V Outlook

1 Economic conditions

1.1 Global economic trends

Despite numerous political risks and escalating trade disputes, the global economy remains robust. However, signs are emerging of a diminishing pace of growth as the economic cycle matures. At present, global economic growth is primarily being driven by the US economy, where tax relief had provided noticeable stimulus for companies and consumers alike in 2017. By contrast, the eurozone and China have seen an economic slowdown.

Germany and many other countries in the eurozone are likely to see a further tailing off of economic growth. The simmering trade dispute with the United States and the ongoing deadlock in the Brexit negotiations between the EU and United Kingdom have dampened appetite for investing activity in the countries that are affected. The Chinese government may potentially fend off a further slowdown by introducing tax relief and a state spending program. Another uncertainty factor for China is the continued threat that punitive tariffs may be imposed by the US government. Although the provisional agreement reached between Washington and Beijing in the trade dispute can be viewed positively, there remains substantial uncertainty about whether the talks will lead to a lasting détente in trade relations between the two countries.

Going forward, global economic output is expected to weaken in 2019, because the effect of government stimulus will gradually diminish and China will switch to a slower growth trajectory. The expansion of the global economy in 2018 is therefore likely to be confirmed at approximately 3.6 percent and will probably slow to around 3.5 percent in 2019.

Monetary policy remains expansionary worldwide. While the ECB has announced the end of its net purchases of bonds, it is continuing with its policy of negative interest rates. The Federal Reserve System, the US central bank, is responding to the late stage of the economic recovery and higher inflation rates in the United States with a steady but gradual departure from expansionary measures. With benchmark rates rising in the United States, there is a widening gap between interest rates in the eurozone and those on the other side of the Atlantic.

In early October 2018, the price of crude oil climbed to a high of US$ 86 per barrel. Since then, various positive news items on the supply side have combined to help oil prices fall again. The recent drop in oil prices indicates that energy prices will make a smaller contribution to inflation in the long term. However, diminishing capacity reserves could have a countervailing effect.

Looking ahead, inflationary pressure is likely to be limited worldwide on the whole. The global inflation rate will probably decrease slightly from around 3.9 percent in 2018 to approximately 3.6 percent in 2019.

1.2 Trends in the USA

Following the buoyant growth of the US economy in 2018, the current employment situation and the positive economic climate provide an encouraging outlook for 2019. Sentiment indicators are at a high level, suggesting that employment will continue to increase in the year ahead. However, jobs are likely to be added at a slightly slower rate due to the growing shortage of skilled workers. Consumer spending will therefore lose a little of its momentum but will nevertheless remain a key economic driver in 2019.

Losing the majority in the House of Representatives has made it harder for the US President to govern. The associated domestic political risks are illustrated by the drastic government shutdown. It can be assumed that the hardened political fronts will unsettle consumers and business.

In these conditions, the US economic growth rate is forecast to fall from approximately 2.9 percent in 2018 to around 2.5 percent in 2019. At the same time, the unemployment rate will continue to go down, from roughly 3.9 percent in 2018 to around 3.7 percent in 2019.

Following the sharp drop in energy prices in November 2018, the United States is expected to see a generally flatter inflation trajectory. Currently, an average inflation rate in the region of 2.2 percent is projected for 2019.

1.3 Trends in the eurozone

The economic climate in the eurozone deteriorated further at the end of 2018. The survey of European purchasing managers in December again pointed to a decline in economic activity in the eurozone. The index covering the industrial and service sectors fell to its lowest level in more than four years. In France, the 'yellow vest' protests caused sentiment indicators to plummet. The escalating protests across France have put a big question mark over the French President's plans for further reform. But Germany too faces a gloomier economic climate, although this should not come as too much of a surprise. The UK parliament has failed to approve the agreement on the United Kingdom's departure from the EU, so the risk of a disorderly Brexit has risen sharply.

Nonetheless, the European job markets are still relatively robust. The number of people in work went up by 0.2 percent in the third quarter, although this was a slightly smaller increase than in previous periods. The eurozone's total economic output in the period July to September was generated by a working population of 158.3 million people in the eurozone. This is the highest number ever recorded for the eurozone.

Overall, the risks to future growth in the eurozone are still regarded as largely in balance. However, a shift toward downside risks is observable due to the continued uncertainty stemming from geopolitical factors, the threat of protectionism, vulnerabilities in emerging markets, and volatility in financial markets.

Against this backdrop, economic growth is forecast to fall to around 1.2 percent in 2019, compared with 1.8 percent in 2018. A slower improvement in the prospects for the labor market now looks likely due to the softening of the economy. The unemployment rate is predicted to decrease to 7.7 percent this year. There are still marked differences between the members of the eurozone. Unemployment rates will remain the highest in large countries such as Spain and Italy. Only smaller reductions are likely to be seen in Germany and the Netherlands, where the job markets are very tight.

