPITAL BANK – GRAWE GRUPPE AG

9. INCOME STATEMENT OF CAPITAL BANK – GRAWE GRUPPE AG FOR THE 2019 FINANCIAL YEAR

		2019 EUR	2018 TEUR
1. Interest and similar income		11,959,737.93	10,995
of which: from fixed-income securities	908,730.65		1,768
2. Interest and similar expenses		-594,270.53	-445
I. NET INTEREST INCOME		11,365,467.40	10,550
3. Income from securities and equity investments		2,412,657.68	2,425
a) Income from shares and other variable-yield securities	1,112,631.22		1,121
b) Income from equity investments	26.46		3
c) Income from shares in affiliated companies	1,300,000.00		1,300
4. Fee and commission income		58,522,391.89	58,219
5. Fee and commission expenses		-32,529,156.24	-31,366
6. Income/expenses from financial operations		-657,209.63	653
7. Other operating income		2,301,350.12	2,322
II. OPERATING INCOME		41,415,501.22	42,803
8. General and administrative expenses		-28,426,151.35	-27,040
a) Personnel expenses	-16,745,259.27		-16,429
aa) Wages and salaries	-13,043,513.69		-12,739
bb) Social security costs, compulsory and other contributions linked to pay	-2,158,387.81		-2,039
cc) Other social security expenses	-132,374.14		-157
dd) Post-employment and other employee benefit costs	-207,354.93		-262
ee) Additions to pension provisions	-28,162.59		-222
ff) Expenses for severance payments and contributions to operational pension funds for employees	-1,175,466.11		-1,010
b) Other expenses (administrative expenses)	-11,680,892.08		-10,611
9. Write-downs of assets reported under asset items 9 and 10		-606,333.54	-687
10. Other operating expenses		-342,347.87	-330
III. OPERATING EXPENSES		-29,374,832.76	-28,057

IV.	**OPERATING PROFIT**	12,040,668.46	14,746
11./12.	**Balance from the sale und the valuation of loans and securities and reserves for contingent liabilities**	3,622,409.53	2,737
13./14.	**Balance from the sale und the valuation of securities evaluated as financial assets and on shareholdings in affiliates companies**	4,532.00	-89
V.	**PROFIT FROM ORDINARY ACTIVITIES**	15,667,609.99	17,394
15.	**Income tax**	-3,043,575.00	-3,359
16.	**Other taxes not reported under item 15**	-118,726.96	-101
VI.	**PROFIT FOR THE YEAR**	12,505,308.03	13,935
17.	**Changes in reserves**	0.00	0
VII.	**NET PROFIT FOR THE YEAR**	12,505,308.03	13,935
18.	**Profit brought forward**	40,229,087.89	31,294
VIII.	**DISTRIBUTABLE PROFIT**	52,734,395.92	45,229

10. CAPITAL AND CAPITAL REQUIREMENT IN € '000

	CAPITAL BANK – GRAWE GRUPPE AG		
	2019	**2018**	**2017**
Tier 1 capital	165,221	156,111	140,600
Subscribed capital	10,000	10,000	10,000
Capital reserves	55,916	55,916	55,916
Retained income	48,096	48,096	48,096
Retained earnings	40,229	31,294	15,962
Liability reserve	11,127	11,127	11,127
Intangible assets	-147	-323	-501
Supplemental elements (Tier 2)	5,079	6,772	8,465
Hidden reserves pursuant to Section 57 (1) BWG	5,079	6,772	8,465
Revaluation reserve			0
Deductions	0	0	0
Eligible capital	170,300	162,883	149,065
Risk amount for			
Credit risk	652,107	526,658	572,313
CVA-Risk	14	0	0
Trading book	8,691	1,363	5,149
Foreign currency risk	0	2,382	5,029
Operational risk	78,237	77,736	76,456
Total risk amount	739,049	608,139	658,947
Total capital ratio	23.0%	26.8%	22.6%
Tier 1 capital ratio	22.4%	25.7%	21.3%
Common equity tier 1 capital ratio	22.4%	25.7%	21.3%

SCHEDULE OF ASSETS
OF CAPITAL BANK AS AT 31 Dez. 2019

11. CAPITAL BANK'S STATEMENT OF CHANGES IN EQUITY AS AT 31 DEC. 2019

in EUR	Cost				
Balance sheet item	**As at 1 Jan. 2019**	**Additions**	**Write-ups**	**Disposals**	**As at 31 Dec. 2019**
2. Public-sector debt instruments	11,213,245.00	0.00	2,543,700.00	497,755.00	13,259,190.00
3. b) Loans and advances to banks (securities)	1,487,775.00	0.00	-497,560.00	0.00	990,215.00
5. a) Loans and advances to customers (securities)	497,500.00	0.00	0.00	0.00	497,500.00
b) Bonds and other fixed-income securities	11,361,004.50	1,589,092.00	-2,046,140.00	2,008,814.00	8,895,142.50
6. Shares and other variable-yield securities	9,963,960.65	0.00	0.00	0.00	9,963,960.65
7. Equity investments	774,557.52	13,858.13	12,000,000.00	0.00	12,788,415.65
8. Shares in affiliated companies	24,007,255.30	0.00	-12,000,000.00	0.00	12,007,255.30
9. Intangible assets	1,842,825.12	15,384.48	0.00	0.00	1,858,209.60
10. Property and equipment	6,679,847.77	347,572.99	0.00	281,209.08	6,746,211.68
TOTAL FIXED ASSETS	67,827,970.86	1,965,907.60	0.00	2,787,778.08	67,006,100.38

Cumulative depreciation, amortisation and write-downs						Net carrying amounts	
As at 1 Jan. 2019	Additions	Write-ups	Transfers	Disposals	As at 31 Dec. 2019	Carrying amount 1 Jan. 2019	Carrying amount 31 Dec. 2019
7,7451.25	42,711.26		35,625.62	23.90	155,764.23	11,135,793.75	13,103,425.77
0.00	0.00		0.00		0.00	1,487,775.00	990,215.00
0.00	0.00		0.00		0.00	497,500.00	497,500.00
76,959.21	6,747.73	0.00	-35,625.62	11,119.66	36,961.66	11,284,045.29	8,858,180.84
-502,525.96	0.00	83,962.20	0.00		-586,488.16	10,466,486.61	10,550,448.81
109,417.47	0.00		0.00		109,417.47	665,140.05	12,678,998.18
300,000.00	0.00		0.00		300,000.00	23,707,255.30	11,707,255.30
1,520,264.23	190,751.11		0.00		1,711,015.34	322,560.89	147,194.26
5,637,169.60	387,843.97		0.00	276,363.96	5,748,649.61	1,042,678.17	997,562.07
7,218,735.80	628,054.07	83,962.20	0.00	287,507.52	7,475,320.15	60,609,235.06	59,530,780.23

STATEMENT OF CASH FLOWS

	31 Dec. 2019 €	31 Dec. 2018 € '000
Profit from ordinary activities	15,668	17,394
Non-cash items contained in the profit for the year		
Write-downs/write-ups of assets in the investment area	544	647
Loss/profit from the disposal of assets in the investment area	-41	-60
Allocation/reversal of risk provisions and other provisions	11.810	10.293
Other (non-) cash expense/income items	-2,942	-3,485
Cash flow from profit or loss	25,038	24,790
Change in assets and liabilities from operations following adjustments for non-cash components		
Loans and advances to banks	30,871	-16,766
Loans and advances to customers	-76,723	-22,019
Securities	6,769	47,830
Other assets from operating activities	-6,486	26,840
Deposits from banks	-5,918	-18,936
Deposits from customers	20,878	105,769
Liabilities evidenced by certificates	-4,092	-70,535
Other equity and liabilities from operating activities	-9,497	-9,627
Income taxes and other taxes	119	444
Cash flow from operating activities	-19,042	67,791
Cash inflow from the sale or redemption of		
financial assets	2,500	13,931
Intangible assets and property and equipment	42	58
Cash outflow due to investments in		
Financial assets	-1,603	-14,327
Intangible assets and property and equipment	-363	-587
Other changes	34	225
Cash flow from investing activities	609	-700

	31 Dec. 2019 €	31 Dec. 2018 € '000
Dividend payments	-5,000	0
Cash flow from financing activities	-5,000	0
Cash and cash equivalents at the end of the previous period	101,189	34,099
Cash flow from operating activities	-19,042	67,791
Cash flow from investing activities	609	-700
Cash flow from financing activities	-5,000	0
Cash and cash equivalents at the end of the period	77,756	101,189

Notes to the annual financial statements of Capital Bank – GRAWE Gruppe AG for the year ended 31 December 2018

A. GENERAL

Capital Bank operates as a partner for all capital market participants, including private monthly savers, small and medium-sized enterprises and institutional investors. Our range of services includes both investment and the procurement of capital.

