INFRA BANKING EXPERTS

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KOMMUNAL
KREDIT

ANNUAL
REPORT OF KOMMUNALKREDIT AUSTRIA AG

2017

BUILDING BRIDGES

WE PROVIDE TANGIBLE BENEFIT
TO THE COMMUNITY

WE PROVIDE TANGIBLE BENEFIT TO THE COMMUNITY

Significant growth in new business

26 projects with commitments worth EUR 635m

Well-balanced new business portfolio

Strongly diversified in terms of product, region and asset class

Funding position enhanced

Customer deposits more than tripled to EUR 644m

Robust result

GAAP profit after tax EUR 18.6m

High quality of loan portfolio

Average rating »A«
NPL ratio 0.0%

Solid capital position

CET 1 ratio 23.5%
Total capital ratio 29.9%

Launch of online retail platform

KOMMUNALKREDIT INVEST with deposits of EUR 116m in first three months

HIGHLIGHTS 2017

Kommunalkredit is well on track as a strong player in the European infrastructure market.

- **Origination – significant growth in new business:** Kommunalkredit managed to close 26 projects in 13 countries with commitments worth EUR 635.2m delivering a P&L impact significantly above plan.
- **Distribution:** Kommunalkredit placed EUR 373.2m of its portfolio with institutional investors and banks. Thereof EUR 194.2m stemmed from new business origination across 9 projects. The successful distribution activity testifies to new business transactions' market conformity in terms of structure, pricing and risk management.
- **Strong client impact:** Kommunalkredit expanded its network of anchor clients evidenced by transaction award from repeat client relationships and a widely diversified group of institutional investors, such as insurance companies, pension funds, banks, family offices and infrastructure funds.
- **First industry awards:**
  - Kommunalkredit was awarded its first industry accolades from leading infrastructure journals, which included the "Europe Transport Deal of the Year" by *PFI* and a "Top 10 Infrastructure Deal" by *Inspiratia*.
  - In a ranking by the Austrian finance magazine *Börsianer*, Kommunalkredit was chosen as the country's top "Specialist Bank" and as the third best bank in Austria, based on strategic innovation.
- **Well-balanced portfolio mix of new business:** In 2017 new business was strongly diversified in terms of product, region and asset class with attractive risk/return profiles and a decreasing duration, thus contributing to an improved asset-liability match.
- **High quality of the loan portfolio:** As of 31 December 2017, the average rating of the loan portfolio was "A", with 89.4% of the loans being investment grade. The non-performing-loan (NPL) ratio was maintained at 0.0% in 2017. The weighted average probability of default was 0.23%.
- **Team and processes strengthened:** The front office team was strengthened by hiring highly experienced experts with a strong international track record, whilst in parallel Kommunalkredit enacted a cost efficiency programme which will lead to a reduction of the cost base in 2018.
- **Funding position enhanced:** Kommunalkredit more than tripled its customer deposits to EUR 644.4m driven by both wholesale and retail deposits. As a major strategic initiative, the bank launched its new online retail platform KOMMUNALKREDIT INVEST in 2017. In addition, Kommunalkredit successfully returned to the capital market with a "Debt Issuance Programme", under which it issued a social covered bond and, for the first time since its privatisation in 2015, a senior unsecured bond.
- **Solid capital position:** As of 31 December 2017, Kommunalkredit's total capital ratio amounted to 29.9%. Its CET 1 ratio stood at 23.5%.
- **Rating:** Kommunalkredit's unsecured debt issues remained stable at investment grade level with a long-term rating of "BBB (low)" (negative trend) and a short-term rating of "R-2 (mid)" from the DBRS rating agency. Standard & Poor's rated Kommunalkredit's covered bonds for the first time on 13 June 2017, assigning them an "A" rating.

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BOARDS
OF THE BANK

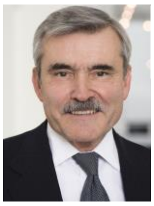
EXECUTIVE BOARD

Alois Steinbichler
Chief Executive Officer

Jörn Engelmann
Member of the Executive Board

Karl-Bernd Fislage
Member of the Executive Board
since 1 February 2017

Wolfgang Meister
Member of the Executive Board



Alois
Steinbichler

Jörn
Engelmann

Karl-Bernd
Fislage

Wolfgang
Meister

SUPERVISORY BOARD

Patrick Bettscheider
Chairman; delegated by Interritus Limited

Christopher Guth
Deputy Chairman; delegated by Attestor Capital

Friedrich Andreae
Delegated by Attestor Capital; Managing Director Gesona Beteiligungsverwaltung GmbH and Satere Beteiligungsverwaltungs GmbH

Katharina Gehra
Delegated by Interritus Limited; Managing Director Gesona Beteiligungsverwaltung GmbH and Satere Beteiligungsverwaltungs GmbH

Jürgen Meisch
Managing Director Achalm Capital GmbH

Werner Muhm
Former Director of the Vienna Chamber of Labour and the Federal Chamber of Labour
until 10 March 2017

Martin Rey
Managing Director Maroban GmbH
since 24 July 2017

Patrick Höller
Delegated by the Staff Council

Franz Hofer
Delegated by the Staff Council
until 6 November 2017

Paul Matousek
Delegated by the Staff Council
since 6 November 2017

Renate Schneider
Delegated by the Staff Council
since 20 February 2017

STATE COMMISSIONER

Edeltraud Lachmayer
State Commissioner; Federal Ministry of Finance

Bettina Horvath
Deputy State Commissioner; Federal Ministry of Finance

GOVERNMENT COMMISSIONER FOR THE COVER POOL FOR COVERED BANK BONDS

Karin Fischer
Government Commissioner; Federal Ministry of Finance

Sandra Kaiser
Deputy Government Commissioner; Federal Ministry of Finance

FOREWORD
BY THE CHIEF EXECUTIVE OFFICER

Ladies and Gentlemen,

I am pleased to present the Annual Report of Kommunalkredit Austria AG (Kommunalkredit) for the financial year 2017. The bank is well on track to meet its growth targets. We achieved or exceeded our main objectives for 2017 and our success is being increasingly recognised in the European infrastructure market. Kommunalkredit bridges the needs of project sponsors (developers and operators of infrastructure) and institutional investors, such as insurance companies, pension funds or banks, for whom infrastructure has become an increasingly attractive asset class.

In 2017, Kommunalkredit Group generated a consolidated IFRS after-tax result of EUR 18.1m (2016: EUR 49.0m). The decrease compared to the previous year resulted from the expected decline in one-off positive effects relating to the buyback of own issues in 2016. The result for 2017 reflects the increasing new business volume, which made a growing contribution to both net interest income and fee and commission income.

Last year, we completed 26 projects with commitments worth EUR 635m across 13 European countries. We played a leading role in notable projects, acting as Mandated Lead Arranger or Co-Arranger, and we were awarded our first industry accolades. In addition to the origination of new business, the placement of financing with end investors is one of the bank's strategic objectives. The bank showed a strong performance by placing a volume of EUR 373m with a variety of leading institutional investors.

We implemented major strategic initiatives. The launch of our online retail platform KOMMUNALKREDIT INVEST represents Kommunalkredit's first product offering for retail customers. Following the appointment of Bernd Fislage as Member of the Executive Board, assuming responsibility for Banking & Markets, our front office team was strengthened with the recruitment of experienced senior bankers. In parallel, we enacted an efficiency programme to streamline internal processes, which will lead to a reduction of the cost base in 2018. The bank's funding position was enhanced significantly. We managed to triple customer deposits to EUR 645m. Furthermore, the bank returned to the capital market with the emission of a EUR 300m covered bond, the first of its kind in Austria.

Kommunalkredit enjoys a very solid capital position. It reports a total capital ratio of 29.9% and a CET 1 ratio of 23.5%. The bank holds a loan portfolio of high asset quality without a single default in 2017. The average rating of the portfolio was "A", with 89.4% of the loans being investment grade. The non-performing-loan (NPL) ratio was maintained at 0.0%.

Based on the progress achieved in the business year 2017, Kommunalkredit is well-positioned to benefit from the opportunities in the European infrastructure market. A dynamic project pipeline promises a continuation of a successful year. With a rising operating result and a continued decline in extraordinary income, Kommunalkredit expects its annual result for 2018 to be above the previous year's level.

We have started 2018 with a dynamic project pipeline. On behalf of the Executive Board, I would like to take this opportunity to thank our clients and business partners most cordially for their excellent cooperation and the trust placed in us. Our thanks also go to our shareholders for their active support and to our employees for their great commitment, which they once again showed over the previous year.

Yours sincerely,

Alois Steinbichler
Chief Executive Officer of Kommunalkredit Austria AG

MANAGEMENT REPORT FOR THE BUSINESS YEAR 2017

ECONOMIC FRAMEWORK

Economic environment in 2017

In 2017, the economy of the euro zone experienced the strongest growth since 2007, picking up by 2.4% compared to 1.8% in 2016. Gross domestic product (GDP) rose by 2.2% in Germany (2016: 1.9%) and by 1.8% in France (2016: 1.2%). The pace of economic growth in Austria was exceptionally fast at 3.1% (2016: 1.5%), whereas the British economy was notably depressed in the context of the looming Brexit, with GDP climbing by only 1.8% (2016: 1.9%).[1]

Especially in the euro zone, the economic growth momentum observed in 2017 was robust and broad-based, driven primarily by private consumption and business investment. Furthermore, growth was supported by steadily rising private income and corporate profits as well as expanded lending spurred by favorable financing conditions. Growth was more balanced and self-sustained across countries and sectors. Household consumption in particular was backed by a solid increase in disposable income and consumer confidence.

The unemployment rate in the euro zone dropped from 9.6% at the end of 2016 to 8.7% at the end of 2017, reaching the lowest level since January 2009. In Austria, it decreased from 5.7% to 5.3% over the same period. From August 2017 onwards, the rate of inflation in the euro zone remained constantly above 1.4%, with the average rate for the full year at 1.4% (after 1.1% in 2016). In Austria, the inflation rate rose significantly to 2.2% (2016: 1.0%). The rebound in inflation had limited impact on household purchasing power owing mainly to further acceleration in job creation. This consumer-led recovery has stimulated the business sector, leading to increased corporate profitability.[2]

Economic activity in the euro zone was resilient to political risks in 2017. The economic implications of the referendum in Catalonia in October 2017 were limited and the considerable delays in forming a government in Germany after the September 2017 elections had no economic consequences. The biggest risk for the euro zone continues to be related to Brexit and the possibility of the UK eventually leaving the EU without a deal and facing a legal void.

[1] European Commission's Winter 2018 Interim Economic Forecast, February 2018.
[2] Eurostat.

At its October 2017 meeting, the Governing Council of the European Central Bank (ECB) decided to extend its Asset Purchase Programme (APP) for another nine months until September 2018 at a reduced monthly pace of EUR 30bn in purchases (previously EUR 60bn/month) without any other changes to interest rates or to forward guidance. The ECB decided to keep its quantitative easing programme (QE) open-ended. The Council took stock of the further improvement of the economic situation, while stressing that the medium-term outlook for inflation, though also improving, was still a concern.[3]

At its December 2017 meeting, the Governing Council of the ECB kept interest rates on main refinancing operations and the deposit facility unchanged at 0.00% and minus 0.40%, respectively. The low-yield environment has furthermore supported the strong demand for fixed income products even at very low yields; the constant demand from QE buying has boosted debt capital market activities, especially in sovereign debt and covered bond markets, and led to constantly reduced volatilities and correlations across debt and equities markets.[4]

In the US, the Federal Reserve System (Fed) reacted to the positive data for employment and inflation by continuing the step-by-step normalisation of its monetary policy. It increased the key lending rate three times in 2017, most recently to a range of 1.25% to 1.50% in December 2017. Furthermore, the Fed began to gradually reduce its total assets. Following the decision to start unwinding QE in October 2017, the decline in the Federal Reserve's balance sheet will scale up until it reaches a maximum of USD 50bn per month in 2018.[5]

Austrian municipalities in 2017

Kommunalkredit is traditionally deeply rooted in the Austrian municipal sector, with cities and municipalities accounting for a major part of its historic portfolio (loans granted before the privatisation in autumn 2015). The bank is well-positioned in the Austrian market when it comes to infrastructure financing, financial advisory, funding and the administration of support programmes. Therefore, Kommunalkredit is very familiar with the financial condition of local authorities. Since 2005, it has been producing the annual "Municipal Finance Report" in cooperation with the Association of Austrian Municipalities and the Association of Austrian Cities and Towns as well as with the support of Statistics Austria. This publication provides a detailed overview of the revenues and expenses of all cities (excluding Vienna) and municipalities in Austria.

According to the 2017 Municipal Finance Report (accounting year 2016), the Austrian local authorities are in solid financial condition. The balance of revenues and expenses for 2016 was positive at EUR 1.72bn, the second highest value since the turn of the millennium. Having generated a surplus according to the Maastricht criteria of EUR 31.0m or 0.01% of the Austrian gross domestic product (GDP), the local governments (excluding Vienna) again met the zero-deficit target of the Austrian Stability Pact adopted in 2012. Municipal investments increased by 1.6% to EUR 2.19bn, remaining at the high level reached in previous years. The downward trend of municipal debt observed since 2011 continued throughout 2016 with a reduction by 1.1% to EUR 11.14bn.

[3] OeNB, Financial Stability Report 34.
[4] OeNB, Financial Stability Report 34.
[5] Board of Governors of the Federal Reserve System, Press Releases.