Domestic inflationary pressure will remain moderate in the eurozone. Current forecasts for 2019 are predicting an inflation rate in the vicinity of 1.7 percent.

1.4 Trends in Germany

The German economy has passed its peak, with growth weakening markedly over the course of 2018 to reach 1.5 percent. In fact, macroeconomic activity contracted in the third quarter of 2018. Trade restrictions and punitive tariffs continue to be a major risk factor. The uncertainty surrounding Brexit and the problems besetting the Macron government in France are putting a particular strain on the economic climate. Consequently, industrial companies' expectations regarding business prospects have slipped back into negative territory for the first time since spring 2016. However, the situation in other sectors still looks a lot rosier. The construction industry is especially benefiting from the boom in the real-estate market.

Economic growth is likely to diminish further over 2019 as a whole. Germany's economic output is expected to rise by around 1.1 percent in 2019.

In 2018, the number of unemployed people fell by 190,000, which was the sharpest drop since 2011. However, the rate of decrease tailed off over the course of the year. Given the continuing rise in employment and economic output, albeit at a slower rate, the positive trend seen in the labor market in recent years is set to continue in 2019. However, the supply-side shortages in the labor market and the diminishing rate of growth in economic output mean that it will be less pronounced. Germany's unemployment rate for 2019 is predicted to fall further, reaching around 4.9 percent.

The rate of inflation has recently been relatively high at 2.3 percent, due in no small part to the rise in prices for heating oil and petroleum. Since its high at the beginning of October 2018, the oil price has already fallen by around 20 percent. Consequently, the average inflation rate for 2019 is expected to be in the region of 1.9 percent.

1.5 Trends in the financial sector

For some years, the financial sector has faced considerable pressure in terms of both adjustment and costs caused by the need to comply with regulatory reforms and implement structural change to adapt to competitive conditions.

The regulatory measures introduced since the financial crisis have had a range of objectives, including restructuring of the supervisory architecture and improved capital and liquidity adequacy in order to make the financial sector more resilient in the event of a crisis. A further objective is to ensure that the risks arising from the business activities in the financial industry are not borne by the public sector and thus the taxpayer.

However, there is always a possibility that European banks could be more heavily impacted by supervisory measures as a result of differences in the way that the rules are applied at international level.

Further information on the regulatory environment can be found in section 5.1.2 of the opportunity and risk report.

In response to these regulatory requirements, banks have reduced their leverage over the last few years and substantially bolstered their risk-bearing capacity by improving capital and liquidity adequacy.

However, in addition to the regulatory environment described above, new competitors with approaches based on the use of data and technology are presenting the financial sector with the challenge of scrutinizing its existing business models, adapting them as required, and substantially improving its efficiency by digitalizing business and IT processes. The corresponding capital investment is initially likely to push up costs in the industry before the anticipated profitability gains can be realized.

Efforts to address the challenges described above will be made more difficult in 2019 by what is expected to still be a comparatively low level of nominal interest rates. This will be accompanied by a relatively flat yield curve and will prevent any significant increase in margins in interest-related business.

This statement is based on the current assessment of the monetary policy pursued by the ECB, which did stop its bond buying program in January 2019 but may continue to reinvest maturing paper. The emergence of a slow tightening and thus normalization of monetary policy would potentially be supported by a cautious raising of the ECB's deposit rate. However, if banks – particularly those in countries on the eurozone's periphery – were to continue to have access to long-term refinancing operations, there would be a countervailing expansionary effect.

In 2018, by contrast, the US Federal Reserve ended the policy of quantitative easing that it had introduced in the wake of the financial crisis and has gradually been raising interest rates with the objective of keeping the US economy on a growth trajectory while ensuring price stability. Implementation of further interest-rate hikes is currently predicted for 2019.

The growth that continues to be expected in large swathes of the global economy should also provide a boost for the financial position and financial performance of the European financial sector.

However, the potential impact of uncertain political and economic trends for the economic position of banks and insurance companies should not be ignored. Further information on macroeconomic risk factors can be found in section 5.1.3 of the opportunity and risk report.

2 Financial performance

Key features of the 2019 financial year alongside a continuation of the tough market and competitive conditions will include the further evolution of the DZ BANK Group's strategy in virtually all entities.