Capital Bank is a subsidiary of HYPO-BANK BURGENLAND Aktiengesellschaft (referred to below as Bank Burgenland), which acts as the parent bank in the banking group. Key subsidiaries of Capital Bank include investments in Brüll Kallmus Bank AG (referred to below as Brüll Kallmus) and Security Kapitalanlage Aktiengesellschaft (referred to below as Security KAG).

In the 2019 financial year, Österreichische Post AG (hereinafter referred to as ÖPAG) acquired the majority shareholding in Brüll Kallmus by way of a capital increase. Following the successful completion of the ownership control procedure on 30 September 2019 by the European Central Bank, a capital increase amounting to €24,000,000 was carried out on 25 October 2019 (closing). As a result, 80% of Brüll Kallmus was acquired by ÖPAG, and Brüll Kallmus thus became part of the Austrian Post

Group. The previous sole owner of Brüll Kallmus, Capital Bank, now holds 20% of the shares.

The ultimate parent company that prepares the consolidated financial statements for the greatest number of entities is GRAWE-Vermögensverwaltung in Graz. The consolidated financial statements are published at the registered office of the ultimate parent company. The parent company that prepares the consolidated financial statements for the banking group of entities is Bank Burgenland, Eisenstadt. The consolidated financial statements of Bank Burgenland are submitted to the Eisenstadt regional court.

The previous year's figures compared to the 2019 financial year and the reporting date of 31 December 2019 are shown in brackets. The annual financial statements of Capital Bank have been prepared in accordance with the provisions of the Austrian Banking Act (BWG) as amended and also – where applicable – in accordance with the provisions of the Austrian Commercial Code (UGB). The statement of financial position and the income statement have been structured in accordance with the templates included in annex 2 to Article I of section 43 of the BWG.

B. ACCOUNTING POLICIES

The annual financial statements have been prepared in accordance with the principles of proper accounting and the general standard of providing a true and fair view of the company's assets, financial position and earnings.

In preparing the annual financial statements the principle of completeness has been observed.

The company was assumed to be a going concern for valuation purposes.

The principle of individual valuation was applied to assets and liabilities.

The principle of prudence was applied, in particular by only showing profits realised as at the balance sheet date. All identifiable risks and impending losses that arose in 2019 or in an earlier financial year have been recognised in the financial statements.

Estimates are based on a prudent assessment. If there was past experience from similar circumstances available that could be established statistically, the company tookk it into account when making estimates.

The accounting and valuation methods applied up until now have been retained, with the exception of the calculation of the flat-rate individual value adjust-

ment. During the course of the change in the core banking system in the banking group, the valuation methodology was standardised. The new method is based on statistically derived parameters that are part of the framework of the collateral approach.

Currency translation

Amounts in foreign currencies are converted at middle rates (reference rates of the European Central Bank) pursuant to section 58(1) of the Austrian Banking Act (BWG). Currency forward agreements have been measured using the forward rate as at the reporting date.

Securities

Securities held as current assets are valued strictly at the lower of cost or market.

Securities permanently dedicated to business operations (financial assets) are valued at the moderate lower of cost or market principle. The difference between higher cost and a lower repayment amount is written off on a pro rata basis over the remaining term.

Trading securities were measured at market value. The criteria for classifying securities as fixed assets was the use of the securities for generating returns over the long term and the existence of restrictions on the use or sale of the securities. Short positions

(for settlement/technical reasons) of securities are reported under other liabilities. The bank has made use of the option to amortise negative differences between cost and settlement amounts on a pro rata basis as permitted by section 56 (2) of the BWG.

When repurchasing issued own bonds, they are offset against the liabilities evidenced by certificates.

Loans and advances to banks and customers

As a matter of principle, loans and advances are stated at their nominal value. At each reporting date, the extent to which there is objective evidence of impairment of a financial asset or group of financial assets is assessed. Individual write-downs/general loan loss provisions or provisions for contingent liabilities are formed for identifiable credit risks.

As part of its credit monitoring activities, the Bank continuously checks whether default events exist for credit exposures and whether specific risk provisions have to be formed as a result. The Bank calculates a specific valuation allowance for defaulted and individually significant loans based on expected recoveries. For loans which are not significant on their own, the calculation of the specific loan loss provision is based on statistical assumptions and experience, taking existing collateral into account.

General loan loss provisions are established for all loans not classified as impaired, depending on their respective risk profile. The calculation takes into account historical default rates per rating level, taking into account existing collateral and parameters based on statistical assumptions and empirical values.

Clients have also hedged risks by entering into derivatives with Capital Bank. For its part, the bank has entered into matching transactions with Bank Burgenland that are the opposite of these hedges, forming a valuation unit together.

Equity investments, shares in affiliated companies

Equity investments and shares in affiliated companies are valued at cost unless there has been permanent impairment from sustained losses which makes devaluation necessary. Write-downs are implemented if the reasons for the unscheduled depreciation or amortisation no longer apply.

The investment in Brüll Kallmus was accounted for using the moderate lower of cost or market principle despite starting losses as at 31 December 2019 and was thus retained. The value of the investment is subject to an annual review.

Intangible fixed assets and property and equipment

Buildings and office and operating equipment are measured at cost and reduced by depreciation. Depreciation is recognised on a straight-line basis. Low-value assets are written off in full in the year of acquisition.

It is valued at acquisition or production cost less scheduled depreciation or amortisation. Depreciation rates for immovable assets ranged from 6.66% to 10% p.a., and for movable assets from 5% to 33.3% p.a. A full year's depreciation is recognised for additions in the first half of the financial year, but only half of a year's depreciation for additions in the second half of the financial year.

Intangible fixed assets solely comprise purchased software. This software is amortised on a straight-line basis at rates of 20% to 33.3% per annum.

Other assets

The other assets are recognised at cost or, in the event of any permanent impairment, at the lower fair value as at the reporting date. Underlying investments included in the other assets that form a valuation unit with liabilities evidenced by certificates are measured at fair value.

Liabilities

Liabilities evidenced by certificates include items for which the settlement amount depends on the price of the defined underlying instrument. Derivatives and collateral instruments were, in accordance with corporate law, balanced in valuation units that are formed between underlying investments and liabilities evidenced by certificates if the documented hedging purpose was available and the material and formal conditions were met. All risks from the underlying investments were taken into account via the calculations of the redemption amount of the liabilities evidenced by certificates and were therefore hedged. The effectiveness of the hedging relationship is measured using the dollar offset method. The formation of valuation units results in the fact that the assets and derivatives stated in various items and the liabilities evidenced by certificates with which the valuation units were formed are accounted for at their fair market value.

The remaining liabilities are recognised at their settlement amount.

Provisions

All identifiable risks and impending losses are taken into account in accordance with legal requirements when measuring the provisions.

All provisions for social capital (provisions for pensions, severance payments and anniversary bonuses) are calculated in accordance with IAS 19 – Employee Benefits – using the projected unit credit method.

The calculation of the need for provisions for severance payments and anniversary bonuses was carried out in accordance with AVÖ 2018-P Rechnungsgrundlagen für die Pensionsversicherung, taking into account the currently valid principles of the International Financial Reporting Standards.