THE BUSINESS MODEL OF KOMMUNALKREDIT AUSTRIA AG

Infrastructure matters

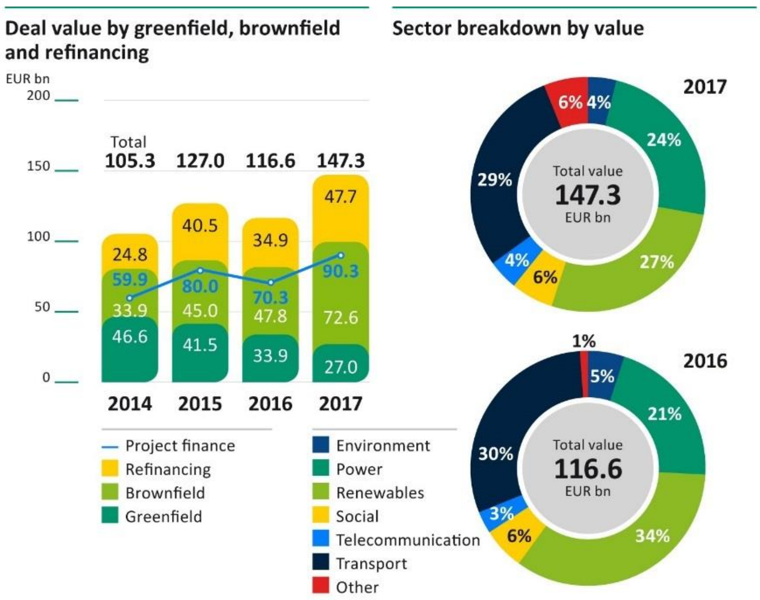
Infrastructure by its very nature is essential to the efficient functioning of society. Infrastructure investments can serve as a powerful tool for answering social needs and fundamentally increasing the general well-being of communities. They create the basis for prosperity and a high quality of life. Modern infrastructure is an indispensable prerequisite for the sustainable use of resources and successful approach to deal with climate change.

Demand for investment in infrastructure is enormous. The European Investment Bank (EIB) forecasts spending required to reach the targets of the Europe 2020 strategy at EUR 150bn to EUR 200bn per year.[6] Investment demand is particularly high in the sectors of energy, with a special focus on renewable energy, transport, social infrastructure and communications technology.

The way in which these projects are financed has changed significantly in recent years. As the financial latitude of the public sector is decreasing on account of the high level of government debt and budget caps, a shift from classic budget finance to project finance continues to occur thanks to private funding. In 2017, more than 60% of all infrastructure schemes in Europe were implemented through project finance.[7] Commercial banks continue to be a main source of debt for infrastructure projects. However, a host of other funders and products have appeared given the increasing acceptance of infrastructure as an asset class in its own right. Private placements, public bonds, direct institutional debt, multilaterals and export credit agencies are also heavily contributing to the sector. For institutional investors seeking stable long-term cash flows from a sustainable asset class, this offers an opportunity for real return enhancement in the current low-yield environment.

The European infrastructure market in 2017

The European infrastructure market was booming in 2017, demonstrated, inter alia, by the significant increase by 26.3% in deal value to a total of EUR 147.3bn.[8] While the value of brownfield projects grew by 52% to EUR 72.6bn, a drop by 8% to EUR 27.0bn was observed in greenfield projects. The refinancing volume rose by 36.7% to EUR 47.7bn.



Source: Inframation. Based on a EUR-USD exchange rate of 1,19930.

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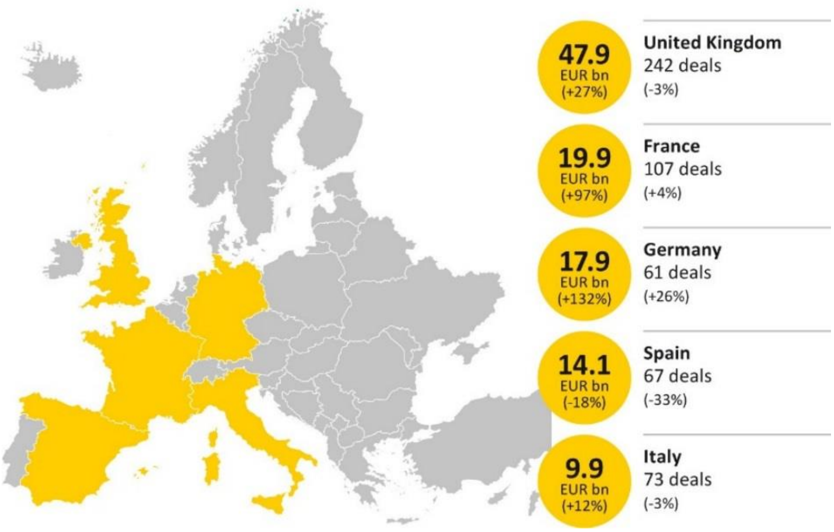
[6] European Investment Bank, The Europe 2020 Project Bond Initiative – Innovative Infrastructure Financing, January 2017.
[7] Infrastructure information platform "Inframation".
[8] All figures in the section „The European infrastructure market in 2017" according to Inframation, based on a EUR-USD exchange rate of 1,19930.

The top 5 European infrastructure markets by deal value and number of deals



2017 experienced a strong inflow of equity from institutional investors and investment funds, with equity (including government grants) accounting for 38.7% of the total financing volume. In addition, the market saw a rise in the share of long-term private placements and capital market bonds. 12.6% of total volume were financed via capital market bonds,

while loans made up 48.7%.

Energy & environment (environment, power, renewables) accounted for 55% of total deal value, transport for 29%, social infrastructure for 6% and communications technology for 4%. As in 2016, the markets with the strongest demand were the United Kingdom (UK) with a financing volume of EUR 47.9bn, France (EUR 19.9bn), Germany (EUR 17.9bn), Spain (EUR 14.1bn) and Italy (EUR 9.9bn). Except for Spain, growth was recorded in all of these markets, especially in France and Germany. The positive development in the UK was particularly worth mentioning with an increase in volume by 27% despite the looming Brexit deadline, which has not discouraged investors from committing capital to UK's infrastructure.

Kommunalkredit's business model

We provide tangible benefit to the community

Kommunalkredit contributes to the sustainable success of infrastructure projects that improve the quality of peoples' life. The bank provides tangible benefit to the community in terms of economic dynamism, job creation, social cohesion, urban development and climate change.

By combining in-depth industry expertise and structuring know-how with the financing ability of a bank and strong relationships with international clients und investors, Kommunalkredit achieves strong impact for its clients and generates sustainable value for its stakeholders. The bank enables the implementation and operation of infrastructure, bridging the needs of project sponsors (developers and operators of infrastructure) and institutional investors, such as insurance companies, pension funds, banks, family offices and infrastructure funds. Kommunalkredit has established itself as a reliable partner for its key clients.

Backed by two international and long-term oriented shareholders, Kommunalkredit positions itself as a leading market player in the European infrastructure market, concentrating on energy & environment, social infrastructure & communications technology and transport.

Energy & Environment
- Energy supply & distribution
- Renewable energy
- Water supply & treatment
- Waste management & disposal

Transport
- Roads, bridges, tunnels
- Airports, ports, waterways
- Rail/light rail, rolling stock

Social Infrastructure & Communications Technology
- Nurseries, schools, universities
- Hospitals, nursing homes
- Police & court buildings
- Administrative buildings
- Broadband / Fibre Optic / Data Center

As a specialised bank, Kommunalkredit advises, structures and funds senior debt and mezzanine structures across the entire life cycle of an infrastructure project. Kommunalkredit's investments are focused on stable, cash flow-based, project secured transactions.

Kommunalkredit cooperates manifold with international institutions, such as the EBRD and the EIB.

SIGNIFICANT EVENTS OF THE BUSINESS YEAR

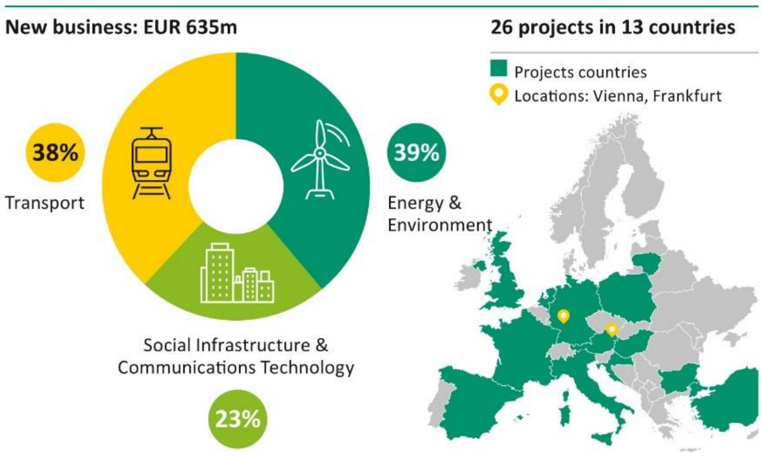
Business review

The bank is well on track to meet its growth targets, looking back on its best year in infrastructure finance so far. In 2017, Kommunalkredit generated a consolidated after-tax result of EUR 18.1m (IFRS). This result reflects the growing contribution from new business both to net interest income and fee and commission income. The bank invested in new strategic initiatives in 2017, such as the implementation of its new online retail platform KOMMUNALKREDIT INVEST, and strengthened its front office team. In parallel, it enacted a cost efficiency programme to streamline processes, which will lead to a reduction of the cost base in 2018.

1. Strong new business development: origination, execution, distribution

Significant growth with a diversified portfolio

Kommunalkredit managed to close 26 projects in 13 countries with commitments worth EUR 635.2m (2016: EUR 146.3m) delivering a P&L impact significantly above plan. The new business portfolio was highly diversified in terms of product, region and asset class with attractive risk/return profiles. It was distributed widely across various asset classes, with 13 projects and 39% of the total volume accounted for by the energy & environment segment (waste-to-energy, on-shore wind, solar), 6 projects and 38% of the volume by transport (roads, airports), and 6 projects and 23% of the volume by social infrastructure & communications technology (hospitals, nursing homes, fixed line/broadband). The total included one public-sector direct finance transaction. With 26 projects spread across 13 European jurisdictions, Kommunalkredit reached a high degree of regional diversification. Kommunalkredit provided finance for both brownfield projects (16 transactions) and greenfield projects (9 transactions). Thus, the steep growth in brownfield projects recorded in Europe in 2017 was reflected in the bank's new business.



Not only the bank's origination but also its distribution activities were highly diversified. Kommunalkredit placed new business worth EUR 194.2m for a total of 9 projects with a wide range of institutional investors across Europe. The successful distribution activity testifies to new business transactions' market conformity in terms of structure, pricing and risk management.

Flagship projects

Kommunalkredit contributed to implementing the financing of a number of notable projects, playing a leading role in half of the transactions either as Mandated Lead Arranger (11 projects) or Co-Arranger (2 projects). In the transport sector Kommunalkredit acted as Mandated Lead Arranger in the EUR 182m refinancing of the A21 Shadow Toll Road in Spain and in the EUR 230m refinancing of a section of the A2 Motorway in Poland. Furthermore, the bank was mandated as Joint Bookrunner and Underwriter in the EUR 1.2bn senior funding of the Superstrada Pedemontana Veneta, an Italian greenfield motorway, via a project bond.

A2 Section Toll Road (Poland)

Kommunalkredit acted as Joint Mandated Lead Arranger in the EUR 230m refinancing of the A2 section 1 Toll Road in Poland. The project was the first toll motorway to be designed, built, financed and operated under a concession-based model in Poland.

The first phase of the A2 involves construction, operation and maintenance of 149km of motorway between Konin and Nowy Tomyśl.

The A2 forms part of Poland's strategic Berlin – Warsaw corridor, providing one of the most important transportation links between Western and Central Europe. Traffic levels have continuously risen with an annual average growth rate of 12% since the opening of the motorway.

A21 Shadow Toll Road (Spain)

Kommunalkredit acted as Mandated Lead Arranger in the EUR 182m refinancing of the Spanish A21 Motorway. The project covers the refinancing of the operation and maintenance of six sections on the motorway. The A21 Autovía del Pirineo is a shadow toll road based on a 30-year concession-based model. Located in Navarra, the motorway is highly important for the region's transport network, running parallel to the Pyrenees at the border between Spain and France.

The project has substantial upside potential as adjacent motorways are expected to be constructed in the coming years. Navarra is one of the wealthiest regions in Spain, boasting the third highest GDP per capita and the lowest unemployment rate.

In the energy & environment segment, the bank contributed to various waste-to-energy deals, inter alia, acting as Mandated Lead Arranger in the EUR 240m financing of the Gipuzkoa plant in Spain and as Senior Lender in the primary syndication of the GBP 505m debt refinancing of the Cory Riverside facility in England, as well as in the GBP 179m financing of Parc Adfer in North Wales. Furthermore, the bank took part as Arranger and Senior Lender in the financing of solar and wind parks in France, Germany, Italy, Spain and the United Kingdom. Eventually, Kommunalkredit acted as Mandated Lead Arranger in the financing of the acquisition of a leading national fixed line telecoms operator in Southeastern Europe and took part in the financing of a nursing home in Germany.

Gipuzkoa Waste-to-Energy (Spain)

Kommunalkredit acted as Mandated Lead Arranger in the EUR 240m financing of the waste-to-energy plant in Spain. The project, implemented under a 35-year availability-based scheme, covers the design, construction, financing, operation and maintenance of the Gipuzkoa Environmental Complex in the Basque Region. The facility includes a mechanical-biological treatment plant, a waste-to-energy plant and auxiliary systems, utilities and ancillary equipment.

The project is of strategic importance to the region as waste is currently transported to be processed elsewhere, leading to costs and environmental inefficiency. The project is a viable alternative to improve the waste management system and reduce costs.

Bité Telecom (Baltics)

Kommunalkredit acted as Senior Lender in the EUR 105m refinancing of Bité, a leading telecoms operator in the Baltic region. Bité was acquired in 2016 by Providence Equity Partners to act as a consolidator in the Baltic telecoms and media markets.