According to the planning for 2019, total assets will end the year somewhat higher compared with the figure as at the end of 2018. This planning is based on the forecast of growth, especially in the BSH, DZ BANK, TeamBank, and R+V operating segments, which will have a corresponding impact on the balance sheet. However, the level of total assets will also reflect the countervailing effect from the planned contraction of the portfolios of loans and advances in the DVB operating segment (sale and transfer of the land transport and aviation finance businesses) and the VR LEASING operating segment.

In these circumstances, **profit before taxes** is likely to increase slightly compared with 2018 and be at the lower end of the long-term target range of €1.5 billion to €2.0 billion.

Financial performance will be impacted by the persistently low level of interest rates. The future financial performance of the DZ BANK Group could be subject to risks arising from the political and economic climate outlined above. This is monitored continuously and factored into planning and management.

In 2019, it is anticipated that **net interest income** including **income from long-term equity investments** will remain steady overall, although there could be some pressure on income in the interest-rate-sensitive business models within the DZ BANK Group, due in part to the continuation of low interest rates.

Once again, **net fee and commission income** is projected to make a very hefty positive contribution to the earnings of the DZ BANK Group in 2019.

Based on the predicted growth in the volume of assets under management and the associated volume-related income, the UMH and DZ PRIVATBANK operating segments will again be responsible for a substantial portion of the net fee and commission income.

Any lasting uncertainty in capital and financial markets could have a negative impact on confidence and sentiment among retail and institutional investors, thereby depressing net fee and commission income.

Gains and losses on trading activities in 2019 are predicted to be at a far higher level than those in 2018.

Customer-driven capital markets business in the DZ BANK operating segment will probably provide particular impetus in 2019.

The primary prerequisite for a steady level of net gains under gains and losses on trading activities is considered to be a stable financial and capital markets environment.

Net gains under **gains and losses on investments** are predicted to make a modest contribution to profit before taxes in 2019 because the non-recurring items recognized in 2018 will not be repeated.

Other gains and losses on valuation of financial instruments in 2019 are projected to improve substantially compared with 2018.

Volatility in capital markets and especially the widening of credit spreads on securities from government issuers could have a negative impact on the forecast gains and losses.

Net income from insurance business is expected to rise in 2019. Based on the prediction of steady gains and losses on investments held by insurance companies, it is currently assumed that a further increase in gross premiums in the different divisions will lead to a higher level of net income from insurance business overall.

Exceptional events in financial and capital markets, changes in underwriting practices, or potential changes in the regulatory requirements faced by insurers may adversely affect the level of net income expected to be earned from insurance business.

Starting from a gratifyingly low level in 2018, expenses for **loss allowances** are likely to return to normal levels in 2019 and change in line with the lending portfolio, the targeted volume of new business, and the long-term standard risk costs.

The effects of possible political and macroeconomic developments on credit markets could have a detrimental impact on loss allowances.

Administrative expenses are predicted to be slightly higher in 2019 than they were in 2018. While administrative expenses in most operating segments will remain comparatively steady or decrease, it is likely that this item will rise in the UMH operating segment in view of the planned growth and capital spending requirements.

The **cost/income ratio** for the DZ BANK Group is likely to fall in 2019 as a result of the expected year-on-year increase in income and an almost unchanged level of expenses. As before, the DZ BANK Group will be focusing its energies on managing costs and generating growth in the operating business.

Regulatory RORAC, the risk-adjusted performance measure based on regulatory risk capital, will hold steady compared with 2018 on current assessments.

3 Liquidity and capital adequacy

Based on the position in the year under review and the funding measures planned for 2019, the DZ BANK Group predicts that it will again be able to ensure an appropriate level of economic and regulatory **liquidity adequacy** in 2019.

Further information on liquidity adequacy can be found in sections 6.2 and 6.3 of the opportunity and risk report.

As matters currently stand, the DZ BANK Group's **capital adequacy** will continue to be assured for 2019 from both economic and regulatory perspectives; that is to say, it will continue to have at its disposal the available internal capital necessary to cover the risks associated with the finance business and other risks arising from the group's business operations.

Further information on capital adequacy can be found in sections 7.2 and 7.3 of the opportunity and risk report.

Over the last few years, the DZ BANK Group has strengthened its capital base from its own resources – by retaining profits and reducing risk – and by implementing a capital increase in 2015. In 2019, a high priority will once again be given to strengthening the capital base.

4 Operating segments in detail

4.1 DZ BANK

Economic conditions at international level are expected to deteriorate in 2019. DZ BANK's earnings growth may thus be held back, particularly in connection with unresolved trade disputes and a renewed flare-up of uncertainty in the eurozone.

Moreover, the protracted period of low interest rates combined with pressure to innovate by further digitalizing products and processes may hinder a more positive financial performance.