On the basis of high-quality corporate bonds, a long-term capital market interest rate of 0.85% (1.55%) was used to value the pension provisions on the reporting date. The long-term capital market interest rate of 0.90% (1.80%) was used to calculate the provisions for severance compensation and anniversary bonuses. Future salary trends were assumed to be 4.00% (4.10%) and future pension increases 2.00% (2.00%). Deductions for fluctuations depending on the length of service were taken into account when calculating the provision for anniversary bonuses.

The assumed retirement age was 60 years for women and 65 years for men. The interest expense arising when assessing the necessary settlement amount of the provisions is included in personnel expenses.

The bank made use of the election option available under section 57 (1) of the BWG in the 2019 annual financial statements in the same way as in the previous year.

Derivatives

Derivatives are accounted for in accordance with the principle of the individual valuation method. Valuation units are formed with banking book derivatives if there is a documented purpose regarding the hedging of an underlying transaction (assets, liabilities along with pending transactions) and if the material and formal conditions are met.

The underlying transactions used for hedging are customer transactions on the assets side and securities in equity as well as own issues on the liabilities side. Hedges are based on the individual transactions (micro hedging relationships). The risks to be collateralised relate to the interest rate risk and the currency risk. They are managed primarily through swaps and currency forward agreements. The hedging period is essentially identical to the term of the underlying transaction.

Effectiveness is measured almost exclusively in a simplified manner (critical term match), since all parameters for the underlying transaction and the hedging transaction (in particular the term, nominal value and interest) which determine the extent of the hedged value changes are identical but contrary with the hedging relationships used. This is seen as an indicator of a completely effective hedging relationship. For the remaining hedging relationships the effectiveness is determined using the dollar offset method.

Capital guarantees are accounted for as derivatives. With these products, the relevant beneficiary under the guarantee has the guarantee that the amount available for disbursement after the binding period has expired will not be lower than the total amount of amounts paid in by the taxpayer plus the government premiums credited for this taxpayer pursuant to section 108g of the EStG.

Products with a capital guarantee from the pension provisions and fund-linked life insurance are presented as short-put options in the relevant guaranteed fund. The three essential unobservable internal input factors are the estimated lapse rate of existing contracts, the long-term (target) volatilities of the guarantee funds and the estimated expected return of the guarantee funds. The lapse rates used in the model are estimates by the experts from Grazer Wechselseitige Versicherung AG, which are continuously validated in Group Risk Control through

the development of premium sums. The lapse rate used is 5% p.a. (5% p.a.) for the products from the future pension plan, or 6% p.a. (6% p.a.) for those from unit-linked life insurance. The target volatilities reported by the fund management are continuously reviewed by Group Risk Control using rolling historical volatilities. The range is between 5.5 and 8% (5.5 to 8%). The expected fund returns are calculated by the Xentis system and, after deduction of all costs for products from the future pension plan, lie within a range of 126 to 231 (2018: 162-225) base points or 55 to 167 (2018: 144-176) base points for those from unit-linked life insurance; calculations by Security KAG. The valuation is based on Monte-Carlo modelling. The market values for the derivatives are calculated using the PMS software application.

In the course of accounting, the market values for maturity ranges with equivalent criteria (closing year, contract term) are formed. Due to the imparity principle, positive fair values are not taken into account in the financial statements.

C. NOTES TO THE STATEMENT OF FINANCIAL POSITION

MATURITY STRUCTURE

Loans and advances/deposits not repayable on demand Total for banks and customers (€ '000)	Loans and advances		Liabilities	
	31 Dec. 2019	31 Dec. 2018	31 Dec. 2019	31 Dec. 2018
Up to 3 months	135,694	148,095	41,353	4,399
More than 3 months to 1 year	180,693	96,109	32,773	21,104
More than 1 year to 5 years	152,034	153,470	17,131	46,203
More than 5 years	9,155	11,949	0	4,635
Total	477,575	409,623	91,257	76,341
Other assets and liabilities (in € '000)				
up to 1 year	7,573	6,823	29,845	26,790
more than 1 year	104,201	99,061	3,775	3,271
Total	111,774	105,884	33,620	30,061

The liabilities with a term of up to one year amount to €545.9 million (€496.5 million).

Of the bonds and other fixed-income securities, a nominal amount of €20.8 million (€5.0 million) is due in the year following the balance sheet date.

Assets and liabilities denominated in foreign currencies in € millions	31 Dec. 2019	31 Dec. 2018
Total amount of assets in foreign currency	136.0	133.5
Total liabilities in foreign currency	48.7	35.9

Securities

The total securities portfolio including pro rata accrued interest amounted to €189.1 million (€201.1 million) at the end of the year. Of this total, an amount of €88.7 million (€103.2 million) was accounted for by underlying investments in liabilities evidenced by certificates with which valuation units were formed. Basic investments in the amount of €21.0 million (€37.8 million) are pledged in favour of the issue buyers.

in € '000 [1]	listed	of which in fixed assets	of which in current assets
2019			
Bonds and other fixed-income securities	50,971	9,468	41,503
Shares and other variable-yield securities	13,469	0	13,469
2018			
Bonds and other fixed-income securities	41,030	11,942	29,088
Shares and other variable-yield securities	21,987	0	21,987

[1] The deduction of the valuation allowance under section 57 has already been taken into account in the values of assets 5 to 8.

The securities included in assets 5 to 8 and admitted to trading on the stock exchange are broken down as follows:
As in the previous year, the bonds did not include any assets of a subordinated nature.

The distinction between financial assets and current financial assets is based on section 198 (2) and (4) of the Austrian Commercial Code. Financial instruments that are intended to serve the business operations on a permanent basis are allocated to financial assets when they are first acquired.

Fixed assets include listed securities with a nominal value of €22.4 million (€23.3 million), which are valued according to the moderate lower of cost or market principle.

Fixed-income securities held as fixed assets are included in the following items:

- in A2, Public-sector debt instruments, in the amount of €13.2 million (€11.2 million);

- in A3, Loans and advances to banks, in the amount of €1.0 million (€1.5 million);

- in A5, Bonds and other fixed-income securities, in the amount of €9.5 million (€11.9 million);

- in A6, Shares and other variable-yield securities, in the amount of €10.6 million (€10.5 million).

In the case of securities admitted to trading on the stock exchange and carried at cost, which are not allocated to financial assets, the difference between the higher market value and the book value is €1.8 million (€1.9 million).

The Bank's fixed assets as at 31 December 2019 included securities with a carrying amount (including pro rata interest) of €34.2 million (€35.1 million). The difference between higher acquisition costs and the repayment amount is €0.2 million (€0.2 million) in accordance with section 56(2) of the Austrian Banking Act (BWG). The difference between the carrying amount and the higher repayment amount is €0.1 million (€0.1 million) in accordance with section 56(3) of the Austrian Banking Act.

The loans and advances to customers included €4.1 million (€2.5 million) relating to loans and advances evidenced by certificates but not admitted to trading on an exchange.

The loans and advances to banks included €10.3 million (€3.1 million) relating to loans and advances evidenced by certificates but not admitted to trading on an exchange. Loans and advances to banks in the amount of €58.7 million (€62.8 million) stem from the assignment of basic investments for liabilities evidenced by certificates to a collateral trustee.

The company maintains a securities trading book pursuant to Part 3, Title I, Chapter 3 of EU Regulation No. 575/2013 and items in the trading book are valued at market prices.

The total securities portfolio did not contain any subordinated securities (€0.0 million) as at the reporting date.