The new facility is used to partially refinance Bité´s own acquisition debt as well as to provide additional funds for the acquisition of MTG Baltics, a leading Baltic TV & Media infrastructure group. The latter deal enables Bité to grow revenues and profit per existing customer as well as to gain market share. This project puts Kommunalkredit on the map both in the CEE region as well as in the communications technology/broadband sector, as evidenced by a number of follow-on transactions in 2017.

First industry awards

The bank's success is being recognised in the market. Kommunalkredit was awarded its first industry accolades in 2017. This included the Superstrada Pedemontana Veneta project, which was elected the "Europe Transport Deal of the Year" by the leading infrastructure journal *PFI,* and the Riverside transaction, which was ranked as one of the "Top 10 Infrastructure Deals" in 2017 by *Inspiratia*, another highly regarded infrastructure journal. In the league table of leading "bond arrangers" in Europe in 2017 published by *Inframation*, a renowned infrastructure platform, Kommunalkredit held 18th position.

PFI Europe Transport Deal of the Year
Superstrada Pedemontana Veneta (Italy)

Kommunalkredit acted as Joint Bookrunner and Underwriter in the EUR 1,2bn project bond financing of the Superstrada Pedemontana Veneta, an Italian greenfield motorway. The project covers the financing of the construction, the operation and maintenance of the motorway with a total length of 162km.

The Superstrada is of significant importance for the region's connection. Its main axis is 94km long and connects 34 municipalities as well as the main industrial areas of Vicenza and Treviso. It also includes the construction of 68km of secondary/access roads. The deal was chosen as the "Europe Transport Deal of the Year 2017" by the leading infrastructure journal *PFI*.

Inspiratia Top 10 Infrastructure Deals
Cory Riverside Waste-to-Energy (UK)

Kommunalkredit acted as Senior Lender in the GBP 505m debt refinancing of the Cory Riverside waste-to-energy plant in England. The facility has been operating at full capacity since its launch in 2012. In 2016 it processed 753,000 tonnes, with 60% of its waste derived from long-term supply contracts with municipal customers.

The plant is unique as it is river-based and London's waste is transported mainly on a fleet of barges, avoiding road transport. The waste is then turned into sustainable energy. This Riverside transaction was ranked as one of the "Top 10 Infrastructure Deals in 2017" by the highly regarded infrastructure magazine *Inspiratia*.

Collaboration between public entities and private partners as an efficient form of procurement

Against the background of the limited financial latitude allowed to public budgets, the collaboration between public entities and private partners offers an efficient and transparent form of procurement for the public sector. In such a cooperation the private partner (usually a special purpose company with significant private-investor participation) agrees to deliver a public infrastructure project and service under a long-term contract. The private partner assumes various project risks, notably with regard to designing, building, operating and financing the project. In practice, two models are widely used: The public authority either pays an availability fee to the private partner as soon as the infrastructure is available (availability-based model) or gives the private partner the right to generate revenues from the provision of the infrastructure (concession-based model).

In 2017, 68 greenfield projects with a value of EUR 13.8bn were implemented in Europe based on this type of partnerships compared to 48 projects with a value of EUR 10.3bn in 2016.[9] Kommunalkredit engaged in several projects, including the financing of both the Gipuzkoa waste-to-energy plant in Spain and the Parc Adfer facility in North Wales and, as Financial Advisor, in the implementation of the Berresgasse school project in Vienna (all availability-based). Furthermore, it took part in the refinancing of the A21 motorway in Spain and the A2 motorway in Poland as well as the financing of the Superstrada Pedemontana Veneta project (all concession-based).

Campus+ Berresgasse School (Austria)

Kommunalkredit acted as Advisor to an Austrian construction group in a bid for a City of Vienna availability-based model for the construction of the Campus+ Berresgasse school project. Kommunalkredit's mandate was to structure the senior debt financing, including an element of the EIB (EFSI) funding, and to tailor a financing model.

The City of Vienna is building a number of schools under its 2013-2023 programme for the construction of new educational facilities (BIENE), Campus+ Berresgasse being the third project implemented under the programme and the first relying on project finance – after Attemsgasse (on-balance) and Stammersdorf (leasing). The BIENE programme has an overall funding volume of about EUR 700m.

Parc Adfer North Wales Waste-to-Energy (UK)

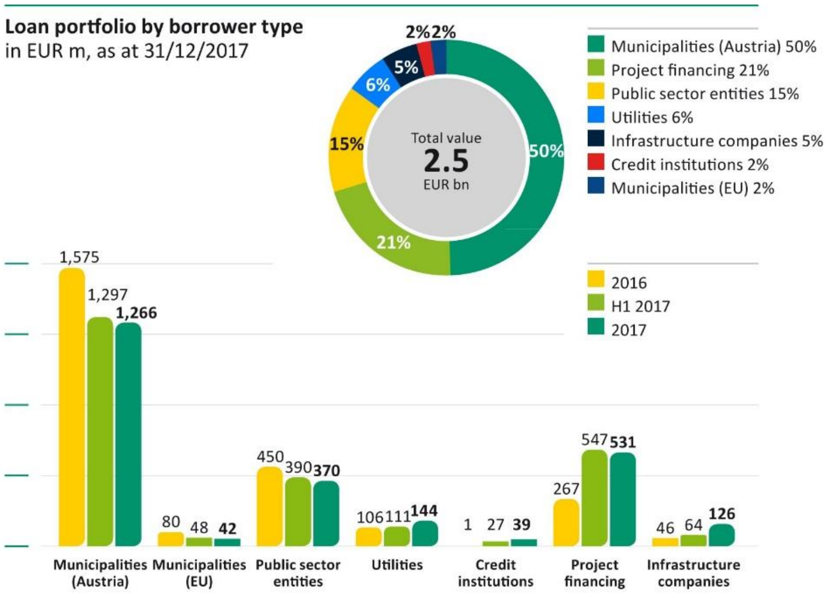
Kommunalkredit acted as Senior Lender in the EUR 179m financing of the Parc Adfer waste-to-energy plant. The facility, partly implemented under an availability-based scheme, is part of a project to manage waste in a more sustainable way in North Wales.

The construction of the plant with a 25-year operational life will be finished in 2019. The facility will have the capacity to deal with 200,000 tonnes of waste annually, with municipal waste accounting for 60% to 70% and merchant waste for 30% to 40%. The plant will supply 16MW of energy to the grid, while steam from the facility will be used to heat commercial and industrial businesses and residential areas in the region. Adfer, the name of the plant, means "to recover" in Welsh.

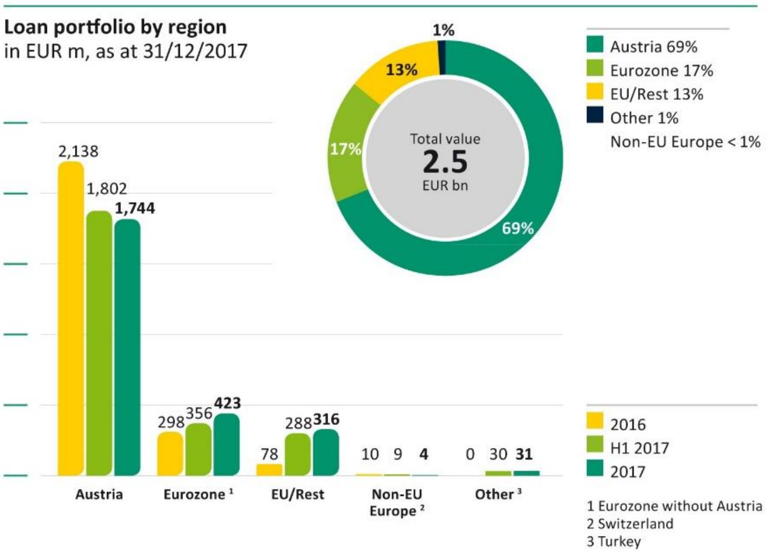
2. High quality of the loan portfolio

The bank holds a loan portfolio of high asset quality without a single default in the reporting year. As of 31 December 2017, the average rating was "A", with 89.4% of the loans being investment grade.

The non-performing-loan (NPL) ratio was maintained at 0.0% in 2017. The weighted average probability of default was 0.23%.



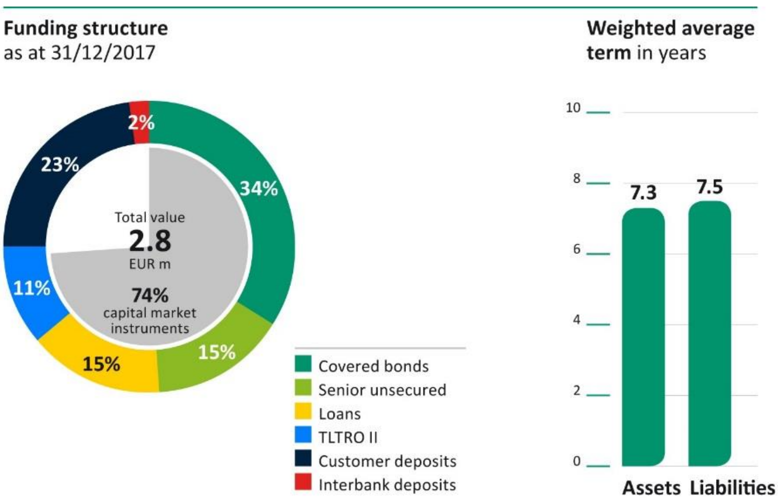
[9] Source: Inframation based on a EUR-USD exchange rate of 1,19930.



The loan portfolio is well-balanced with increasing project finance transactions and a prevalence of municipalities. As of 31 December 2017, municipalities accounted for 52% of the portfolio, with Austrian municipalities making up 50 percentage points. Project financing already accounted for 21%, while public sector enterprises had a share of 15%. Regionally, Austria contributed 69% to the loan portfolio, followed by the rest of the euro zone with 17% and other EU countries with 13%.

3. Funding position strengthened

As of 31 December 2017, Kommunalkredit continued to report a very strong liquidity position with a free liquidity reserve of EUR 283.1m (31/12/2016: EUR 390.4m). This included high-quality liquid assets (HQLA) in the amount of EUR 133.1m (31/12/2016: EUR 54.3m). Furthermore, EUR 150.0m (31/12/ 2016: EUR 336.1m) were eligible for funding via the ECB-tender or the General Collateral Pooling (GC Pooling).



In 2017, the bank succeeded in further strengthening its funding structure and broadening its investor base. Amounts owed to customers increased to a total of EUR 1,038.0m (31/12/2016: EUR 552.1m). This positive development was primarily driven by the tripling of customer deposits to EUR 644.4m (31/12/ 2016: EUR 210.8m).

Amounts owed to customers also included long-term private placements to customers of EUR 329.9m (31/12/2016: EUR 341.3m) and liabilities from collateral received in connection with derivatives of EUR 63.7m (31/12/2016: EUR 0.0m).

Kommunalkredit issued a EUR 300m social covered bond with a term of 4 years in 2017. This was the first emission of this asset class in Austria. Other capital market instruments, especially covered (34%) and senior unsecured bonds (15%), accounted for 74% of the bank's funding. The weighted average term of liabilities stood at 7.5 years, thus slightly exceeding the weighted average term of assets standing at 7.3 years.

Rising volume of customer deposits

- Retail deposits (KOMMUNALKREDIT INVEST): At the end of September 2017, Kommunalkredit launched its online retail platform KOMMUNALKREDIT INVEST in Austria as the bank's first move into retail business. KOMMUNALKREDIT INVEST takes sight deposits as well as term deposits for terms of up to ten years. By the end of 2017, the bank had attracted 1,900 retail customers with a deposit volume of EUR 115.7m (31/12/2016: EUR 0.0m). Since the beginning of January 2018, KOMMUNALKREDIT INVEST has also been operational in the retail market in Germany.

- Wholesale deposits (KOMMUNALKREDIT DIREKT and direct business with corporate customers): With its online platform KOMMUNALKREDIT DIREKT, the bank offers an efficient investment and cash management tool to municipalities and corporates. The strong growth seen throughout the year testifies to Kommunalkredit's close connection with its traditional municipal customer base in Austria. In addition, deposits by corporates rose significantly. In total, wholesale deposits more than doubled to EUR 528.8m as of 31 December 2017 (31/12/2016: EUR 210.8m). With an average volume of about EUR 2m, these deposits are highly granular, with a growing trend towards longer maturities.

Return to the capital market

In the second quarter of 2017, Kommunalkredit launched a Debt Issuance Programme (DIP) for medium-term notes (MTN), under which it placed a social covered bond with a volume of EUR 300m and a term of four years on 12 July 2017. This successful transaction marked Kommunalkredit's return to the capital market with its first public bond issue since its privatisation in 2015. The substantial investor interest was reflected in the order book, which was closed at EUR 530m, the issue being 1.8 times oversubscribed. In accordance with the general market environment, secondary market performance of the bond showed a spread tightening from mid swap +38bps at the time of issuance to approximately mid swap +30bps at year-end 2017.

Kommunalkredit was the first issuer of a publicly placed social covered bond in Austria, addressing the growing national and international demand for this investment category. About 50% of the investors are dedicated ESG[10] investors. In line with the green bond principles of the ICMA (International Capital Market Association), the net proceeds from the social covered bond issue are used to finance projects in the field of social infrastructure, i.e. education, health care and social housing, both for the funding of Kommunalkredit's existing social infrastructure portfolio and for new projects. As required, Sustainalytics, a leading sustainability rating agency, reviewed the implementation of the framework programme for social covered bonds at Kommunalkredit and confirmed all prerequisites for the issuance of the bond.