In view of this worsening of market conditions and the challenges presented by the growing use of digital technologies, DZ BANK AG launched the 'Verbund First 4.0' strategic program in 2018 with the aim of improving profitability.

In 2019, **profit before taxes** will be roughly on a par with 2018, although the figure for the year under review was influenced by various one-off items.

The main one-off items with a positive impact on profit before taxes in 2018 were the disposal of securities and the high level of net reversals of loss allowances.

Net interest income (excluding income from long-term equity investments) in 2019 is predicted to be above the 2018 level, due to positive factors such as the growth and intensification of corporate banking.

Income from long-term equity investments will probably go up in 2019 because of the favorable assessment of profitable growth opportunities for the main management units.

Net fee and commission income is expected to be slightly lower in 2019 than it was in 2018. The steady volume-related growth of transaction banking is having a positive impact on net fee and commission income, although a countervailing effect is expected in the shape of a fall in fees and commissions from brokerage with retail customers.

The net gain under **gains and losses on trading activities** is projected to rise, reflecting the strategic growth targets defined for the customer business. Both the institutional customer business and the retail customer business are believed to still offer opportunities for growth in spite of the tough market conditions.

The stepping up of the cross-selling approach, focusing on risk management products and capital market products, should enable market potential to be harnessed, particularly in corporate customer business. As a result, the further consolidation of marketing activities in line with the corporate strategy should lead to additional operating income in the capital markets business.

Gains and losses on investments will probably deteriorate significantly in 2019 compared with 2018 because of the one-off item arising on the disposal of securities in the liquidity pool.

Expenses for **loss allowances** will probably rise to a normal level in 2019. Reversals of allowances in the year under review were not included in the planning. No net reversals are anticipated in 2019. The planning for 2019 is based on the expected loss from the lending business, particularly in corporate banking.

In all probability, **administrative expenses** will hold steady in 2019, having fallen sharply in 2018. The increase in costs was reduced by implementing the synergies decided upon in connection with the merger and by lowering project costs. Strategic cost targets are being defined as part of 'Verbund First 4.0' in order to achieve a sustained reduction in administrative expenses.

From the current perspective, it is anticipated that the **cost/income ratio** will improve in 2019 owing to the positive earnings expectations and an only small increase in administrative expenses.

Regulatory RORAC will probably rise in 2019 based on slightly higher capital requirements and income.

4.2 BSH

Although economic growth is expected to slacken in 2019, the same cannot be said of house-building. Construction activity is predicted to continue to grow at a fast pace this year. The umbrella trade organizations for the construction industry anticipate nominal revenue growth of 5.5 percent in 2019, compared with 6.5 percent in 2018. They also estimate that 315,000 homes will be completed (2018: 300,000). But that still does not match the level of demand, which various studies put at 350,000 to 400,000 homes per year. The predicted increase is restricted to the construction of apartments, which continues to boom. Construction of classic owner-occupied housing, however, will stagnate at the 2018 level. The biggest barrier to residential construction remains the lack of available building plots, but the shortage of construction capacity is also increasingly becoming an issue. In terms of financing, at least, the barriers remain low thanks to the persistently favorable interest-rate environment. BSH, a specialist in home finance, will also benefit from these conditions.
In its core home finance business, BSH expects earnings to be maintained at the high level seen in 2018. As regards home savings, the second core business at BSH, new business is predicted to be slightly below the 2018 level because of the continuing challenges presented by low interest rates and significant regulatory requirements.

BSH is anticipating a significant fall in **profit before taxes** in 2019, largely because of a decrease in net interest income.

The low interest rates are likely to have a substantial detrimental impact on income in 2019. Based on these expectations, **net interest income** is forecast to decline this year.

Net fee and commission income is predicted to remain at the prior-year level in 2019, assuming a more or less steady level of new business in the core home savings business.

With regard to **loss allowances**, BSH will continue to benefit from Germany's good economic performance and low unemployment rate. As a consequence, loss allowances will – adjusted for one-off items in 2018 – hold steady in 2019 despite the marked expansion in non-collective lending business in previous years.

Administrative expenses will be marginally higher in 2019, a consequence of strategic projects and action plans in connection with the further development of the home savings and home finance core businesses. Strict cost discipline and savings will help to limit the increase.

From the current perspective, the **cost/income ratio** is likely to rise as a result of the lower net interest income.

Regulatory RORAC will probably be well down because of the slightly higher capital requirements and the aforementioned fall in profit before taxes.

4.3 DVB

The year under review was another challenging one for the DVB operating segment.

In 2018, DVB continued to focus on the international transport business, which can be broken down into the shipping, aviation, and land transport segments.