Capital Bank presents capital guarantees in the banking book as derivatives, particularly in connection with government-aided pension provision (PZV) in the amount of €101.6 million (€98.6 million) and the unit-linked life insurance in the amount of €63.9 million (€58.1 million). Under the arrangements for capital guarantees in the PZV product and fund-linked life insurance, the associated market risk is transferred from the pension or insurance provider to Capital Bank. With this the relevant beneficiary under the guarantee has the guarantee that the amount available for disbursement after the binding period has expired will not be lower than the total amount of amounts paid in by the taxpayer plus the government premiums credited for this taxpayer pursuant to section 108g of the EStG. The three essential input factors for determining the market value are the estimated cancellation rate for existing contracts, the long-term (target) volatilities of the guarantee funds and the estimated expected return from the guarantee funds. The valuation is based on Monte-Carlo modelling. The provision was increased by €0.7 million to €4.6 million as of 31 December

2019 (€3.9 million) due to the calculation for negative market values of the capital guarantees in connection with the government-aided pension provision (PZV) and the unit-linked life insurance.

There were no trust fund deposits as at 31 December 2019.

Equity investments and shares in affiliated companies

LIST OF EQUITY INVESTMENTS

Equity investments and shares in affiliated companies	Consoli-dation[1]	Share capital in € '000	Share-holding	Equity in € '000[2]	Profit for year in € '000[3]	Annual financial state-ments [4]
Brüll Kallmus Bank AG	E	30,000	20%[5]	41,427	-26,244	2019
Security Kapitalanlage Aktiengesellschaft	V	4,362	100%	55,626	8,377	2019
Corporate Finance – Grawe Gruppe GmbH	V	1,000	100%	1,154	177	2019
CENTEC.AT Softwareentwicklungs und Dienstleistungs GmbH	V	35	100%	167	5	2019
BK Immo Vorsorge GmbH	N	35	100%	3,416	893	2019
CB Family Office Service GmbH	V	35	100%	140	-2	2019

1) E = at equity, V = fully consolidated and N = not consolidated.

2) Equity calculated in accordance with section 229 of the Austrian Commercial Code (UGB) including reserves after tax.

3) Pursuant to section 231 (2) no. 22 UGB, profit/loss for the year is figured before changes in reserves.

4) The annual financial statements 2019 are provisional financial statements.

5) The share in BK has been reduced from 100% to 20% in the course of transferring the ownership to ÖPAG.

As at 31 December 2019, the Bank directly held at least 20% of the shares in the following companies: The reported equity investments and shares in affiliated companies are not admitted to trading on a stock exchange.

As at 31 December 2019, there were no reciprocal equity investments.

Securitised and unsecuritised loans and advances to affiliated companies and companies in which the Bank has a participating interest are included in the following items:

By balance sheet item	Affiliated companies		Equity investments	
in € '000	31 Dec. 2019	31 Dec. 2018	31 Dec. 2019	31 Dec. 2018
Loans and advances to banks	136,108	159,324	0	0
Loans and advances to customers	0	0	1,509	0
Total	136,108	159,324	1,509	0

Deposits from affiliated companies and companies in which the Bank has a participating interest are included in the following items:

By balance sheet item	Affiliated companies		Equity investments	
in € '000	31 Dec. 2019	31 Dec. 2018	31 Dec. 2019	31 Dec. 2018
Deposits from banks	1,843	6,064	0	0
Deposits from customers	2,560	2,827	65	0
Total	4,403	8,891	65	0

There are no transactions of the Company with related companies or persons which were significant or concluded under conditions which are not customary in the market.

Since 1 January 2019, there has been an extended consolidated tax group for VAT purposes between Capital Bank and Bank Burgenland.

Capital Bank is part of a corporate group as defined by section 9 of the Austrian Corporation Tax Act (KStG), the parent is Bank Burgenland.

The disclosures pursuant to section 431 ff CRR are the responsibility of the parent bank, Bank Burgenland.

Fixed assets

The breakdown of fixed assets and the changes in fixed assets during the reporting year are presented in the statement of changes in fixed assets (see Annex I to the notes). As at the reporting date, the bank held neither developed nor undeveloped land as part of its property and equipment, as was also the case in the previous year.

Obligations from the use of property and equipment not shown in the statement of financial position will amount to €1.0 million (€1.0 million) in the following year and a total of €6.0 million (€5.7 million) in the years 2020 to 2024.

Provisions

The provision for severance payments in the amount of €8.4 million (€7.3 million) is shown in the statement of financial position. The requirement for the pension provision was calculated at €0.7 million (€0.6 million).

Other provisions primarily include provisions for claims amounting to €5.6 million (€7.3 million), for capital guarantees of €4.6 million (€3.9 million), for unused holidays of €1.0 million (€0.9 million), for other personnel expenses of €4.9 million (€5.1 million) and for commission payments of €5.0 million (€5.2 million).

Capital Bank received distributions in the 2017 to 2019 financial years from investments made by the Bank, some of which also include loans and advances to customers. Insofar as it was legally possible to allocate the amounts distributed to customer portfolios on the one hand and bank portfolios on the other, this has since been done. To what extent further distributed sums ultimately remain with the Bank or are to be allocated to customer portfolios in accordance with the agreements reached in each case, and if so, at what amount, cannot yet be precisely quantified on the reporting date. There are still legal uncertainties here, in particular proceedings at the investment level have not yet been concluded in the respective jurisdictions.

Based on the information available and taking a security discount into account for the distribution amounts not yet allocated to customer portfolios on the one hand and bank portfolios on the other, Capital Bank estimated what amount of the distribution sums are to be allocated in any event to the Bank on the reporting date. The amount in excess of this was recorded as a provision.

Long-term provisions, in particular provisions for warranty payments, are recognised and discounted at their settlement amount and using the Euro Swaps Curve.

Equity capital

The company's share capital remained unchanged at €10.0 million and was divided into 1,376,030 registered shares.

The capital reserves result from payments and deposits made by the shareholder.

The retained income of the company encompass statutory and voluntary reserves as well as profits generated in previous years, reduced by dividend disbursements.

The Management Board proposes to distribute a dividend of €5.0 million (€5.0 million) to the owner, Bank Burgenland, from the distributable profit of €52.7 million (€45.2 million) and to carry the remaining distributable profit forward to new account.

Liabilities evidenced by certificates

The liabilities evidenced by certificates are certificates of underlying investments. They form valuation units with assets and derivative transactions stated in various items on the statement of financial position (underlying investments) and have no final maturity (open end).

Deferred taxes

The deferred tax assets at the reporting date were formed for temporary differences between the tax and corporate valuation for the following items:

In € '000	31 Dec. 2019	31 Dec. 2018
Property and equipment	247	147
Shares and other variable-yield securities	4,807	4,422
Write-downs	25,065	24,807
Long-term staff provisions	6,054	5,358
Long-term provisions	4,251	3,150
Total difference amount	40,423	37,884
Tax losses carried forward	0	0
Resulting deferred taxes as at 31 Dec. (25%)	10,106	9,471

Deferred taxes were capitalised in full in the year under review and recognised in profit or loss. The balance of deferred tax assets existing as at 1 January 2016 was capitalised in full and will be distributed over 5 years by forming a deferred income item pursuant to section 906 (33f) of the Austrian Commercial Code.

Deferred taxes developed as follows:

In € '000	2019	2018
As at 1 Jan.	9,471	8,805
Change recognised in profit or loss	633	665
Change not affecting net income	2	0
As at 31 Dec.	10,106	9,471

D. FURTHER INFORMATION ON THE STATEMENT OF FINANCIAL POSITION

Other assets included underlying instruments for liabilities evidenced by certificates amounting to €103.8 million (€100.1 million).

Other liabilities include liabilities to the tax authorities of €4.8 million (€2.4 million) and securities clearing liabilities of €4.8 million (€6.4 million). Expenses that were only payable after the reporting date largely consisted of personnel expenses of €4.9 million (€4.4 million) and various other administrative expenses. Most of the other liabilities of €33.6 million (€30.1 million) are due within one year. The other liabilities include liabilities due to affiliated companies amounting to €16.0 million (€14.7 million).

The credit risks reported below the line on the balance sheet related to loans that had not yet been drawn amounting to €53.4 million (€67.5 million).

As in the previous year, there were no genuine repurchase agreements in the year under review.