Besides the social covered bond issue, a first senior unsecured bond was sold as a private placement with an international investor in December 2017 within the framework of the successfully introduced Debt Issuance Programme.

[10] ESG = Environment Social Governance according to ICMA (International Capital Markets Association).

Buyback programme for CHF-denominated covered bonds

In May 2017, Kommunalkredit launched a buyback programme capped at CHF 200m addressing CHF 651.3m (outstanding as of 31/12/2016) covered bonds. This was to improve the currency structure in the cover pool (CHF denominated bonds vs. EUR assets; no currency mismatch in the bank). A volume of CHF 140.0m was tendered and accepted by the bank; this in combination with an ensuing 4-year EUR-denominated 300m newly issued covered bond achieved the targeted improvement. The enhanced profile was reflected in the covered bond rating. On 25 July 2017[11], Moody's upgraded the rating from "Baa2" to "Baa1", while S&P assigned an "A" rating to the newly issued EUR covered bond.[12]

Strong liquidity ratios

The Liquidity Coverage Ratio (LCR), which measures the short-term resilience of a bank's liquidity risk profile over a 30-day scenario, is closely monitored as part of the bank's early-warning system. With 449.9% as of 31 December 2017 (31/12/2016: 719.1%), the bank clearly exceeded the new regulatory minimum of 100% effective 1 January 2018.

The Net Stable Funding Ratio (NSFR), which, under Basel III, requires banks to maintain a stable funding profile in relation to the composition of its assets and off-balance sheet activities, stood at 101.5% as of 31 December 2017 (31/12/2016: 83.9%). The final definition of the ratio and associated implementation timeframe has not yet been confirmed by regulatory authorities.

4. Rating

Kommunalkredit's unsecured debt issues have a long-term rating of "BBB (low)" (negative trend) and a short-term rating of "R-2 (mid)" from the DBRS rating agency.

On 13 June 2017, Standard & Poor's assigned an "A" rating to Kommunalkredit's covered bonds, thus confirming the high quality of the underlying cover pool. Moody's assigned a "Baa1" rating to Kommunalkredit's covered bonds. On 24 November 2017, Kommunalkredit terminated its rating agreement with Moody's. Accordingly, the rating was withdrawn by Moody's on 14 December 2017. The rating agreement with S&P remains unchanged.

New appointments to the Executive Board and to the Supervisory Board

Effective 1 February 2017, Karl-Bernd Fislage was appointed to the Executive Board, assuming responsibility for Banking & Markets. The Executive Board consists of Alois Steinbichler, (Chief Executive Officer), Jörn Engelmann (Chief Risk Officer), Karl-Bernd Fislage (Banking & Markets) and Wolfgang Meister (Chief Operating Officer and Chief Financial Officer).

Effective 24 July 2017, Martin Rey, Managing Director of Maroban GmbH, was appointed as Member of the Supervisory Board. Werner Muhm resigned from his position as of 10 March 2017.

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[11] Rating Action, 25 July 2017 by Moody's.
[12] RatingsDirect, 13 June 2017 by S&P.

OTHER MATERIAL DISCLOSURES

Service Agreement between Kommunalkredit and KA Finanz AG

Under the service agreement (SA), which has been in place since 2009, Kommunalkredit provides operational services for banking operations to KA Finanz AG. Kommunalkredit's expenses under the SA are charged to KA Finanz AG. In addition, as of 31 December 2017, 14 staff members were delegated to KA Finanz AG on a full-time basis, according to a staff leasing agreement.

In February 2018, KA Finanz AG has published a tender for services currently provided by Kommunalkredit. The bank intends to submit an offer for the continuation of such services. A decision by KA Finanz AG is expected by midyear 2018. Should the bank not be awarded with a continuing contract, the service contract with KA Finanz AG will expire in the first half of 2019. In such case the operative capacity will be adjusted during a contractually existing transition period of 12 months.

Corporate Governance and Risk Management

Kommunalkredit has a clear corporate governance and risk management structure.

Supervisory Board

In 2017, the Supervisory Board performed its tasks, as defined in the Articles of Association and the rules of procedure, within the framework of its ordinary and extraordinary meetings. Four regular Supervisory Board meetings, one extraordinary Supervisory Board meeting, two Audit Committee meetings, two Risk Committee meetings, two Nomination Committee meetings as well as one Remuneration Committee meeting were held in 2017.

Executive Board

The Executive Board of Kommunalkredit was enlarged to four members. The allocation of tasks and the procedures for cooperation within the Executive Board are determined in the rules of procedure of the Executive Board. The members of the Executive Board continuously exchange information among themselves and with staff members in executive positions reporting to them. The Executive Board provides the Supervisory Board with regular, timely and comprehensive information on all relevant issues of business development, including the risk position and risk management of the company and its material subsidiaries.

In addition, in the interest of good corporate governance, regular exchanges take place between the Chairman of the Supervisory Board and the Executive Board. These include in particular the definition of the company's strategy and information on the bank's performance and its risk management. The latter issues are regularly brought to the attention of the Chairman of the Risk Committee.

The agenda of the weekly Executive Board meetings comprises decision-making and reporting items, which are recorded in the minutes; follow-up items are agreed and strictly monitored.

Internal audit / Compliance and money laundering

Internal Audit reports monthly to the Executive Board and submits quarterly reports directly to the Supervisory Board. Apart from ongoing contacts within the framework of day-to-day business, compliance submits semi-annual written reports to the Executive Board. The compliance officer also acts as anti-money-laundering officer pursuant to § 23(3) of the Financial Markets Money Laundering Act (*FM-GwG – Finanzmarkt-Geldwäschegesetz*) and, as such, is responsible for measures to ensure compliance with the provisions of the Financial Markets Money Laundering Act, in particular the duties of diligence vis-à-vis customers as laid down in §§ 5ff. The semi-annual AML and compliance reports are also submitted to the Supervisory Board.

Capital Adequacy

In accordance with the agreed allocation of tasks, the members of the Executive Board share the responsibility for ICAAP (Internal Capital Adequacy Assessment Process). ICAAP is a core element of Pillar 2 of the Basel Accord, comprising all procedures and measures applied by a bank to secure appropriate identification, measurement and limitation of risks, a level of capitalisation in line with the risk profile of the business model, and the use and continuous further development of suitable risk management systems.

Kommunalkredit uses a detailed risk-bearing-capacity analysis for the quantitative assessment of its capital adequacy. Depending on the target pursued, three different control loops are applied:

- Regulatory control loop
- Economic control loop (liquidation perspective)
- Going-concern control loop

Furthermore, regular stress tests are performed to test the robustness of the business model and to ensure the adequacy of the bank's capitalisation.

The risk management and ICAAP methods of the bank are reviewed annually. The monthly meetings of the Risk Management Committee (RMC) deal with credit, liquidity, market, operational and other risks on the basis of comprehensive reports. Other committees dealing with credit, capital and liquidity issues meet at least once a week (see also Notes to the Consolidated Financial Statements of the Kommunalkredit Group).

ASSETS, FINANCIAL POSITION AND INCOME

Financial performance indicators of Kommunalkredit Austria AG according to Austrian Company Code

Selected balance sheet figures in EUR m	31/12/2017	31/12/2016
Total assets	3,273.5	3,268.8
Cash and balances with central banks	318.1	310.5
Public-sector debt instruments and bonds	285.4	204.3
Loans and advances to banks	139.5	100.0
Loans and advances to custmers	2,439.4	2,556.8
Amounts owed to banks	534.7	795.6
Amounts owed to customers	1,038.9	538.2
Securitised liablities	1,289.8	1,535.5
Total of fund for general bankings risks (§ 57 (3) Austrian Banking Act)	40.0	40.0

Selected income statement figures in EUR m	1/1-31/12/2017	1/1-31/12/2016
Net interest income	32.8	36.2
Net fee and commission income	8.5	0.6
General administrative expenses	-45.7	-38.7
Other operating result	23.7	14.0
of which income from services provided for KA Finanz AG & Kommunalkredit Puclic Consulting	*14.1*	*13.2*
of which income from the transfer of real estate assets	*8.6*	*0.0*
Other operating expenses	-0.7	-11.6
of which stability tax	*-0.7*	*-11.6*
Operating result	**18.6**	**0.7**
Loan impairment, valuation and sales result	-0.2	54.8
Appropriation to provision (§ 57 (1) Austrian Banking Act)	-3.8	0.0
Profit on ordinary activities	**18.3**	**55.5**
Appropriation to the fund for general banking risks (§ 57 (3) Austrian Banking Act)	0.0	-25.0
Taxes on income	-0.1	7.0
Profit for the year after tax	**18.9**	**37.5**

Key indicators in EUR m or %	31/12/2017	31/12/2016
Total risk exposure amount pursuant to Art. 92 CRR (risk-weighted assets)	992.4	686.1
Own funds[1]	297.2	290.3
Total capital ratio	29.9%	42.3%
Common equity tier 1 after deductible items[1]	233.0	225.5
Common equity tier 1 ratio	23.5%	32.9
Number of shares	31,007,059	31,007,059

[1] Own funds/common equity tier 1 taking into account Kommunalkredit's profit for the year acording to Austrian GAAPof EUR 18.9m minus a proposed dividend of EUR 11.5m

Rating	31/12/2017	31/12/2016
Long-term DBRS	BBB (low)	BBB (low)
Short-term DBRS	R-2 (mid)	R-2 (mid)
Covered Bonds S&P	A	-

Balance sheet structure

As of 31 December 2017, total assets according to Austrian GAAP stood at EUR 3.3bn, nearly unchanged compared to the previous year, with loans and advances to customers of EUR 2.4bn (31/12/2016: EUR 2.6bn) and bonds and debt securities worth EUR 0.3bn (31/12/2016: EUR 0.2bn) accounting for the major part thereof.

Income position

Kommunalkredit's unconsolidated financial statements for 2017 prepared in accordance with Austrian GAAP showed an operating result of EUR 18.6m (2016: EUR 0.7m). This figure reflects the growing new business volume, which also led to rising interest and fee and commission income. Furthermore, the bank invested in new strategic initiatives, in particular in the launch of its new online retail platform KOMMUNALKREDIT INVEST. The front office team was strengthened through the recruitment of experienced experts with an international track record. In parallel, Kommunalkredit enacted a cost efficiency programme to streamline operational processes and the structure of the companies holding its participations.

Profit on ordinary activities totalled EUR 18.3m in 2017 (2016: EUR 55.5m), while after-tax profit for the year amounted to EUR 18.9m (2016: EUR 37.5m). The decrease compared to the previous year resulted mainly from one-off positive effects relating to the buyback of own issues not materialising to the same extent as in 2016. This, however, was fully in line with expectations and budget. As in the previous year, the loan impairment charge of EUR -0.3m reported for 2017 (2016: EUR 0.1m) was solely due to the changes to the general loan loss provision. No loan defaults were recorded in 2017. Kommunalkredit's non-performing-loan (NPL) ratio (definition of default according to Basel III) remained at 0.0%. The appropriation to the general risk provision pursuant to § 57 (1) of the Austrian Banking Act amounted to EUR 3.8m.

The material income and expense items are as follows:

- **Net interest income**
  Net interest income stood at EUR 32.8m (2016: EUR 36.2m), reflecting higher than expected income from new business in infrastructure financing and an expected reduction due to scheduled maturities in the existing portfolio, including funding.

- **Net fee and commission income**
  Net fee and commission income rose to EUR 8.5m in 2017 (2016: EUR 0.6m). This significant year-on-year increase by EUR 7.9m was mainly due to income from the lending business of EUR 9.2m (2016: EUR 0.9m) as well as a rise in income from services of EUR 0.9m (2016: EUR 0.2m). These amounts are booked against fee and commission expenses of EUR 1.7m (2016: EUR 0,6 Mio.). In addition to current transaction and payment fees, these expenses include in particular costs related to the issue of a social covered bond.

- **General administrative expenses**
  General administrative expenses stood at EUR -45.7m (2016: EUR 38.7m), comprising personnel expenses of EUR -29.8m (2016: EUR -23.2m) and other administrative expenses of EUR -15.9m. (2016: EUR -15.5m). The increase in general administrative expenses was mainly due to the following factors:

- Strengthening of the front office team through experienced experts with an international track record;
- Investments worth EUR 3.0m in new strategic initiatives such as the online retail platform KOMMUNALKREDIT INVEST;
- Expenses of EUR 2.7m in relation to a cost efficiency programme to streamline operational processes;
- Expenses of EUR 0.5m to implement new regulatory requirements (e.g. MiFiD 2, IFRS 9).

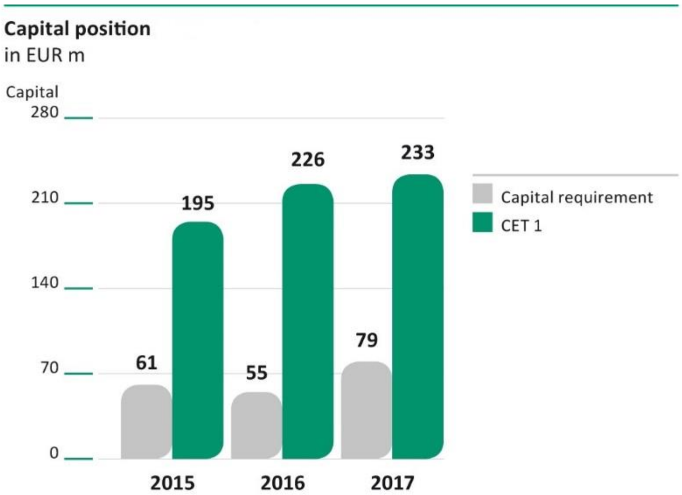
- **Other operating result**
  At EUR 23.7m, the other operating result rose by EUR 9.7m compared to the previous year (2016: EUR 14.0m). The other operating result comprises revenues generated from the provision of operational services for KA Finanz AG and Kommunalkredit Public Consulting GmbH in the amount of EUR 14.1m (2016: EUR 13.2m.). Under the bank's programme to streamline the legal structure of its real estate assets and participations, the transfer of real estate assets into a newly founded subsidiary generated a profit of EUR 8.6m.