As well as macroeconomic and sector-specific factors, the evolution of the business model was influenced by the decisions described below.

- DZ BANK and DVB have been examining all the strategic options for DVB since the start of 2018. Based on this analysis and in consultation with DZ BANK, DVB entered into contracts for the sale and transfer of the land transport business (contract signed on December 21, 2018) and the aviation finance business, including aviation asset management and aviation investment management (contract expected to be signed in the first half of 2019).

- The non-core asset (NCA) strategy for scaling back non-strategic businesses in a way that preserves value was initiated at the start of the reporting year. As at December 31, 2018, the volume of the NCA portfolio stood at €3.0 billion (December 31, 2017: €4.7 million).

In view of the adopted strategy, the objectives for 2019 are as follows:

- Systematically, purposefully, and successfully implement the sale and transfer contracts by the applicable transaction completion dates
- Examine the strategic options for the future positioning of DVB's continuing shipping finance business and of the NCA portfolio
- Ensure adequate profitability, with ongoing review and adjustment of the cost and workforce structures in the business model on the basis of restructuring activities
- Further reduce portfolio risk, in particular by rigorously implementing the NCA strategy and thereby continuing with the successful scaling back of the NCA portfolio that got under way in 2018.

Overall, DVB's projected financial performance will be influenced by conditions in the maritime market, the sale of the land transport finance and aviation finance businesses, and the examination of further strategic options. The bank therefore expects that its **profit before taxes** will at best be at break-even in 2019, with a sharp fall in both income and administrative expenses.

4.4 DZ HYP

In 2018, the political and economic risks at global level were reflected in the German economy, which was therefore unable to sustain the relatively high growth rates of previous years. The real increase in economic output in 2018 was 1.5 percent, the slowest rate registered since 2013. According to forecasts prepared by DZ HYP, the German commercial real estate market is nonetheless likely to remain stable in 2019. From today's vantage point, the high volume of capital chasing real estate investment opportunities coupled with the continuation of Germany's great economic strength and the ECB's expansionary monetary policy will once again result in high turnover in the real estate market. However, the end of the bond buying program and a potential interest-rate hike might have a detrimental effect. The robust labor market will ensure that demand for office space is maintained at a sound level. Higher wages will give a boost to retailers and help consumers pay housing rents, which continue to increase. The downward pressure on yields is therefore likely to remain significant and risk premiums could continue to go down.

Reflecting the portfolio, **net interest income** will probably be slightly higher than the 2018 level. Real estate lending is expected to increase slightly.

The spreads in government financing are expected to deviate only minimally from their level in 2018. **Other gains and losses on valuation of financial instruments** are therefore expected to be in neutral territory in 2019, having amounted to a net loss in 2018.

Expenses for **loss allowances** are predicted to return to normal levels in 2019. Net reversals of loss allowances, as seen in previous years, are not expected in the year ahead.

Administrative expenses will be considerably lower than in 2018. This is primarily due to a reduction in costs in connection with the merger of WL BANK and DG HYP to become DZ HYP, which has now been completed in legal terms.

As a result of the net effect of various opposing factors, **profit before taxes** for 2019 is expected to be slightly higher than in 2018 thanks to the sustained success of DZ HYP's business.

The **cost/income ratio** is projected to improve year on year for the reasons specified above.

Regulatory RORAC is also likely to improve due to the increase in profit before taxes forecast for 2019.

Details of the merger of WL BANK and DG HYP to create DZ HYP, which was completed in legal terms in 2018, can be found in section 2.4 of the group management report.

4.5 DZ PRIVATBANK

Although the economy of the eurozone will lose momentum in the medium term, economic sentiment remains in positive territory despite the adverse factors.

The inflation rate in the eurozone will probably not exceed the ECB's target of 2 percent in the next few years.

Net interest income will hold steady in 2019, even though interest rates remain low.

In 2019, **net fee and commission income** is predicted to rise thanks to the good performance of the private banking and fund services businesses. The main value driver is fund volume, which is likely to grow substantially – particularly in the case of third-party funds. The assets under management in private banking will also rise because of falling outflow rates.

Gains and losses on trading activities are forecast to hold steady in 2019.

Administrative expenses are expected to rise by only a modest amount thanks to the ongoing efforts to manage efficiency and effectiveness. The increase will be due not only to the sustained growth of costs relating to regulatory requirements but also to high levels of capital expenditure.

From today's perspective, the positive trend in income combined with the absence of one-off items (impairment of goodwill and customer relationships in 2018) is likely to mean that **profit before taxes** goes up significantly in 2019.

The **cost/income ratio** and **regulatory RORAC** are both forecast to improve substantially.