Capital

The following table shows the eligible own funds of Capital Bank pursuant to Part 2 of EU Regulation No. 575/2013.

in € '000	31 Dec. 2019	31 Dec. 2018
Subscribed capital	10,000	10,000
Open reserves	115,139	115,139
Retained earnings	40,229	31,294
Tier 1 capital	165,368	156,443
Eligible supplementary capital	5,079	6,772
Less a deduction for curtailment	-147	-323
Supplementary capital	4,932	6,449
Eligible capital	170,300	162,883

Other

Securities with a carrying amount of €5.4 million (€10.2 million) are deposited as an arrangement deposit. Securities with a carrying amount of €40.5 million (€47.5 million) were held in a blocked account as security for use of the refinancing option via the tender procedure at the ECB. In addition, the bank held cover assets for pension provisions at the amount of €0.3 million (€0.3 million).

Collateral for transactions with derivatives was provided in the amount of €0 thousand (€0 thousand) and €50 thousand (€1,480 thousand) was taken.

The contingent liabilities include guarantees and financial commitments amounting to €15.9 million (€13.4 million).

E. INCOME STATEMENT DISCLOSURES

A breakdown of income by geographical markets as required pursuant to section 64 (1) no. 9 of the Austrian Banking Act (BWG) has not been included because the geographical markets do not differ materially from the location of the bank organisation.

The loan processing fees amounting to €1.3 million (€0.9 million) stated in the interest income were deferred as in the previous year to reflect the term of the loan.

The interest and similar expenses item includes negative interest amounting to €0.2 million (€0.1 million) from deposits at the Austrian National Bank.

Income from securities and equity investments included €1.3 million (€1.3 million) relating to dividends from affiliated companies.

The net commission income is essentially composed of profit from securities transactions amounting to €25.2 million (€28.3 million). A provision for pending losses of €1.0 million (€1.0 million) was accounted for in the net commission income associated with the government-aided pension provision (PZV) and unit-linked life insurance in the 2019 financial year.

Gains from currency valuation and disposal gains from securities transactions amounting to €7.1 million (€5.3 million) are offset in the income/

expenses from financial operations item by exchange losses from this area of €7.8 million (€4.7 million).

Other operating income largely comprised income from service level agreements amounting to €1.9 million (€1.8 million) and income from the reversal of provisions amounting to €0.02 million (€0.1 million).

Expenses for severance payments and contributions to occupational pension funds included occupational pension fund expenses of €90 thousand (€81 thousand).

The allowances for losses on loans and advances and additions to provisions for contingent liabilities and credit risks were adjusted as permitted by section 57 (1) of the BWG. The provision formed in the previous year in the amount of €0.3 million for negative market values of capital guarantees in connection with government-aided pension provision (PZV) and unit-linked life insurance was also released in this item.

The item “taxes on income” comprises current income tax for the financial year and deferred taxes of €1.7 million (€1.7 million).

The total return on assets is 1.3% (1.4%) and is defined as the quotient of the annual net profit after taxes divided by the total assets as at the reporting date.

F. OTHER DISCLOSURES

Derivative financial instruments

As of the reporting date 31 December 2019, the following forward transactions were still outstanding:

AS YET UNSETTLED FORWARD TRANSACTIONS AS AT THE REPORTING DATE

31 Dec. 2019		**Notional amount**
€ '000	**Banking book**	**Trading book**
Volume Total	297,388	0
OTC products	297,388	0
Exchange-traded products	0	0
Interest rate	35,236	0
OTC products	35,236	0
Exchange-traded products	0	0
Foreign currencies and gold	96,710	0
OTC products	96,710	0
Exchange-traded products	0	0
Other	165,441	0
OTC products	165,441	0
Exchange-traded products	0	0

31 Dec. 2018		**Notional amount**
€ '000	**Banking book**	**Trading book**
Volume Total	287,744	0
OTC products	282,020	0
Exchange-traded products	5,724	0
Interest rate	38,516	0
OTC products	32,792	0
Exchange-traded products	5,724	0
Foreign currencies and gold	92,515	0
OTC products	92,512	0
Exchange-traded products	0	0
Other	156,716	0
OTC products	156,716	0
Exchange-traded products	0	0

Positive fair value		Negative fair value	
Banking book	Trading book	Banking book	Trading book
4,026	0	5,578	0
4,026	0	5,578	0
0	0	0	0
141	0	149	0
141	0	149	0
0	0	0	0
1,060	0	621	0
1,060	0	621	0
0	0	0	0
2,825	0	4,808	0
2,825	0	4,808	0
0	0	0	0

Positive fair value		Negative fair value	
Banking book	Trading book	Banking book	Trading book
3,923	0	7,446	0
3,923	0	7,399	0
0	0	0	0
165	0	246	0
165	0	198	0
0	0	47	0
416	0	1,865	0
416	0	1,865	0
0	0	0	0
3,342	0	5,336	0
3,342	0	5,336	0
0	0	0	0

The capital guarantees reported in the category "Other" were presented as a banking book product from 31 December 2017 in accordance with the regulatory reclassification because there is no longer any intent to trade.

Currency forward agreements and swaps were measured using the rates published by the ECB for the reporting date taking into account the interest rates for the currencies involved and the residual maturities.

The fair value of derivatives in hedging relationships was €0.7 million (€-0.5 million) as of the reporting date 31 December 2019.

Market values in the amount of €1.0 million (€0.4 million) are recorded in the other assets and €0.3 million (€0.9 million) in the other liabilities for currency forward agreements that form part of a valuation unit with the bank's own issues or other underlying transactions.

Negative fair values that are not covered by an equivalent positive fair value from an underlying transaction in a hedging relationship are taken into account by recognising a provision pursuant to AFRAC opinion 15: "Derivatives and hedging instruments (UGB)" for imminent losses from pending forward transactions. Such a provision amounting to €232 thousand (€958 thousand) was formed as at 31 December 2019.

Accrued interest on derivative transactions is accounted for in the same way as the underlying transactions for valuation units. Contracts are measured using recognised financial methods. The market values were calculated based on present value and from obtaining corresponding confirmations from business partners.

Statement of Cash Flows

The cash flow statement shows the composition of and changes in cash and cash equivalents during a financial year and is broken down into operating activities, investing activities and financing activities. Capital Bank has presented the cash flow from operating activities using the indirect method (see Appendix II to the Notes).

Other

In the course of the spin-off and takeover agreement of 11 June 2019 between Brüll Kallmus Bank AG and Capital Bank regarding the spin-off of certain assets, shares in the balance sheet item other assets in the amount of €3.4 million and linked notes in the balance sheet item liabilities evidenced by certificates in the amount of €3.4 million were spun off from Brüll Kallmus and transferred to Capital Bank retroactively as of 1 January 2019. In addition, two forward exchange transactions, which were in a valuation unit with the other equity interests and the linked notes, with a nominal value of €1.8 million

were spun off from Brüll Kallmus and transferred to Capital Bank.

Deposit protection

Pursuant to section 8 (1) of the Deposit Guarantee Schemes and Investor Compensation Act (ESAEG), Capital Bank, as a deposit-taking institute (CRR institute) with its headquarters in Austria, belongs to the uniform protection scheme in accordance with section 1 (1) (1) of the ESAEG. On the basis of the transitional provisions of section 59 (3) of the Deposit Guarantee Schemes and Investor Compensation Act, the function of the protection scheme was to act as a deposit guarantee for Banken und Bankiers Ges.m.b.H. until 31 December 2018. Each protection scheme must set up a deposit protection fund consisting of available financial resources in the amount of at least 0.8 per cent of the sum of the covered deposits of the member institutions as target funding. The amount to be contributed depends on the amount of the covered deposits and on previously determined risk factors (this is called a risk-based contribution calculation).

As at 1 January 2019, the task of the sectoral protection scheme will be transferred to Einlagensicherung Austria G.m.b.H. (ESA). This will not result in any changes for depositors. The agendas of the protection schemes of the professional associations of banks and bankers and of Volksbanks will also be taken over by the Unified Protection Scheme on this date.