- **Other operating expenses**
  Other operating expenses of EUR -0.7m (2016: EUR -11.6m) comprise only the stability tax payable by Austrian banks. In 2016, Kommunalkredit had decided to make a non-recurrent special payment of EUR 7.7m, which resulted in a substantial reduction of the stability tax for the business years from 2017 onwards.

- **Loan impairment, valuation and sales result**
  In 2017, the loan impairment, valuation and sales result stood at EUR -0.2m (2016: EUR 54.8m). The decline compared to the previous year was primarily due to the fact that as expected, positive one-off effects from the buyback of own issues did not occur to the same extent in 2017 (2017: EUR 6.2m, 2016: EUR 51.8m). As in the previous year, the loan impairment charge of EUR -0.3m reported for 2017 (2016: EUR 0.1m) was solely due to the changes to the general loan loss provision. No loan defaults were recorded in 2017. Kommunalkredit's non-performing-loan (NPL) ratio (definition of default according to Basel III) remained at 0.0 %.

Risk-weighted assets and regulatory own funds

As of 31 December 2017, Kommunalkredit's own funds totaled EUR 297.2m (31/12/2016: EUR 290.3m) and its common equity tier 1 capital (CET 1) stood at EUR 233.0m (31/12/2016: EUR 225.5m). During the reporting period of 2017, risk-weighted assets increased by 44.6% to EUR 992.4m (31/12/2016: EUR 686.1m) owing to a higher weighting of new business in infrastructure project finance compared to the decreasing portfolio with mostly Austrian public entities.



As of 31 December 2017, Kommunalkredit thus reported a total capital ratio of 29.9% (31.12.2016: 42.3%) and a CET 1 ratio of 23.5% (31/12/2016: 32.9%). The leverage ratio stood at 7.3% as of 31 December 2017 (31/12/2016: 7.2%).

Kommunalkredit has to comply with the own funds requirements as stipulated in article 92 CRR and the related Supervisory Review and Evaluation Process (SREP). Under these parameters Kommunalkredit had to maintain a minimum CET 1 ratio of 6.05%, a minimum core capital ratio of 7.65% and a minimum total capital ratio of 9.85% as of 31 December 2017; these ratios are significantly exceeded by the bank.

The foregoing figures reflect the regulatory capital indicators based on the unconsolidated financial statements of Kommunalkredit pursuant to the Austrian Company Code/Austrian Banking Act as reported in the financial statements for 2017. Equity already reflects a dividend of EUR 11.5m., which the Executive Board will propose at the annual shareholders' meeting for the business year 2017.

Kommunalkredit is also part of a group of credit institutions whose parent is Satere Beteiligungsverwaltungs GmbH (Satere). As of 31 December 2017, the consolidated total capital ratio shows 29.2% (31.12.2016: 42.3%), the consolidated CET 1 ratio shows 22.8% (31/12/2016: 32.9%).

Public sector covered bonds / Cover pool

As of 31 December 2017, Kommunalkredit had a well-diversified cover pool with a nominal value of EUR 1.3bn. At the same time, EUR- and CHF-denominated public-sector covered bonds in the nominal amount of approx. EUR 965m were outstanding. As of 31 December 2017, the cover pool comprised assets from Austria (96.9%), Germany (2.0%) and Poland (1.2%); 80.6% of the cover pool was rated "AAA" or "AA"; 19.4% of the cover pool assets had an "A" rating.

For its covered bonds in circulation, Kommunalkredit committed itself to maintaining a voluntary nominal over-collateralisation of approx. 10% of the redemption amount. As of 31 December 2017, the level of over-collateralisation was 30.3%.

Capitalisation – Dividend policy

Kommunalkredit since its privatisation in 2015 has enjoyed a very strong capital position. At year end 2017 this reflects a capital ratio of 29.9% with a CET 1 ratio of 23.5%. This is based on EUR 233.0m paid-in capital and capital reserves as well as EUR 64.2m tier 2 capital. As of 31 December 2017, the available capital exceeded the regulatory requirement by EUR 199.4m based on RWAs of EUR 992.4m. The bank has been investing excess capital in the build-up of new business; in the medium term a core capital ratio of around 15% is targeted. The foregoing capital position already reflects the dividend of EUR 11.5m, which the Executive Board will propose at the annual shareholders' meeting for the business year 2017.

The shareholders support the bank's strategy and growth plans to position Kommunalkredit as a leading player in the European infrastructure market. There are no predefined exit horizons for the shareholders' investment in Kommunalkredit. It is anticipated that additional capital will be available to support the bank's growth strategy. This also is evidenced by the availability of EUR 79.7m authorised capital implemented at the annual shareholders' meeting in March 2017.

NON-FINANCIAL PERFORMANCE INDICATORS

Employees

The average headcount of Kommunalkredit Austria AG in 2017 was 199 FTEs (full-time equivalents; 2016: 178). On average, 16 of these employees worked exclusively for KA Finanz AG (2016: 14); as of 31 December 2017, the corresponding number was 15 (2016: 18). The other employees of Kommunalkredit also provided operational services for KA Finanz AG under a service agreement (SA) and a service level agreement (SLA).

The remuneration policy and practice of the Kommunalkredit Group meet the legal requirements for variable remuneration in banks pursuant to § 39b of the Austrian Banking Act. The Supervisory Board has installed a remuneration committee. The principles of the bank's remuneration policy and practice are described in the Disclosure Report pursuant to Art. 450 CRR.

Communication

Kommunalkredit communicates actively and transparently with its stakeholders – the community, customers, business partners, investors, employees, regulatory authorities and shareholders. To engage in dialogue with its stakeholders, Kommunalkredit employs a broad range of communication tools. These include various forms of personal communication as well as digital media, classic public relations and direct marketing. Consistency in the bank's internal and external communication is ensured by the Corporate Communications unit.

In its external communication activities, Kommunalkredit in 2017 focussed on intensifying its presence in the media, both in the Austrian business media and in the international infrastructure press, and on promoting its two online investment platforms, KOMMUNALKREDIT DIREKT (for local authorities and corporates) and KOMMUNALKREDIT INVEST (for retail customers).

In Austria, Kommunalkredit has positioned itself as a knowledge platform for infrastructure and the municipal sector. It has developed a range of communication formats to address its main target groups, above all project sponsors with an emphasis on municipalities and institutional investors. One of the communication highlights in 2017 was the "Municipal Summer Symposium", a municipal-policy forum, which Kommunalkredit organised for the twelfth time in cooperation with the Association of Austrian Municipalities in 2017. In addition, Kommunalkredit presented the "Municipal Finance Report", which offers a detailed overview of the revenues and expenses of all cities and municipalities in Austria. The report has been published by the bank in close cooperation with the Association of Austrian Municipalities and the Association of Austrian Cities and Towns since 2005.

In its internal communication, Kommunalkredit makes every effort to ensure a transparent flow of information within the company. The bank uses a broad range of communication channels, from internal road shows to town hall meetings to communication via the intranet and the Kommunalkredit Academy, an internal portal with a variety of training options. The activities of the Sustainability Team and the Staff Council complement the active exchange of information.

To support its capital market activities, the Investor Relations unit intensified its direct contacts and conversations with investors and rating agencies, providing regular and transparent information about Kommunalkredit's development. Investor relations activities focused, above all, on the organisation of national and international roadshows as well as preparations for Kommunalkredit's return to the capital market with the social covered bond issue on 12 July 2017. These measures served to broaden the bank's stable base of investors and other stakeholders.

BRANCH OFFICES

As of 31 December 2017, Kommunalkredit had a branch office in Frankfurt am Main, Germany.

RESEARCH AND DEVELOPMENT

Given the sector in which the company operates, statements on research and development do not apply.

SIGNIFICANT EVENTS AFTER THE BALANCE SHEET DATE

Online retail platform KOMMUNALKREDIT INVEST also launched in Germany

At the beginning of January 2018, Kommunalkredit also introduced its online retail platform KOMMUNALKREDIT INVEST in Germany. KOMMUNALKREDIT INVEST offers sight deposits as well as term deposits for terms of up to ten years.

Services for KA Finanz AG

In February 2018, KA Finanz AG published a tender for services currently provided by Kommunalkredit. The bank intends to submit an offer for the continuation of such services. A decision by KA Finanz AG is expected by midyear 2018. Should the bank not be awarded with a continuing contract, the service contract with KA Finanz AG will expire in the first half of 2019. In such case the operative capacity will be adjusted during a contractually existing transition period of 12 months.

IFRS 9

As of 1 January 2018, the new IFRS 9 accounting standard introducing new rules on the recognition and valuation of financial instruments (loans, securities etc.) has come into effect. Kommunalkredit applies the new rules according to the standard; first adoption of IFRS 9 is expected to result in an increase in IFRS equity by approx. EUR 10m to around EUR 294m compared to 31 December 2017.

RISK MANAGEMENT

Risk management strategies and procedures

The instruments used by Kommunalkredit for the complete identification of the risk drivers of the business model are risk assessments and a risk map. Within the framework of risk assessment, the main types of risk for the bank are identified through a structured analytical process. Based on the results of the assessment, a risk map is drawn up for the bank as a whole, which contains a definition of risks, broken down by risk type, and assesses the individual risks in terms of significance, risk transparency, control frequency and limitation. The risk map serves to establish a uniform understanding of the risk concept and a uniform view of risk priorities, and to review the system for completeness and identify potential control gaps. The types of risk covered are those which are classified as highly relevant, but are characterised by low risk transparency and a low control frequency and are therefore given top priority in respect of further development needs. This analysis is performed annually.

Within the framework of the risk strategy for the main types of risk, the Executive Board specifies the principles for their adequate management and limitation. For each main type of risk and each field of business, the economic risk is limited in accordance with the risk-bearing capacity (ICAAP – Internal Capital Adequacy Assessment Process and/or ILAAP – Internal Liquidity Adequacy Assessment Process) and the risk appetite of the bank. Monthly reviews are performed to check the level of utilisation of the risk budget, as well as the risk appetite, for the entire bank and to verify that it is not overrun. Counterparty limits as well as the operational risk limits for the open FX position are reviewed on a daily basis. Kommunalkredit's business operations do not include any trading activities.

Kommunalkredit has a trading book, but its use is strictly limited. The transactions exclusively are risk-free through-trading activities within the framework of the provision of customer services. Subject to this limited use, Kommunalkredit does not engage in any activities with the intention to trade or any other activities resulting in open positions in the trading book.

Organisational structure of risk management and risk monitoring

The overall responsibility for ICAAP lies with the Executive Board. The risk-policy principles and the risk strategy are derived from Kommunalkredit's business-policy strategy. The Executive Board also decides on the risk management procedures to be applied and regularly informs the Supervisory Board and/or its committees (above all the Risk Committee, the Audit Committee and the Credit Committee) on Kommunalkredit's risk position.

Kommunalkredit has established an organisational structure for risk management, which clearly defines and sets out the tasks, competences and responsibilities within the framework of the risk management process. Risk-taking organisational units (front office) are clearly separated from organisational units in charge of the monitoring and communication of risks (back office) at all levels up to the Executive Board.

The Chief Risk Officer (CRO) is a member of the Executive Board. The function receives technical and operational support from Risk Controlling and Credit Risk Management. Together, these functions independently perform the tasks of a risk management pursuant to § 39 (5) of the Austrian Banking Act and report directly to Kommunalkredit's Executive Board.

Thus, the organisational structure fully meets the regulatory requirement of separation between front-office and back-office functions.

Pursuant to § 39d of the Austrian Banking Act, a Risk Committee of the Supervisory Board has been set up. The committee's mandate includes, in particular, advising the management on the current and future risk appetite and risk strategy of the bank, monitoring the implementation of this risk strategy in connection with the management, monitoring and limitation of risks, and monitoring the capital position and the liquidity position of the bank. Besides the reports submitted by the Risk Committee, the Supervisory Board regularly receives information on the risk position of the bank through comprehensive quarterly risk reports and a monthly key data sheet showing the development of the most important capital, earnings and risk indicators.

Risks are managed and monitored by the Risk Management Committee (RMC), the Asset-Liability Committee (ALCO) and the Credit Committee.

The Risk Management Committee (RMC) constitutes the central element of the comprehensive risk management process, providing information to the Executive Board on the overall risk position of the bank on a monthly basis. In organisational terms, Risk Controlling is in charge of this committee. The RMC is responsible for the establishment of guidelines for the implementation of the risk strategy and is in charge of limit setting (except country and counterparty limits) and limit monitoring by type of risk.

The weekly Asset-Liability Committee (ALCO) supports the operational management of market and liquidity risks. In organisational terms, the Market Division is in charge of this committee. At its meetings, the committee evaluates the market situation, monitors the limits and discusses the management of interest rate and liquidity risks. In addition, a detailed daily liquidity monitoring process is in place.

The weekly Credit Committee (CC) meeting is the central element of the credit approval process and the continuous portfolio and single-name review process. In organisational terms, Credit Risk is responsible for this committee (analysis and assessment of single-name risks, casting of a second vote on credit approval and/or review, management of single-name risks and/or other risks, work-out cases, qualitative portfolio analyses and rating).

Risk Controlling is responsible for the quantification of risks and the aggregate risk cover as well as for the performance of stress tests.

The objective of asset and liability management is to optimise the use of capital resources in terms of risk and return within the framework of the bank's risk appetite and risk-bearing capacity.