4.6 R+V

In the opinion of R+V, the 2019 financial year will continue to be shaped by the challenging conditions. The market environment will remain very tough from any number of perspectives, including political issues, regulation, low interest rates, economic conditions, and consumer behavior.

Customers hold DZ BANK, the Volksbanken Raiffeisenbanken cooperative financial network, and the latter's insurance specialist, R+V, in very high standing due to their financial strength, resilience, fair advice, good service, and tailored solutions.

In 2017, R+V launched its 'Wachstum durch Wandel' (growth through change) program with the overall objective of consolidating its strong position in the market and equipping itself for the future. The main aims within the strategic program are to safeguard profitable growth over the long term, bring about further growth in sales, refine the strong R+V corporate culture, and sharpen the focus on customer needs. This future-oriented strategy is being driven forward with support from the implementation of a digitalization strategy, encompassing a broad range of activities from the provision of products and services for customers and sales partners to the processing of customer inquiries. R+V is enhancing its sales function, thereby underpinning the process of change in the local cooperative banks.

It is paving the way for profitable growth by stepping up business and attracting new customers both in the corporate customer segment (occupational pension provision business and non-life business) and in the retail customer segment (introduction of innovative cooperative solutions). Various customer-facing and back-end processes are becoming increasingly digitalized. This creates advantages in terms of process efficiency and quality, reduces costs, results in quicker processing of customer inquiries, and puts R+V on a secure footing for the future. In 2018, for example, R+V ran successful pilot projects in the field of robotic process automation (RPA).

The aim is to transfer R+V's tried-and-proven business model for direct insurance to the hybrid world by ensuring permanently high quality of advice across all channels and thereby accelerating the growth of the insurance business. The company will make use of its regional focus and steadily increase the value added for customers, the Volksbanken Raiffeisenbanken cooperative financial network, and employees over the long term. As part of this, it will also update the range of products for retail and corporate customers. To this end, it constantly tailors its advisory and business processes to meet the requirements regarding collaboration with the cooperative banks. The successful transformation of the traditional approach for the digital world is illustrated by the provision of video-based advice. In 2018, R+V implemented new technologies and processes that are both digital and personal, enabling customers to obtain tailored advice directly via digital channels.

The quality of advice is becoming increasingly important for customers, sales partners, and the sales force. R+V continues to focus firmly on advising customers in the round and ensuring consistently high-quality advice whatever the channel. Based on the cooperative 'R+V-BeratungsQualität' advisory process, R+V has introduced an optimized process for advising retail customers. All partners are better integrated into this process, which lays the foundations for even more successful marketing.

In line with this strategy, R+V is planning to continue on its trajectory of profitable growth in 2019. R+V, the composite insurer in the Volksbanken Raiffeisenbanken cooperative financial network, is aiming to use its highly effective product portfolio to steadily increase its market penetration. Further consolidation of R+V's market leading positions in a number of areas, including personal pension products, occupational pension provision, vehicle fleets, and credit insurance, will be based on developing the potential available from both corporate and retail customers. R+V intends to achieve a lasting increase in market share by focusing on organic growth to be achieved by leveraging the potential available in the cooperative financial network, increasing cross-selling activity, offering innovative products, and expanding online and multichannel activities. This will also help to steadily increase the value added for the Volksbanken Raiffeisenbanken cooperative financial network.

In non-life insurance, R+V forecasts that **gross premiums written** will grow significantly in 2019. The **claims rate** will probably be lower than in 2018. Based on a slight rise in the expense ratio, the **combined ratio** (total of insurance business operating expenses and claims expenses divided by premiums earned) is projected to be on a par with 2018.

In the life insurance and health insurance business, R+V aims to back up the successes achieved in previous years with a long-term diversification strategy. **Gross premiums written** are predicted to remain at a high level in 2019.

The public at large has recognized that the statutory pension needs to be topped up by private and/or occupational pension provision. These circumstances alone already offer potential for growth. Particular momentum in the occupational pensions business could be provided by small and medium-sized enterprises in Germany. In businesses with fewer than 100 employees, many of these employees do not yet make use of the benefits available under occupational pension schemes. The German Act to Strengthen Occupational Pensions (BRSG), which came into force in 2018, addresses this situation in particular. This will give rise to new sales opportunities that will be actively exploited by R+V. Industry-specific pension schemes such as the dedicated schemes available in Germany for the chemicals industry (Chemie-Versorgungswerk), engineering industry (MetallRente), pharmacy industry (ApothekenRente), healthcare industry (KlinikRente), and media industry (Versorgungswerk der Presse) are helping to popularize occupational pension provision.