G. SIGNIFICANT EVENTS AFTER THE REPORTING DATE

In the period between the end of the reporting year 2019 and the preparation of the annual financial statements, no events took place on which separate reports would have to be made.

H. MANDATORY DISCLOSURES ON EXECUTIVE BODIES AND EMPLOYEES

During the 2019 financial year, the bank had an average of 143 (145) salaried and 5 (5) non-salaried employees (weighted number of part-time employees).

As in the previous year, the loans and advances to customers as at 31 December 2019 did not include any loans to members of the Management Board. There are loans to Supervisory Board members amounting to €28 thousand (€35 thousand).

The loans were granted at normal market conditions.

Expenses for severance payments and pensions, including the allocation to provisions, amount to €1.1 million (€1.2 million) for active members of the Management Board and senior executives and €406 thousand (€274 thousand) for other employees.

The expense for pensions to former other employees amounts to €8 thousand (€20 thousand).

Remuneration to active members of the Management Board amounted to €1.5 million (€1.4 million). The members of the Supervisory Board did not receive any remuneration during the financial year under review.

The following persons served as members of the Management Board and the Supervisory Board during the financial year:

Management Board

Christian Jauk, MBA MAS
CEO

Mag. Constantin Veyder-Malberg
Deputy Chairman

Wolfgang Dorner
Member of the Management Board

Supervisory Board

Dr. Othmar Ederer
Chairman of the Management Board of GRAWE-Vermögensverwaltung
Chairman of the Supervisory Board

Mag. Klaus Scheitegel
Chairman of the Management Board of Grazer Wechselseitige Versicherung AG
Deputy Chairman of the Supervisory Board

Dipl. Techn. Erik Venningdorf
Member of the Management Board of GRAWE Vermögensverwaltung
Member of the Supervisory Board

Dr. Franz Hörhager
Member of the Supervisory Board

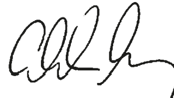
Employee representatives:

Rudolf Laudon
Harald Greimel

Graz, 2 March 2020

CAPITAL BANK – GRAWE GRUPPE AG

Christian Jauk, MBA MAS
CEO



Mag. Constantin Veyder-Malberg
Member of the Management Board

Wolfgang Dorner, CIA
Member of the Management Board

AUDIT CERTIFICATE

CAPITAL BANK – GRAWE GRUPPE AG, Graz
Report on the audit of the annual financial statements as at 31 December 2019

Report on the annual financial statements

We have audited the annual financial statements of Capital Bank, Graz, consisting of the statement of financial position as at 31 December 2019, the income statement for the financial year ending at this reporting date, and the notes.

In our opinion, which is based on the findings of our audit, the financial statements comply with legal requirements and give a true and fair view of the financial position as at 31 December 2019 and of its financial performance for the financial year ending on said date, in agreement with Austrian statutory company and banking regulations.

Basis for the audit opinion

We completed our audit in accordance with EU Regulation No 537/2014 (referred to below as the Regulation of the Appendix to the Audit Report) and with the Austrian principles of orderly accounting. These standards require application of the International Standards on Auditing (ISA). Our responsibilities under these regulations and standards are described in further detail in the “Responsibilities of the auditor

for auditing the annual financial statements" section of our audit certificate. We are independent of the company in accordance with Austrian company, banking and professional laws and have fulfilled our other professional obligations in accordance with these requirements. In our view, the audit evidence we obtained provides a satisfactory and suitable basis for our audit opinion.

Key Audit Matters

Key audit matters are those matters that, in our professional judgement, were of most significance in our audit of the annual financial statements for the financial year. These matters were considered in association with our audit of the annual financial statements as a whole and for the purposes of forming our audit assessment, and we do not give any separate audit assessment on these matters.

We have identified the following particularly important audit issues:
- Change in the core banking system
- Impairment of loans and advances to customers
- Recognition and measurement of capital guarantees

Change of the core banking system

The risk for the financial statements
In June 2019, the Bank changed its core banking system and migrated its accounting-relevant data to the core banking system ARCTIS/VB91 (new system), operated by the General Computing Centre. Due to the complexity associated with a change of the core banking system and the comprehensive effects on banking operations, potentially incorrect data transmission poses risks with regard to the accuracy of the financial information in the annual financial statements.

Our audit approach

- We checked the data migration to the new system during course of the project. Before the go-live date, we collected the documentation on the project management, the procedure for testing the data transfer and the planned migration steps, including the quality assurance measures planned by the bank, and assessed whether these processes were suitable for preventing, detecting and correcting errors in the course of the data migration and thus ensuring a complete and correct migration of all the data.

- To audit the data migration, we appointed IT specialists to the audit team who have special expertise and experience in system migration. In addition, we have identified controls that are essential to the Bank's accounting with regard to the migration of accounting-related data and have repeated these controls to ensure that the data was migrated correctly.

- With regard to the general ledger account balances, we have reconciled the balances under the old system with the balances under the new system's chart of accounts. Furthermore, we checked the correct and complete transfer of the securities holdings (nostro) to the new system on the migration date. As part of the credit audit, we also verified the correct transfer and updating of individual value allowances in the new system.

- After the go-live, we carried out walkthroughs of key business processes and key controls to determine how the changes and adjustments were implemented. We tested individual key processes/controls (automatic interest calculation, overdue counter). We also assessed the adequacy of the temporary workarounds and measures still in place until the regular process was fully implemented.

- In the course of the audit, we also determined whether the valuation principles and methods used by the Bank to date are still functioning in the new system.

Impairment of loans and advances to customers

The risk for the financial statements
Loans and advances to customers are shown in the statement of financial position – after deduction of risk provisions – in the amount of €429 million and are mainly spread over Lombard loans and real estate financing.

The Management Board describes the process for monitoring credit risk and the procedure for determining risk provisions in Chapter II "Accounting policies" in the notes and in the "Credit risk" section of the risk report in the management report.

The Bank reviews whether there is any risk of default as part of its credit monitoring and whether any specific provisions for loan losses or provisions for liabilities issued have to be created as a result.

For defaulted and individually significant loans, the Bank calculates a specific valuation allowance on the basis of expected recoveries. For defaulted loans with a commitment of less than €500 thousand, an automatic specific valuation allowance is determined based on statistical assumptions and empirical values. Portfolio-based loan loss provisions are established for all loans not classified as impaired depending on their respective risk profile (rating level). The calculation takes into account historical default rates per rating level, existing collateral values and parameters based on statistical assumptions and empirical values.

The risk for the financial statements results from the fact that the risks of default are not recognised in good time and that the calculation of provisioning for impairment losses is based to a significant extent on assumptions and estimates which give rise to discretionary scope and estimation uncertainties with regard to the level of provisioning for impairment losses.

Our audit approach

- We have documented the processes for granting, monitoring and risk provisioning for loans and assessed whether these processes are suitable for identifying a risk of default and adequately depicting the recoverability of loans and advances to customers. We tested the relevant key controls for design, implementation and, on a random basis, for effectiveness.
- We used a random sample of loans to examine whether there is a risk of default and whether adequate provisioning for impairment losses had been formed. In the process, we analysed the determination of the specific loan loss provision and, in particular, reconstructed the value in test cases. The selection procedure for determining the sample was risk-oriented on the basis of a statistical selection procedure.

- In examining the automatic specific loan loss provisions and the portfolio-based loss provisions, we assessed the methodology used and the parameters taken into account in this. To this end, we reviewed

whether the assumptions are appropriate based in particular on analyses of back-testing and validations carried out. We have tracked the calculation of provisions by means of spot checks.

- Finally, we assessed whether the disclosures in the Notes to the annual financial statements are appropriate for determining the allowance for losses on loans.