The strategies, methods, reporting rules and organisational responsibilities for the management of risks are documented in writing in the ICAAP manual, in risk management manuals for each type of risk and in organisational guidelines, which can be downloaded via the Intranet in their current versions at any time by all staff members concerned.

The following types of risk were identified up to the balance sheet date and are continuously monitored at Kommunalkredit:

- **Credit risk**
  Default and counterparty risk
  Replacement risk in the event of counterparty default
  Rating migration risk
  Investment risk
  Country and/or transfer risk
  Settlement risk
  Securitisation risk
  Cluster risk
  Concentration risk

- **Liquidity risk**
  Structural liquidity risk
  Funding risk
  Market liquidity risk

- **Market risk**
  Interest rate risk – banking book
  Interest rate risk – trading book
  Currency risk
  Commodity risk
  Credit spread risk
  Basis spread risk
  Option price risk
  OIS risk

- **Operational risk**
  Risks from human failure, processes, systems and external risks
  Legal risk
  Risk from service level agreement (SLA) with KA Finanz AG
  ICT risk

- **Funding risk**
  BCVA risk*
  Replacement risk through rating trigger
  ** comprises CVA risk and DVA risk and is allocated in its entirety to the funding risk*

- **Other risks**
  Strategic risk
  Risk from demerger liability
  Equity risk
  Reputational risk
  Business risk
  Excessive debt risk
  Risk of money laundering and terrorism financing
  Systemic risk from a financial institution
  Macroeconomic risk
  Placement and syndication risk

A formalised and structured approval and implementation procedure has been set up for the introduction of new fields of business, new markets or new products, ensuring that these are adequately reflected in all areas of settlement, risk management and reporting, accounting and financial reporting.

Risk-policy guidelines for risk management

The guidelines followed at Kommunalkredit are based on the following risk management principles:

- The limitation of risks at Kommunalkredit is commensurate with the bank's earning strength and its equity base.
- Kommunalkredit supports a risk culture characterised by a deliberate management of risks in day-to-day business, observance of the agreed risk appetite and the promotion of open dialogue on risk-related issues at all levels.
- The expertise of Kommunalkredit staff and the systems in place must correspond to the complexity of the business model and have to be developed together with the core fields of business.
- In terms of organisational structure, a clear separation between risk-taking on the one hand and risk calculation and/or risk management on the other hand is essential. Conflicts of interest for staff members are avoided through a clear separation of the different fields of activity.
- Risk management is an integral component of the business process and is based on recognised methods of risk measurement, monitoring and control. For credit and market risks, this principle is applied on an economic basis (value-at-risk approach).
- All measurable risks are subject to a limit structure; regular monitoring of the observance of limits on the basis of transparent and uniform principles is obligatory. An escalation process applies in the event of limit breaches. A capital buffer is kept for risks that have been identified but are not/not yet sufficiently measurable.
- The risk measurement results have to be subjected to regular stress testing and taken into account in determining the risk-bearing capacity of the credit institution. The results of stress testing have to be related to a limit and/or a hedging target.
- Kommunalkredit's system of risk management provides for comprehensive, regular and standardised risk reporting, with reports on the risk position of Kommunalkredit being produced at least once a month and, if necessary, supplemented by ad-hoc risk reports.
- An integrated IT infrastructure, as a prerequisite for the systematic reduction of risks from interfaces and data inconsistencies and as a basis for efficient reporting and data processing, constitutes an essential organisational and risk-policy objective.
- Core areas of the banking business and important control functions are not outsourced, unless an adequate level of know-how and experience is maintained within the bank.

Securing minimum capital adequacy

ICAAP (Internal Capital Adequacy Assessment Process) and ILAAP (Internal Liquidity Adequacy Assessment Process) are core elements of Pillar 2 of the Basel Accord and comprise all procedures and measures applied by a bank to ensure the appropriate identification, measurement and limitation of risks, a level of capitalisation in line with the risk profile of the business model, and the use and continuous further development of suitable risk management systems.

For the main types of risk (in particular: liquidity risk, credit default risk, market risk and syndication risk), the economic capital required to cover the risk is calculated according to recognised internal bank management procedures. In addition, a risk buffer is provided to cover risks that cannot be adequately quantified (in particular: operational risk, reputational risk, legal risks and other risks) as well as potential model inaccuracies. The economic perspective serves to secure adequate long-term capitalisation of the bank.

Kommunalkredit uses the method of risk-bearing-capacity analysis for the quantitative assessment of its capital adequacy, by which the economic risks are compared with the risk coverage potential. Depending on the hedging target pursued, two economic control loops are applied:

- **Liquidation perspective**
  (economic control loop based on the principle of creditor protection)

  Target: The main focus is on the protection of creditors and on securing a level of capitalisation to ensure that, in the event of liquidation of the company, all lenders can be satisfied with a defined probability.

  Economic capital requirements (internal risk measurement) are compared with the company's own funds, adjusted for hidden burdens and reserves. The aggregate risk cover is determined on the basis of its present value ("full fair value" approach) and is therefore not subject to accounting and measurement rules. A confidence level of 99.95% is used in determining the economic risk.

  Risk status: As at 31 December 2017, the economic risks correspond to 26.3% (31/12/2016: 19.9%) of the aggregate risk cover, the **risk buffer** being **73.7%** (31/12/2016: 80.1%).

- **Going concern perspective**
  (economic control loop based on the going-concern principle)

  Target: If the risks materialise, the survival of the bank as a going concern without additional equity is to be ensured with a defined degree of probability. The defined level of protection from risk under the going-concern perspective is a minimum tier 1 ratio of 13%.

  All risks impacting on profit and loss must be covered by the budgeted annual result, realisable reserves and the "free tier 1" capital. Free tier 1 is the tier 1 portion over and above the capital required to secure a tier 1 ratio of 13%. The aggregate risk cover is broken down into primary and secondary coverage potential, always considering possible realisation and external effects; early warning levels have been introduced. A confidence level of 95% is used in determining the economic risk.

  Risk status: As at 31 December 2017, the economic risks correspond to 43.1% (31/12/2016: 32.2%) of the aggregate risk cover, the **risk buffer** being **56.9%** (31/12/2016: 67.8%).

Additionally, stress tests are performed regularly to test the robustness of the business model and to ensure capital adequacy. For this purpose, two different economic scenarios (general recession scenario and portfolio-specific stress) are defined and their impact on the bank's risk-bearing capacity is quantified. In addition to the stressed risk-bearing capacity, a stressed three-year budget is drawn up for each scenario in order to test the stability of the business model over time. Besides the macroeconomic stress tests, reverse stress tests are performed. These are intended to show the extent to which parameters and risks can be stressed before regulatory or internal minimum requirements can no longer be met.

Credit risk management

Credit risk is the risk of financial losses arising from a counterparty not meeting its contractual payment obligations.

Personal forms of collateral (sureties and guarantees) play an important role in securing credit exposures. If personal collateral is available, the exposure can be counted towards the collateral giver, depending on the assessment of the risk, and included in the portfolio model and the limit system. Financial collateral include netting arrangements and cash collateral that reduce the counterparty risk. Financial collateral received reduces the existing exposure.

Based on the current CRR standardised approach for all classes of receivables, Kommunalkredit primarily uses external ratings. If no external ratings are available, ratings are derived from internal scoring and/or rating models for internal risk control. Every active customer is assigned an external or internal rating, which is updated at least once a year. Thus, assets on the banking book and off-balance-sheet transactions can be classified fully according to probability of default and collateralisation. On the basis of an internal rating scale (master scale), the probabilities of default are grouped in categories, to which external ratings can be assigned. To ensure a uniform system of determining the probabilities of default, all internal and external rating procedures and/or ratings have to be calibrated against the master scale. The discriminatory power of the rating procedures and their ability to forecast defaults are checked regularly and adjusted, if necessary.

Unexpected loss

To quantify the unexpected loss, monthly credit VaR calculations are performed to manage and limit the risk and to determine the economic capital required within the framework of risk-bearing-capacity analyses. Kommunalkredit uses a default model based on the CreditRisk+ approach to quantify the risk of unexpected default for credit risks. To calculate the credit VaR, rating-dependent one-year probabilities of default (PD) as well as regional and sector-specific loss ratios (LGD) are used. These parameters are reviewed and updated at least once a year and documented in a validation report.

From the **liquidation perspective**, the potential unexpected loss from credit defaults for a holding period of one year as at 31 December 2017 amounted to 5.8% (31/12/2016: 4.3%) relative to the economic aggregate risk cover.

From the **going-concern perspective**, the potential unexpected loss from credit defaults for a holding period of one year as at 31 December 2017 amounted to 14.6% (31/12/2016: 4.2%) relative to the economic aggregate risk cover.

The model used is based on statistical methods and assumptions. It should be pointed out, however, that statistically well-founded conclusions drawn from the past do not always apply to future developments. To take account of this fact, the model calculations are supplemented by additional, event-triggered analyses and regular stress tests, and adequate risk buffers are maintained.

Breakdown by rating

The breakdown of credit exposure by rating shows that the exposure is concentrated in the top rating categories: as at 31 December 2017, 46.4% (31/12/2016: 60.8%) of the exposure was rated “AAA”/“AA”, 89.4% was rated investment grade. Overall, the Kommunalkredit portfolio has a high asset quality; the exposure-weighted average rating of the total exposure is “A” (according to Standard & Poor’s rating scale).

Breakdown of exposure* by rating 31/12/2017 in EUR million	Exposure	Proportion	of which securities	of which guarantees	of which loans
AAA	17.9	0.6%	0.0	0.0	17.9
AA	1,337.2	45.7%	93.9	0.0	1,242.7
A	461.9	15.8%	46.6	0.0	348.1
BBB	795.3	27.2%	145.0	6.0	599.2
BB	249.7	8.5%	0.0	0.0	249.7
B	61.1	2.1%	0.0	0.0	61.1
CCC	0.0	0.0%	0.0	0.0	0.0
D	0.0	0.0%	0.0	0.0	0.0
not rated	0.0	0.0%	0.0	0.0	0.0
Total	**2,923.3**	**100%**	**285.4**	**6.0**	**2,518.8**

* Breakdown of exposure according to S&P rating scale

Breakdown of exposure* by rating 31/12/2016 in EUR million	Exposure	Proportion	of which securities	of which guarantees	of which loans
AAA	48.2	1.7 %	0.0	0.0	48.2
AA	1,694.6	59.1 %	96.3	0.0	1,595.5
A	693.3	24.2 %	108.1	0.0	513.2
BBB	392.0	13.7 %	10.8	9.5	326.3
BB	24.9	0.9 %	0.0	0.0	24.9
B	15.4	0.5 %	0.0	0.0	15.4
CCC	0.0	0.0 %	0.0	0.0	0.0
D	0.0	0.0 %	0.0	0.0	0.0
not rated	0.0	0.0 %	0.0	0.0	0.0
Total	**2,868.5**	**100.0 %**	**215.1**	**9.5**	**2,523.5**

* Breakdown of exposure according to S&P rating scale

Concentration risk

Risk concentrations are taken into account in the process of loan origination, monitored in the course of the monthly credit risk reports to the RMC, and shown in reports to the Credit Committee and the Supervisory Board. The total portfolio is broken down according to different parameters (breakdown by country, region, top 20/100 groups of related customers, rating, sector); limits are set by top risk drivers, sectors and geographic regions. In addition, risk concentrations in individual sub-portfolios are identified by Credit Risk Management, which performs sub-portfolio analyses. Portfolio analyses comprise correlating regional and/or sectorial risks or risk concentrations and permit the early detection, limitation and management of risk portfolios under current and future conditions. Depending on the risk assessment, reviews are performed at different intervals, but at least once a year. Event-triggered portfolio reviews may also be required on an ad-hoc basis and between the scheduled intervals.

The exposure to the top-20 “group of related customers” comprises an exposure of EUR 0.7bn (EUR 1.1bn) to the Republic of Austria and the Austrian provinces, accounting for 44.2% (31/12/2016: 55.1%) of the total exposure. It includes broadly diversified mortgage loans in a total amount of EUR 151.4m (31/12/2016: EUR 156.0m) that are guaranteed by the Austrian provinces concerned. Excluding Austria and the Austrian provinces, the exposure to the top-20 “group of related customers” comprises 25.3% (31/12/2016: 21.8%) of the total exposure.

Economic country risk

Credit exposures are reported for the purpose of internal risk management on the basis of the economic country risk. Kommunalkredit’s country risk is reported monthly to the RCM and at least once a year to the Credit Committee of the Supervisory Board. For each country, information on the country rating, exposure by product type, expected and unexpected loss, and limit utilisation is monitored.

Geographically, most of the exposure is accounted for by EU Member States (EU, incl. Austria, 98.2%). The exposure to non-EU Europe, i.e. 0.3% (31/12/2016: 0.4%) of the total exposure, is accounted for entirely by Switzerland. As at 31 December 2017, Kommunalkredit had no exposure to Greece and Ukraine.