R+V expects the fierce competition in the reinsurance sector to continue. Following the major loss events that occurred in 2017 and 2018, it is anticipated that there will be a moderate increase in the price of reinsurance cover in 2019. In both commercial and retail business, the adversely impacted natural catastrophe segments are particularly expected to benefit from this trend. R+V will continue to pursue its strategy of profitable growth in its inward reinsurance business. Further growth of gross premiums written is expected. The retention of the stringent underwriting guidelines will ensure rigorous compliance with the income-oriented business policy. On the costs side, R+V anticipates a slightly higher **administrative expenses ratio** (net insurance business operating expenses divided by net premiums earned) and an improvement in the **combined ratio** in 2019.

Investing activity is based on a long-term investment strategy combined with a state-of-the-art approach to risk management. Focusing on asset protection, the strategy is designed to ensure that insurance obligations can be met at all times.

In the expectation that the environment of low interest rates will remain largely unchanged, the net gains under **gains and losses on investments held by insurance companies** are forecast to hold steady in

2019. This item will thus continue to make a significant contribution to overall profit before taxes at R+V in the future.

Overall, these developments are projected to cause a rise in **profit before taxes** year on year.

Regulatory RORAC is expected to go up in 2019 in line with the forecast growth of profit before taxes combined with a slight rise in capital requirements.

4.7 TeamBank

Although there are early signs that the economy is clouding over, consumer spending is likely to remain a key driver of economic growth in 2019. The consumer finance market is therefore predicted to deliver a stable performance. This solid growth trajectory, combined with consumers' increasing preference for digital delivery channels, makes the market very attractive to competitors. Further digital competitors with disruptive business models are expected to enter the market. Fintechs are becoming more and more important, and even tech giants such as Amazon and PayPal are increasingly making their presence felt in the German lending sector (e.g. installment payments for purchases of Amazon's own products).

In collaboration with the cooperative banks, TeamBank is aiming in 2019 to generate profitable, sustainable growth at a rate that is consistently higher than that of the market. TeamBank remains focused on establishing connectivity between the various methods of customer access, directing customers who prefer online/mobile channels to the cooperative banks, and attracting new customers and members as well as retaining existing ones.

TeamBank is forecasting a substantial gain in **net interest income** for 2019 based on portfolio growth.

In 2019, customer creditworthiness is expected to deteriorate compared with 2018. Given that the portfolio is likely to grow, **loss allowances** will therefore probably rise sharply.

Rigorous management of costs by focusing on the core business and targeted capital investment to ensure TeamBank's future competitiveness will help ensure that **administrative expenses** in 2019 are only slightly higher than the 2018 level.

Taking into account the hefty rise in net interest income, the slight increase in administrative expenses, and the greater level of loss allowances, **profit before taxes** in 2019 is forecast to be at the same high level reported for 2018.

Nonetheless, the **cost/income ratio** will remain at the pleasingly low level achieved in 2018.

The rise in minimum capital requirements will lead to a decline in **regulatory RORAC** in 2019.

4.8 UMH

UMH has continued to set itself ambitious targets for 2019, even though it has just completed a financial year in which it generated the third-highest net profit in its history, attained significant net inflows, and achieved a high level of assets under management.

Against the backdrop of persistently challenging conditions – the United Kingdom's imminent departure from the EU, the behavior of the United States under the Trump administration, and the drifting apart of the major currency areas and the associated fallout for the global economy – UMH intends to continue systematically exploiting opportunities to deliver a positive business performance in both the national and international environments.

In 2019, UMH is aiming to maintain new business at a very high level and forecasts that the positive trend in assets under management will continue, despite lower expectations regarding overall performance.

Net fee and commission income, which includes volume-related income, is projected to remain at a very high level in 2019, mainly as a consequence of the expected higher level of average assets under management. The countervailing effect of the planned sale of Union Investment Towarzystwo Funduszy Inwestycyjnych S.A. (TFI) on January 31, 2019 has already been factored in. A reduction in expected returns from performance-related management fees is also anticipated.

Net finance costs – comprising net interest income, gains and losses on investments, and other gains and losses on valuation of financial instruments – are likely to improve significantly in 2019, primarily due to a reduced expense in relation to the valuation of guarantee commitments and the expectation of a more positive valuation of own-account investments.

Administrative expenses are projected to rise significantly in 2019. Staff expenses will rise because of the growth-driven increase in the number of employees, the effect over a whole year from prior-year appointments, and planned salary increases. Building costs and IT costs will cause general and administrative expenses to go up. Depreciation, amortization, and impairment will increase as a result of the first-time capitalization of capital expenditure relating to completed projects. The planned sale of TFI will partly offset the rises across all items of administrative expenses.