Recognition and measurement of capital guarantees

The risk for the financial statements
As at 31 December 2019, the Bank issued capital guarantees for products of "government-aided pension provision (PZV)" and "unit-linked life insurance" (FLV) with a guaranteed amount of €165.5 million. The Bank allocates these capital guarantees to the banking book as derivative financial instruments.

The presentation of these derivatives and their ongoing valuation are described in the Notes in Chapter II "Accounting policies" and Chapter III "Notes to the balance sheet" and in the management report under the section "Market risk".

The valuation of these instruments is based on financial mathematical calculation models. The parameters used depend on future developments on the capital markets and the estimated cancellation rates for existing contracts.

The risk for the financial statements results from the fact that the determination of the market values of the capital guarantees is based on assumptions and estimates which give rise to discretionary scope and estimation uncertainties with regard to the amount of the provision for impending losses from negative market values.

Our audit approach

– We recorded the processes for monitoring, accounting and valuation of capital guarantees and assessed whether these processes are suitable for ensuring an appropriate risk assessment and determination of the market value. We tested the relevant key controls for design, implementation and, on a random basis, for effectiveness.
– We evaluated the valuation model, the planning assumptions and the parameters used with the involvement of our valuation specialists. The valuation model used was reconstructed and it was examined whether it is suitable to adequately determine the risk from these capital guarantees. The assumptions taken into account in the model – primarily the lapse rates, interest rate components and volatilities – were evaluated and assessed by comparison with standard market benchmarks to determine whether the assumptions used to determine interest rates and volatilities are within an appropriate range.

- The calculation of the provisions for negative market values and their depiction in the annual financial statements was simulated in test cases.

- Finally, we assessed whether the disclosures in the Notes on valuation and accounting as well as the disclosures in the risk report of the Management Report on capital guarantees are complete and appropriate.

Responsibility of the legal representatives and the Supervisory Board for the financial statements

The management is responsible for preparing the annual financial statements and for the fact that these provide a true and accurate picture of the company's financial and earnings position in accordance with Austrian generally accepted accounting principles and statutory company and banking requirements. The management is also responsible for the internal controls it deems necessary in order to enable the preparation of annual financial statements that are free from intentional or unintentional material misstatements.

When preparing the annual financial statements, the management of the company is responsible for assessing the company's ability to continue its corporate activities as a going concern, for stating any facts associated with continuing its corporate activities as a going concern as relevant, and for applying the accounting principles to continuation of its corporate

activities as a going concern, unless the management of the company intends either to liquidate the company or to discontinue its corporate activities, or has no other realistic alternative to this.

The Supervisory Board is responsible for monitoring the company's accounting process.

Responsibilities of the auditor for auditing the annual financial statements

Our objectives are to obtain sufficient certainty as to whether the annual financial statements as a whole are free from material misstatements whether as a result of inaccuracy or through fraud, and to award an audit certificate which contains our audit opinion. Adequate certainty is a high degree of certainty, but not a guarantee, that any audit of the financial statements carried out in accordance with the Regulation of the Appendix to the Audit Report (AP-VO) and in accordance with Austrian generally accepted auditing standards, which require the application of ISAs, will always reveal a material misrepresentation if one has been made. Misstatements may be the result of fraud or a mistake and are considered to be material if either individually or as a whole there could be a reasonable expectation that these will influence the economic and financial decisions of readers made based on these annual financial statements.

As part of any audit in accordance with the Regulation of the Appendix to the Audit Report and in

accordance with Austrian generally accepted auditing standards we exercise due diligence and maintain a critical approach during the entire audit.

The following provisions also apply:

- We identify and assess the risks of intentional or unintentional material misstatements in the financial statements, plan audit actions as a response to these risks, implement these and obtain audit evidence that forms an adequate and appropriate basis for our audit opinion. The risk that material misstatements resulting from fraudulent action will not be uncovered is higher than those resulting from inaccuracies, as fraudulent action may involve fraudulent collusion, forgeries, intentional incompleteness, misleading statements or bypassing of internal controls.

- We gain an understanding of the internal control system relevant to the audit in order to plan audit activities that are appropriate under the given circumstances. However, these activities are not intended to represent a judgement of the effectiveness of the company's internal control system.

- We assess the appropriateness of the accounting methods applied by the company management and the tenability of the estimated values provided by the company management in the accounts and associated statements.

- We draw conclusions on the appropriateness of the application of the accounting principle of continuation of the company's activities as a going concern by the company management, and on whether there is any material uncertainty associated with events or facts which could raise significant doubts regarding the company's ability to continue as a going concern based on the audit evidence obtained. If we conclude that there is material uncertainty, we are under an obligation to refer to the associated statements in the annual financial statements in our audit certificate, or to amend our audit certificate if these statements are inappropriate. We draw our conclusions based on the audit evidence obtained by the date of our audit certificate. Future events or facts may result, however, in the company discontinuing its corporate activities.

- We assess the overall presentation, structure and content of the annual financial statements, including the notes, and judge whether the annual financial statements convey the underlying transactions and events in a manner that provides a picture that is as true and accurate as possible.

- We hold discussions with the Supervisory Board inter alia on the planned scope and schedule for the statutory audit and on significant audit findings, including any significant defects in the internal control system that we identify during our statutory audit.

- Based upon the circumstances which we have discussed with the Supervisory Board, we determine those circumstances that were most significant for the audit of the annual financial statements for the financial year and are therefore the audit circumstances that are of particular importance. We describe these circumstances in our Audit Certificate, unless statutes or other legal regulations prohibit public disclosure of the relevant facts, or in extremely rare cases if we determine that a circumstance should not be communicated in our Audit Certificate as it can be reasonably expected that the negative consequences of any such communication would exceed the benefits of this to the public interest.

Other statutory and legal requirements

Report on the Management Report

Pursuant to Austrian company law, the Management Report must be audited in order to review whether it is consistent with the annual financial statements and whether it has been prepared in accordance with the applicable legal requirements.

The company's management is responsible for preparing the Management Report in accordance with Austrian company law.

We prepared our audit in line with professional principles related to conducting audits of management reports.

Opinion
In our opinion, the Management Report has been prepared in accordance with the applicable legal requirements and is consistent with the annual financial statements.

Declaration
We have not identified any material misstatements in the Management Report based on the findings from the audit of the annual financial statements and the understanding acquired of the company and its environment.

Additional information according to Article 10 of the Regulation of the Appendix to the Audit Report
We were elected as auditors by the Annual General Meeting on 9 April 2018 and were appointed by the Supervisory Board on 9 April 2018 to audit the financial statements of the Company for the financial year ending 31 December 2019.

On 8 March 2019, we were elected for the financial year ending 31 December 2020, and on 12 March 2019, we were commissioned by the Supervisory Board to audit the financial statements.

We have been the auditors of the Bank's financial statements without interruption since the financial statements as at 31 December 2005.

We hereby declare that the audit opinion in the section "Report on the Financial Statements" is consis-

tent with the additional report to the Supervisory Board pursuant to Article 11 of the Regulation of the Appendix to the Audit Report.

We declare that we have not provided any prohibited non-audit services (Article 5 (1) of the Regulation of the Appendix to the Audit Report) and that we have maintained our independence from the audited company in the performance of the audit.

We provided the following services, which were not disclosed in the annual financial statements or the management report, in addition to the audit of the financial statements for the audited company and for the companies controlled by it:

- Preparation of tax returns (corporate income tax and value added tax).

Auditor responsible for the engagement
The auditor responsible for the audit of the financial statements is Mag. Georg Blazek.

Vienna, 2 March 2020

KPMG Austria GmbH
Wirtschaftsprüfungs- und Steuerberatungsgesellschaft

CAPITAL BANK – GRAWE GRUPPE AG SUB-GROUP

The following financial statements in accordance with UGB/BWG for the subgroup of CAPITAL BANK – GRAWE GRUPPE AG are intended to provide the reader with information on the financial performance of Capital Bank and its subsidiaries.