Breakdown of exposure by region 31/12/2017 in EUR million	Exposure	Proportion	of which securities	of which guarantees	of which loans
Austria	1,826.2	62.5%	79.5	1.5	1,744.0
EU-28 (European Union excl. Austria)	1,044.0	35.7%	193.5	4.5	739.5
of which EU-19 (euro area excl. Austria)	564.2	19.3%	80.4	4.5	423.2
Non-EU Europe	9.0	0.3%	0.0	0.0	4.3
Other	44.1	1.5%	12.4	0.0	31.1
Total	**2,923.3**	**100.0%**	**285.4**	**6.0**	**2,518.8**

Breakdown of exposure by region 31/12/2016 in EUR million	Exposure	Proportion	of which securities	of which guarantees	of which loans
Austria	2,256.6	79.0 %	96.3	9.1	2,137.7
EU-28 (European Union excl. Austria)	589.7	20.6 %	118.9	0.4	375.4
of which EU-18 (euro area excl. Austria)	*379.7*	*13.2 %*	*10.8*	*0.4*	*297.8*
Non-EU Europe	11.5	0.4 %	0.0	0.0	10.3
Other	1.7	0.1 %	0.0	0.0	0.0
Total	**2,868.5**	**100.0 %**	**215.1**	**9.5**	**2,523.5**

Exposure to sovereigns and territorial authorities as at 31 December 2017

Direct exposures to sovereigns and territorial authorities as well as exposures guaranteed by sovereigns in the countries of the euro area (EU-19) are broken down as follows:

31/12/2017 in EUR million	Exposure	of which sovereigns	of which territorial authorities	of which government-guaranteed
Austria	1,346.1	0.0	1,346.1	0.0
Germany	25.1	0.0	7.2	17.8
Ireland	10.2	10.2	0.0	0.0
Slovakia	10.6	10.6	0.0	0.0
Slovenia	15.7	15.7	0.0	0.0
Italy	10.3	10.3	0.0	0.0
Lithuania	10.2	10.2	0.0	0.0
Spain	21.3	16.0	5.4	0.0

The comparative values of the previous year are as follows:

31/12/2016 in EUR million	Exposure	of which sovereigns	of which territorial authorities	of which government-guaranteed
Austria	1,671.2	0.0	1,671.2	0.0
Germany	56.6	0.0	36.8	19.8
Ireland	0.0	0.0	0.0	0.0
Slovakia	0.0	0.0	0.0	0.0
Slovenia	0.0	0.0	0.0	0.0
Italy	0.0	0.0	0.0	0.0
Lithuania	0.0	0.0	0.0	0.0
Spain	10.8	10.8	0.0	0.0

Except for Austria and Germany, these exposures concern, in particular, securities held for liquidity control.

Exposure to Austrian provinces as at 31 December 2017

Of Kommunalkredit's total exposure to Austria in a volume of EUR 1,826.2m (31/12/2016: EUR 2,265.6m), the following exposures are to Austrian provinces and/or provincial entities guaranteed by provincial governments:

31/12/2017 in EUR million	Direct exposure	Exposure guaranteed by provincial government	Total exposure
Province of Upper Austria	3.4	95.8	99.2
Province of Lower Austria	33.7	94.1	127.8
Province of Carinthia	0.0	127.1	127.1
Province of Styria	0.0	49.8	49.8
Province of Burgenland	0.0	99.5	99.5
City of Vienna	16.8	0.0	16.8
Total	**53.9**	**466.3**	**520.2**

The comparative values of the previous year are as follows:

31/12/2016 in EUR million	Direct exposure	Exposure guaranteed by provincial government	Total exposure
Province of Upper Austria	7.3	237.1	244.4
Province of Lower Austria	33.8	122.3	156.1
Province of Carinthia	0.0	147.7	147.7
Province of Styria	0.0	114.1	114.1
Province of Burgenland	0.0	101.9	101.9
City of Vienna	20.7	0.0	20.7
Total	**61.8**	**723.1**	**784.9**

In addition to the exposures listed in the above table, Kommunalkredit holds housing loans of Austrian provinces secured by mortgages in a total volume of EUR 151.4m (31/12/2016: EUR 155.6m), which are guaranteed by the provinces concerned (Burgenland EUR 97.1m (31/12/2016: EUR 101.4m); Upper Austria EUR 54.3m (31/12/2016: EUR 54.2m)).

Portfolio quality

Given the good ratings (weighted average rating of the total portfolio "A") and the degree of diversification, the portfolio quality is sound. This is also reflected in the non-performing-loan ratio of 0.00% as at 31 December 2017 (31/12/2016: 0.0%). Kommunalkredit had no financial assets (receivables) on its books that were more than 90 days past due, nor any substantial payment arrears of between 0 and 90 days.

Loan loss provisions

The portfolio is reviewed regularly for objective indications of impairments of customer exposures or exposures to groups of related customers. Assessments of impairment are performed in the course of the annual rating updates, the annual rating review or on an event-triggered basis. Impairments to be booked for defaulting loans are determined by Risk Management, subject to approval by the Executive Board.

Counterparties with increased credit risk

A multi-stage risk control process is applied to identify, monitor and manage counterparties with increased credit risks; all exposures/counterparties are classified in four risk classes.

- Risk class 0: Regular business
- Risk class 1: Intensive management / performing
- Risk class 2: Workout / restructuring
- Risk class 3: Workout / resolution

As at 31 December 2017, the exposure in risk class 1 (intensive management/performing) amounted to EUR 23.4m (31/12/2016: EUR 24.1m). None of Kommunalkredit's exposures are classified as risk classes 2 and 3.

Credit Risk Management continuously updates the list of counterparties with increased credit risk and submits monthly reports to the Credit Committee meeting, which then decides on the measures to be taken.

Investment risk

Given the nature of the participations held, the investment risk is of minor importance. As at 31 December 2017, the book value of investments in associates (at equity) was EUR 0.0m (31/12/2016: EUR 0.0m; for details see Note 18). The book value of investments in assets available for sale amounted to EUR 2.8m (31/12/2016: EUR 3.0m).

Counterparty default risk from derivatives, repo transactions and securities transactions

Legally binding netting arrangements for derivatives and repo transactions (close-out netting) have been concluded with all active counterparties of Kommunalkredit. For derivatives, credit support agreements and/or collateral annexes to framework contracts providing for daily collateral margining in accordance with the bilateral collateralisation requirement of the European Market Infrastructure Regulation (EMIR) have been concluded with all active financial counterparties. The only exception are derivative agreements in the cover pool, for which framework agreements and netting arrangements have been made at market conditions (unilateral collateralisation by the counterparty, rating trigger).

The exposure to the counterparty default risk of derivatives, which is taken into account in credit risk, is defined as the residual risk from the current replacement cost (positive market value), considering CSAs and netting arrangements, plus an "add-on" for potential market value changes during the so-called "residual period of risk" between the default of the counterparty and the closing out/replacement of the derivative transaction.

Repo transactions are cleared in the form of genuine repos mainly via platforms with daily margining.

If in repo or securities lending transactions, a counterparty default risk results for Kommunalkredit from the difference between the liability/receivable and the market value of the corresponding collateral put up/received, this risk counts as exposure to the counterparty and is taken into account in credit risk.

Securities transactions are cleared exclusively on the basis of "delivery against payment" via Euroclear and/or Clearstream.

Counterparty default risk positions are limited through volume-based counterparty and credit concentration limits, on the one hand, and credit-VaR-based portfolio limits, on the other hand. Given the settlement and clearing principles described above, the counterparty default risk from derivatives, repo transactions and securities transactions is immaterial.

The counterparty default risk from derivatives is calculated as a credit valuation adjustment (CVA) according to IFRS 13. Kommunalkredit calculates CVA and DVA (debt valuation adjustment), aggregated as BCVA (bilateral CVA), on the basis of the potential exposure method by means of Monte Carlo simulations. The risk of BCVA fluctuations (BCVA risk) is determined by means of a VaR-based approach.

Liquidity risk management

Based on the ILAAP (Internal Liquidity Adequacy Assessment Process) definition, Kommunalkredit distinguishes between the structural liquidity risk, the funding risk and the market liquidity risk. The structural liquidity risk (liquidity risk in the narrow sense of the term) arises if follow-up financing for asset portfolios cannot be secured according to the maturity schedules. The funding risk is determined by the degree of diversification of funding sources and the risk of potentially restricted access to certain main funding markets under stressed market conditions. The market liquidity risk consists in a possible increase of liquidity costs due to bank-specific or idiosyncratic factors (liability-side market liquidity risk), on the one hand, and the necessary acceptance of discounts or time delays in the realisation of a position due to its relative size and/or the absence of a liquid market (asset-side market liquidity risk), on the other hand.

Kommunalkredit distinguishes between short-term (up to one year) and long-term (more than one year) liquidity management.

Central elements of liquidity risk management include the following:

- Analysis of the liquidity position
- Reporting to the Executive Board and the Supervisory Board
- Determination of the medium- and long-term funding requirements, including a liquidity plan
- Scenario-based dynamic liquidity forecast and liquidity coverage ratio (LCR) simulation
- Management and further development of the liquidity model
- Regular review and setting of internal transfer prices
- Securing of operational liquidity by defining time-to-wall hedging targets for the base case and the stress case. Thus, the survival of the bank for the defined minimum period is secured even without access to money and capital markets.
- Internal limitation of maturity transformation by setting limits on structural liquidity gaps
- Regulatory limitation of maturity transformation through the liquidity coverage ratio and the net stable funding ratio
- A liquidity emergency plan with clearly defined responsibilities, reporting requirements and measures is in place in case a liquidity crisis occurs.

Operational liquidity risk (< 1 year)

For the purposes of short-term liquidity management, the management uses short- and medium-term liquidity scenarios drawn up on a daily basis. These scenarios include not only contractually determined cash flows, but also expected cash flows from new issues, the termination of transactions, cash-out from new transactions, cash inflows from syndication agreements, retail deposits repayable on demand, repo prolongations and liquidity demand for cash collateral received (under credit support agreements/ISDA arrangements). The resulting liquidity gaps are managed daily in the short-term liquidity scenario, subsequently to be followed by monthly management.

The following table shows the expected liquidity gaps after the measures planned, the free liquidity reserve, and the net liquidity position resulting from the liquidity gap and the liquidity reserve:

31/12/2017 in EUR million	Expected liquidity gap	Available liquidity	Liquidity position
Up to one month	273.9	183.7	457.6
More than one month up to three months	97.5	16.9	114.5
More than three months up to one year	214.5	-19.8	194.7
Total	**585.9**	**180.9**	**766.8**

The comparative figures for 2016 are as follows:

31/12/2016 in EUR million	Expected liquidity gap	Available liquidity	Liquidity position
Up to one month	396.2	205.3	601.5
More than one month up to three months	-201.2	-67.3	-268.6
More than three months up to one year	237.6	-37.7	199.9
Total	**432.6**	**100.3**	**532.9**

The capital-weighted residual maturity of liabilities exceeds that of assets. Moreover, Kommunalkredit has a large portfolio of free assets eligible as collateral.

The daily management of cash collateral for derivative contracts practiced at Kommunalkredit greatly reduces the credit risk.

Structural liquidity risk (>= 1 year)

For the purposes of liquidity management and the structural analysis of its liquidity risk position, Kommunalkredit analyses the expected capital flows over the entire term of all on-balance and off-balance transactions. Overhangs from capital inflows and capital outflows are monitored by maturity range and at cumulative level and provide the basis for strategic liquidity management.

Organisation and reporting

A liquidity forecast, including an assessment of the additional liquidity available, is drawn up every other day, reported regularly to the Executive Board member in charge and submitted monthly to the full Executive Board within the framework of the RMC. In addition, weekly ALCO meetings on operational and strategic liquidity management are held. The long-term liquidity risk is monitored and managed by the monthly RMC.

Emergency plan

The bank’s liquidity emergency plan specifies the tasks and the composition of emergency units to be set up in a crisis, the internal and external communication channels and, if necessary, the measures to be taken. The emergency plan permits efficient liquidity management in a market environment in crisis and is activated by clearly defined events and/or early warning indicators. In the event of an emergency, liquidity management is taken over by the emergency unit, which then decides on the specific measures to be taken.

ILAAP

Introduced alongside ICAAP within the framework of Pillar 2 of the Basel Accord, the Internal Liquidity Adequacy Assessment Process (ILAAP) serves the purpose of safeguarding the adequacy of the bank's own liquidity risk management procedures.

The individual components of ILAAP cover:
- Liquidity risk strategy and tolerance
- Organisation / policies / processes
- Risk measurement and reporting
- Stress testing
- Liquidity ICS framework
- Emergency plan
- Funding plan

All ILAAP components form an integral part of the more comprehensive ICAAP, which covers all bank-specific risks, including the liquidity risks in all its forms.

Analysis of financial liabilities

The following table shows the maturities of contractual, non-discounted cash flows of financial liabilities as at 31 December 2017 (net for interest and currency swaps, gross for cross-currency swaps, positive value for pay-out overhang):

Cash flows in EUR million as at 31/12/2017	Liabilities at amortised cost	Derivatives designated as hedging instruments	Trading*
Up to one month	147.5	1.8	3.6
More than one month up to three months	125.4	0.9	31.1
More than three months up to one year	378.7	14.1	26.6
More than one year up to five years	1,515.0	26.6	64.6
More than 5 years	1,555.3	15.7	37.1
Total	**3,721.8**	**59.1**	**163.1**

* The derivatives are not formally embedded in a micro-hedge as defined in IFRS, but serve for risk management at portfolio level. Kommunalkredit does not engage in any trading activities.

As at 31 December 2017, the nominal amount of interest-rate and currency swaps was EUR 3.1bn (31/12/2016: EUR 3,3bn).

The comparative figures for 2016 are as follows:

Cash flows in EUR million as at 31/12/2016	Liability at amortised cost	Derivatives designated as hedging instrument	Trading*
Up to one month	1855	2.0	4.6
More than one month up to three months	442.1	1.4	11.2
More than three months up to one year	228.1	14.5	18.6
More than one year up to five years	1,026.7	57.5	77.3
More than five years	1,591.5	21.3	49.3
Total	**3,473.8**	**96.7**	**161.0**

* The derivatives are not formally embedded in a micro-hedge as defined in IFRS, but serve for risk management at portfolio level. Kommunalkredit does not engage in any trading activities.

Besides redemptions, the cash flows also comprise interest payments. For liabilities with variable cash flows, future cash flows are determined on the basis of forward rates.