A sharp increase in **other net operating income** is expected due to the anticipated gain on the sale of TFI.

Based on the factors described above, **profit before taxes** in 2019 is likely to remain close to the level reported for 2018.

The situation will be similar for the **cost/income ratio** and **regulatory RORAC**.

4.9 VR LEASING

VR LEASING's priority for 2019 is to carve out a clear position in an increasingly fierce competitive environment and thus provide the best possible support to the cooperative banks. It therefore needs to continue to offer solutions to meet customers' expectations, which have risen with the advance of digitalization. This is all the more important given that expectations regarding business prospects in 2019 – particularly among small and medium-sized enterprises (SMEs) – might dampen the propensity to invest and could thus push down demand for financing solutions. Regulatory requirements and the prediction of a continued policy of low interest rates remain challenging factors for the business environment.

Business model firmly focused on supporting the cooperative banks

Accompanying its new VR Smart Finanz brand, VR LEASING will continue to forge ahead with focusing its business model on being a digital provider of finance for the self-employed and small businesses in 2019. It will concentrate on generating sustainable growth and, as a strategic partner, giving the best possible support for the cooperative banks' business with corporate customers. Joint marketing should unlock potential among the self-employed and small businesses as well as (at the lower end of) the SME segment (BVR clusters 2–4). To this end, VR LEASING will optimize its digitally based solutions on an ongoing basis and make them available across all channels. It will also continue to develop smart data analysis. The aim is for the solution portfolio to be the ideal complement to the cooperative digital ecosystem.

Reorganization

To help sharpen the focus of its business model, VR LEASING intends to successfully complete the sale of VR-IMMOBILIEN-LEASING GmbH, BFL Leasing GmbH, and the centralized settlement business by June 30, 2019. This process began in 2018 when the contracts of sale were signed. The factoring business is to be taken over by DZ BANK, and in so doing be strengthened – particularly in terms of the range of products.

The transformation of the business model in 2018 heralded the start of VR LEASING's organizational restructuring. The first step, involving a reduction of the workforce to 500 full-time equivalents, is to be implemented by June 30, 2019.

Increasing the market penetration of digitally based solutions at the cooperative banks is expected to provide fresh growth impetus and lead to a rise in the commission it pays to the cooperative banks. Consequently, a small **profit before taxes** is projected for 2019.

Further development of simple, automated financing solutions

In 2019, VR LEASING will further optimize its automated liquidity solutions and decision-making for financing of up to €750,000 so that it can provide the best possible support for the cooperative banks' omnichannel sales. This will include enhancements to the 'VR Smart flexibel' business lending product and the 'VR Smart express' asset finance solution as well as joint marketing activities. Looking ahead, the limit for automated decisions on financing is to be increased in stages to €750,000.

To further strengthen the digital sales channel, the internet-based ordering process that enables corporate customers to enter into a borrowing agreement of up to €60,000 in an entirely online process on the websites of affiliated local cooperative banks will be continually enhanced and adapted to meet customer needs.

Expansion of digital value-added services
VR LEASING refines its digital value-added services systematically on the basis of customer feedback. One example is VR Smart Guide, which has been available since December 2018 as a joint, even more effective solution from VR LEASING and DZ BANK and brings together the previous stand-alone solutions SmartBuchhalter and VR-FinanzGuide. This application simplifies accounting and financial planning for self-employed and small-business customers on an ongoing basis. Bonitätsmanager (credit status manager), which has been available online since 2018, is an application that enables businesses across Germany to check their credit rating and get tips on how to optimize it. The application is to be expanded in 2019.

Enhancement of the digitally supported solutions and the even greater focus on the self-employed and small-business customer segment and on SME customers are likely to lead to significant expansion of the volume of business and a substantial increase in the benefits for local cooperative banks in 2019. As a result, a further year-on-year rise in **net interest income** is predicted for 2019.

The greater level of market penetration achieved by the 'VR Smart flexibel' business lending product will be accompanied by an increase in **loss allowances** in line with the planned growth in new business.

The progress achieved on the transformation into a digital provider of finance for the self-employed and small businesses will lead to a substantial fall in **administrative expenses** in 2019 compared with 2018. As expected, income is likely to decrease as a result of finally disposing of parts of the business in 2019. Overall, the **cost/income ratio** will improve in 2019. The reduction in headcount at the end of 2018 as part of a voluntary severance program is, as planned, projected to lead to a further decrease in staff expenses.

Taking into account the predicted improvement in earnings and the stability in risk-weighted assets compared with 2018, an improvement in **regulatory RORAC** is forecast for 2019.