12. CAPITAL BANK – GRAWE GRUPPE AG SUBGROUP
CONSOLIDATED STATEMENT OF FINANCIAL POSITION AS AT 31 DECEMBER 2019

ASSETS		31 Dec. 2019 €		31 Dec. 2018 € '000
1. Cash on hand and balances at central banks		77,756,146.02		101,289
2. Public-sector debt instruments eligible as collateral for central bank funding				
Public-sector debt instruments and similar securities		17,682,967.35		17,175
3. Loans and advances to banks		201,908,216.99		241,576
4. Loans and advances to customers		413,146,107.28		337,325
5. Bonds and other fixed-income securities		50,971,062.21		46,765
6. Shares and other variable-yield securities		138,691,999.67		149,752
7. Equity investments[1)]		12,678,998.18		672
of which: in banks	12.004.215,00		4	
8. Shares in affiliated companies		35,000.00		35
9. Intangible assets in fixed assets		177,596.86		388
10. Property and equipment		3,350,061.47		3,537
11. Other assets		114,277,697.26		111,518
12. Prepaid expenses		787,019.94		1,106
13. Deferred tax assets		10,765,961.03		10,032
TOTAL ASSETS		1,042,228,834.26		1,021,170
Below-the-line items				
1. Foreign assets		372,032,973.10		369,293
2. Fund assets of managed investment funds		5,674,102,010.73		4,942,505

[1)] the at-equity approach of bank99 AG (formerly Brüll Kallmus Bank AG) was not taken into account, as this is done at the group level of HYPO-BANK BURGENLAND Aktiengesellschaft

EQUITY AND LIABILITIES		31 Dec. 2019 €		31 Dec. 2018 € '000
1. Deposits from banks		16,217,694.45		20,300
2. Deposits from customers		495,508,948.47		475,064
a) Savings deposits	2,410,539.07		4,997	
b) Other deposits	493,098,409.40		470,067	
3. Liabilities evidenced by certificates		224,668,660.92		232,193
Other liabilities evidenced by certificates	224,668,660.92		232,193	
4. Other liabilities		38,837,855.50		35,791
5. Prepaid expenses		2,840,870.70		4,323
6. Provisions		45,190,720.48		45,621
a) Provisions for severance payments	9,415,144.46		8,430	
b) Provisions for pensions	668,022.00		640	
c) Tax provisions	46,294.32		0	
d) Other	35,061,259.70		36,551	
7. Subscribed capital		65,915,661.65		65,916
8. Generated capital		153,048,422.09		141,962
9. Minority interests		0.00		0
TOTAL EQUITY AND LIABILITIES		1,042,228,834.26		1,021,170
Below-the-line items				
1. Liabilities from guarantees and liabilities from the provision of collateral		15,881,018.31		13,444
2. Credit risks		53,416,846.50		67,487
3. Liabilities from trust transactions		24,282,776.94		63,823
4. Eligible capital pursuant to part 2 of EU Regulation no. 575/2013		215,179,274.76		199,797
of which: supplementary capital pursuant to part 2 title I chapter 4 of EU Regulation no. 575/2013: €5,079,000.00 (previous year: €6,772 thousand)				
5. Capital requirements pursuant to Art. 92 of EU Regulation no. 575/2013 (Total risk amount)		777,333,522.16		638,969
of which: capital requirements pursuant to 92 (1a-c) of EU Regulation no. 575/2013:				
a) Common equity tier 1 capital ratio		27.03%		30.2%
b) Tier 1 capital ratio		27.03%		30.2%
c) Total capital ratio		27.68%		31.3%
6. Foreign liabilities		89,680,885.47		97,029

13. CAPITAL BANK - GRAWE GRUPPE AG SUBGROUP
CONSOLIDATED INCOME STATEMENT FOR THE 2019 FINANCIAL YEAR

		2019 €		2018 € '000
1. Interest and similar income		12.024.352,98		11.115
of which: from fixed-income securities	426.999,00		1.903	
2. Interest and similar expenses		-840.775,65		-828
I. NET INTEREST INCOME		11.183.577,33		10.288
3. Income from securities and equity investments		2.326.912,82		2.325
a) Income from shares and other variable-yield securities	2.026.886,36		2.017	
b) Income from equity investments	26,46		7	
c) Income from shares in affiliated companies	300.000,00		300	
4. Fee and commission income		93.445.893,16		93.775
5. Fee and commission expenses		-48.668.850,67		-47.984
6. Income/expenses from financial operations		-657.888,46		653
7. Other operating income		3.868.966,64		3.034
II. OPERATING INCOME		61.498.610,82		62.090
8. General and administrative expenses		-39.830.514,50		-35.846
a) Personnel expenses	-23.995.168,76		-23.141	
aa) Wages and salaries	-19.403.319,36		-18.427	
bb) Social security costs, compulsory and other contributions linked to pay	-2.793.292,87		-2.808	
cc) Other social security expenses	-166.883,13		-194	
dd) Post-employment and other employee benefit costs	-319.809,63		-399	
ee) Additions to pension provisions	0,00		-222	
ff) Expenses for severance payments and contributions to operational pension funds for employees	-1.311.863,77		-1.091	
b) Other expenses (administrative expenses)	-15.835.345,74		-12.706	
9. Write-downs of assets reported under asset items 9 and 10		-800.225,92		-972
10. Other operating expenses		-344.074,86		-391
III. OPERATING EXPENSES		-40.974.815,28		-37.210

		2019 €	2018 € '000
IV.	**OPERATING RESULT**	20.523.795,54	24.880
11./12.	**Balance from the sale und the valuation of loans and securities and reserves for contingent liabilities**	3.160.673,92	2.544
13./14.	**Balance from the sale und the valuation of securities evaluated as financial assets and on shareholdings in affiliates companies**	822.286,23	-582
V.	**PROFIT OR LOSS ON ORDINARY ACTIVITIES**	24.506.755,69	26.841
15.	**Income tax**	-5.881.995,02	-5.817
16.	**Other taxes not reported under item 15**	-95.843,92	-124
VI.	**PROFIT FOR THE YEAR**	18.528.916,75	20.900
17.	**Changes in reserves**	-7.400.000,00	-6.205
	of which: appropriation to the liability reserve	0,00	0
VII.	**NET INCOME FOR THE YEAR**	11.128.916,75	14.695
18.	**Profit brought forward**	40.459.905,92	32.241
VIII.	**DISTRIBUTABLE PROFIT**	51.588.822,67	46.937
19.	**Minority interests' share of profit for the year**	0,00	0
IX.	**NET PROFIT OR LOSS FOR THE YEAR [1)]**	51.588.822,67	46.937

[1)] the at-equity approach of bank99 AG (formerly Brüll Kallmus Bank AG) was not taken into account, as this is done at the group level of HYPO-BANK BURGENLAND Aktiengesellschaft

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Published by
CAPITAL BANK – GRAWE GRUPPE AG
Burgring 16
A-8010 Graz
Tel.: +43.316.8072.0
Fax: +43.316.8072.390
office@capitalbank.at
www.capitalbank.at

Vienna Branch:
Palais Esterházy
Wallnerstraße 4
A-1010 Vienna
Tel.: +43.1.31614
Fax: +43.1.31614.11
office.wien@capitalbank.at

Salzburg Branch:
Linzergasse 4
A-5020 Salzburg
Tel.: +43.662.870810
Fax: +43.662.870810.2517
office.salzburg@capitalbank.at

Kitzbühel Branch:
Kitzbühler Hof, Franz-Reisch-Str. 1
A-6370 Kitzbühel
Tel.: +43.5356.66309
office.kitzbuehel@capitalbank.at

Klagenfurt Branch:
Kardinalschütt 9
A-9020 Klagenfurt am Wörthersee
Tel.: +43.463.908118-0
office.klagenfurt@capitalbank.at

Responsible for the content
Christian Jauk, MBA MAS,
Mag. Constantin Veyder-Malberg,
Wolfgang Dorner, CIA,
Thomas Ortner, MSc, Mag.(FH) Harald Hofherr

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Texts: Christian Ortner, Capital Bank
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