As a matter of principle, the amounts are allocated on the basis of their contractual rather than expected residual maturity. If the date of repayment is at the lender's discretion, the amount is allocated to the maturity range with the earliest possible redemption. Payments that have been pledged but not yet called are included in liabilities at amortised cost.

Market risk management

Interest rate risk

For the measurement, management and limitation of interest rate risks from positions not held in the trading book, Kommunalkredit distinguishes between the period-oriented repricing risk and the NPV-oriented risk of changing interest rates.

For the purpose of efficiently managing the interest rate risk and net interest income, Kommunalkredit uses an analysis and simulation tool (interest rate gap structure by currency, interest rate VaR, sensitivity analyses, simulation trades), which permits the forecast and targeted management of the bank's interest rate risk from positions not held in the trading book, the P&L sensitivity of the fair value portfolio according to IFRS, and net interest income for the period. To calculate the interest rate VaR, the variance/co-variance approach with a holding period of 20 trading days and a confidence interval of 95% is used, based on equally weighted historical volatilities and correlations.

Kommunalkredit's portfolio mainly comprises positions with clearly defined interest rate and capital commitment. As a rule, non-linear risks are completely hedged. Open positions are strictly limited and monitored. Retail deposits include positions without clearly defined interest rate and capital commitment (deposits repayable on demand). In principle, the interest rate commitment of deposits repayable on demand is modelled as a function of the pricing strategy. Non-linear risks that are not hedged are quantified through a scenario analysis and added to the interest rate VaR. Kommunalkredit uses the fully integrated SAP/SEM-IT system for risk quantification.

For interest rate risk management by the RCM and ALCO, the gap structures, broken down by currency, are analysed and the price sensitivity of the overall position as well as the impact of interest rate changes on the net interest income of the period (repricing risk) are quantified for different scenarios. The repricing risk is measured daily for the main currencies of Kommunalkredit (EUR, USD, CHF, JPY) and communicated to Treasury as a basis for risk management.

For risk management purposes, Kommunalkredit differentiates between the following sub-portfolios:

- less-than-twelve-months interest-rate position (short-term ALM)
- more-than-twelve-months interest-rate position (long-term ALM)
- equity investment portfolio ("equity book")
- IFRS fair value position

An analysis and management tool is used for the daily management of short-term, less-than-twelve-months interest risk positions, which permits the efficient management of the repricing risk by currency.

- Annual net interest income effect from Kommunalkredit's repricing risk as at 31 December 2017 in EUR million in the event of a parallel rise of short-term interest by +100bp:

EUR	USD	CHF	JPY	Other	Total
+4.6	0.0	-0.3	0.0	0.0	**+4.3**

- NPV risk of interest rate changes in Kommunalkredit's banking book as at 31 December 2017 in EUR million in the event of a +25bp parallel shift in the yield curve:

EUR	USD	CHF	JPY	Other	Total	VAR total
+1.7	0.0	-0.2	+1.0	-0.4	**+2.1**	**-1.1**

- NPV risk of interest rate changes of the IFRS interest-rate risk position carrying through profit or loss in EUR million as at 31 December 2017 in the event of a +25bp parallel shift in the yield curve:

EUR	USD	CHF	JPY	Other	Total	VAR total
+3.6	0.0	-0.4	-0.1	0.0	**+3.1**	**-2.1**

The comparative figures for 201 are as follows:

- Annual net interest income effect from Kommunalkredit's repricing risk as at 31 December 2016 in EUR million in the event of a parallel rise of short-term interest by +100bp:

EUR	USD	CHF	JPY	Other	Total
-1.3	0.0	-0.6	+0.1	0.0	**-1.8**

- NPV risk of interest rate changes in Kommunalkredit's banking book as at 31 December 2016 in EUR million in the event of a +25bp parallel shift in the yield curve:

EUR	USD	CHF	JPY	Other	Total	VAR total
+1.4	-0.4	-0.3	+1.6	-0.4	**+1.9**	**-5.9**

- NPV risk of interest rate changes of the IFRS interest-rate risk position carrying through profit or loss in EUR million as at 31 December 2016 in the event of a +25bp parallel shift in the yield curve:

EUR	USD	CHF	JPY	Other	Total	VAR total
+4.5	0.0	-0.6	-0.1	0.0	**+3.8**	**-3.6**

Currency risk

The currency risk is the risk of losses in foreign currency positions caused by an unfavourable change in the exchange rate, the open FX position being the difference between the sum total of asset positions and the sum total of liability positions, including FX derivatives, in a given currency.

To measure the risk, a VaR of the open foreign currency position according to Austrian GAAP is determined daily, based on a variance/co-variance approach with a holding period of one trading day and a confidence interval of 99%, using exponentially weighted historical volatilities and correlations.

Except for a small residual position according to Austrian GAAP, the open FX position is closed daily.

The FX VaR as at 31 December 2017 was EUR 0.011m (as at 31/12/2016: EUR 0.011m).

Spread widening risk

The spread widening risk is the risk of losses in value due to market-related changes in credit spreads.

The credit spread risk of P&L according to IFRS in the event of spreads widening by one basis point (CS01) amounted to EUR -0.4m as at 31 December 2017 (as at 31/12/2016: EUR -0.4m), resulting from fair value portfolios against Austrian public borrowers.

Basis spread risk

The basis spread risk is the risk resulting from a change in basis spread, which is factored into the variable interest rate conditions for non-standard reference interest rates and payment frequencies.

Except for residual risks, the basis spread risk is hedged in the individual currencies.

As at 31 December 2017, the basis spread risk in the event of basis spreads widening by 1 basis point was EUR +0.1m (as at 31/12/2016: EUR +0.2m).

Option price risk

The option price risk for Kommunalkredit is the risk of changes in the market values of open option positions.

To measure the option price risk, a scenario matrix is used to determine interest rate shifts (-/+ 50bp), volatility shifts (-/+30%) and combined shifts.

The option price risk in the banking book calculated on the basis of the scenario matrix amounted to EUR -0.8m as at 31 December 2017 (as at 31/12/2016: EUR -0.7m). However, the open option price risk in the banking book results almost exclusively from unilateral call rights of Kommunalkredit for own issues (i.e. Kommunalkredit has the right to call). As at 31 December 2017, there were no P&L-relevant option price risks.

Operational risk

Kommunalkredit defines operational risk as the possibility of losses occurring due to the inadequacy or failure of internal processes, people and systems or as a result of external events. The legal risk is part of the operational risk. External events classified as pure credit risk, market risk, liquidity risk or other types of risk with no operational background are not covered by this definition. Operational risk management (ORM) is intended to generate added value for the bank through the ORM process.

An operational risk officer and a deputy have been appointed. Operational risk correspondents (ORC), appointed by the management in consultation with the operational risk officer, act as points of contact for the individual units and support the ORM process.

An operational default database as well as risk and control self-assessments are the instruments available for the management of operational risk. The operational default database represents a retrospective view, i.e. realised gains/losses from operational events in the past are recorded in the database and cleared for further processing by the line managers in charge. Operational risk and control self-assessments represent a prospective, future-oriented view. Risks are identified and their severity is subjectively assessed. At Kommunalkredit these assessments are performed as coached self-assessments, i.e. individual risks are assessed and evaluated by the units concerned. The entries in the operational default database serve as input and provide feedback for the revaluation of risks. The management is informed about operational risks at the monthly RMS meetings and on a quarterly basis at the Executive Board meetings.

Kommunalkredit uses the standardised approach to quantify its capital adequacy requirements. The capital held on this basis is significantly in excess of actual losses suffered in the past.

Business Continuity Management

Business continuity management (BCM) ensures the adequate, comprehensive and efficient management of business continuity. This includes the elaboration and management of continuity and re-start-up plans as well as the implementation of measures designed to minimise interruptions of critical business processes. This includes the provision of alternative workplaces in the event of Kommunalkredit’s office premises being out of order.

The annual resource assessment was performed, and the resources required in the event of a crisis were established. The annual business impact analysis (BIA), performed within the framework of the resource assessment, served to assess business processes and IT services for their criticality and to verify the time to full restoration of services. The emergency plans were revised at the same time. The annual emergency exercise was performed in the fourth quarter of 2017.

INTERNAL CONTROL SYSTEM (ICS)

Introduction

The objective of the internal control system (ICS) is to support the management in the implementation of effective and continuously improving internal controls, especially in terms of compliance with the relevant legal provisions, the regularity of accounting practices, the reliability of financial reporting and the effectiveness and efficiency of operational processes. The ICS is intended, on the one hand, to ensure compliance with guidelines and regulations and, on the other hand, to create the prerequisites for specific control measures to be applied in key accounting and financial reporting processes. Its primary goals include the correct and transparent disclosure of the assets, the financial position and the income of the company, as well as ensuring compliance with regulatory requirements.

The internal control system of Kommunalkredit comprises five interrelated components: control environment, risk assessment, control measures, information and communication, and supervision.

Control environment

The corporate culture as the overall framework for all management and staff activities represents the fundamental aspect of the control environment. Central organisational principles concern the avoidance of conflicts of interest through a strict segregation of front-office and back-office operations, the transparent documentation of core processes and control steps, as well as the consistent implementation of the four-eyes principle. Furthermore, areas of responsibility and the scope of action at top management level are defined and/or limited by the Supervisory Board committees with different functions and the rules of procedure for the Executive Board.

The internal audit unit independently audits all departments for compliance with the internal rules on a regular basis. The head of the internal audit unit and the compliance officer report directly to the Executive Board and the Supervisory Board.

Risk assessment

Kommunalkredit's risk management is aimed at discovering all identifiable risks and, if necessary, initiating defensive and preventive measures through optimised processes. The risk management system comprises all processes serving to identify, analyse and assess risks. Risks are assessed and monitored by the management. Special attention is paid to risks regarded as material. The internal control measures taken by the units in charge are evaluated on a regular basis.

Control measures

Kommunalkredit has a regulatory system which defines the structures, processes, functions and roles within the company as well as the related control activities. It provides explicit instructions on how to deal with and/or enforce standard operating procedures or guidelines.

This also applies to information processing, the documentation of information sent and received, as well as the avoidance of transaction errors.

All control measures are implemented to ensure that potential errors or non-compliances in financial reporting are prevented and/or discovered and corrected.

IT security control measures are an essential component of the internal control system. The separation of sensitive activities is supported through a restrictive policy of granting IT user authorisations; compliance with the four-eyes principle is strictly enforced.

Information and communication

The individual units of Kommunalkredit and, in particular, its risk controlling and/or accounting units, submit regular reports, including monthly and quarterly results, to the Executive Board, which in turn reports regularly to the Supervisory Board. The head of the internal audit unit and the compliance officer also report directly to the Supervisory Board. Furthermore, the risk managers of the credit risk management and risk controlling units report to the Risk Committee of the Supervisory Board.

Comprehensive reports are submitted to the Supervisory Board and its committees on a regular basis. The flow of information comprises the financial statements (balance sheet and income statement, budget and capital budget, deviations of actual figures from target figures, including comments on significant developments) of the company, comprehensive quarterly risk reports, as well as liquidity risk analyses by the treasury department and analyses of the activities of the market units. The shareholders, investors and market partners as well as the public are informed through the mid-year financial report and the annual financial report. Information is also communicated in the form of ad-hoc disclosures, as required by law.

Supervision

Financial statements to be published are subject to a final review, to be coordinated with the external auditor, and explicitly released by senior accounting staff and the Executive Board prior to their submission to the Audit Committee of the Supervisory Board.

By monitoring compliance with all rules, Kommunalkredit hopes to achieve a maximum level of security for all operational procedures and processes and ensure conformity with all group-wide and legal standards. If risks and weaknesses in the control system are detected, remedial and defensive measures are immediately established and implementation of the follow-up steps is monitored.

To ensure compliance with rules and guidelines throughout the bank, regular audits are performed in accordance with the annual audit plan drawn up by the internal audit unit.

SUSTAINABILITY

Sustainability firmly rooted in Kommunalkredit's business model

Kommunalkredit contributes to the sustainable success of infrastructure projects that improve the quality of people's lives and sustainability is firmly rooted in Kommunalkredit's business model.

An environmental management system according to the EMAS Regulation was established within Kommunalkredit already in 1997. Over the years, it has been developed into an integrated sustainability management system. The principles of sustainability are firmly embedded in Kommunalkredit's day-to-day activities and reflected in a broad range of measures. The importance attributed to a sustainable business model is also expressed in the issuance of the first Austrian social covered bond in 2017.

Kommunalkredit Public Consulting (KPC), a subsidiary of Kommunalkredit, contributes to the sustainable implementation of national and international environmental and climate protection projects. On the one hand, KPC develops and manages support programmes in the environment and energy sectors and contributes to the fight against global warming through Climate Austria, a voluntary carbon compensation programme. On the other hand, KPC supports the development and dissemination of environmental and technological standards through a range of consulting projects (e.g. establishment of credit lines for energy efficiency projects in Russia and the Western Balkan countries).

Sustainability ratings

Sustainability rating agencies have recognised and rewarded Kommunalkredit's commitment to its sustainability management system and its willingness to continuously improve its sustainability performance: In its most recent audit in 2016, Oekom research rated Kommunalkredit as a "PRIME company". The investment research unit of imug (Beratungsgesellschaft für sozial-ökologische Innovationen) recently confirmed its rating of "very positive" for Kommunalkredit's covered bonds. In 2017, Kommunalkredit was awarded "Qualified" status in the sustainability rating of rfu Mag. Reinhard Friesenbichler Unternehmensberatung, an Austrian company specialising in sustainable investment and sustainability analyses.

Ecological and social issues

A mindful use of resources – ranging from waste sorting and waste avoidance to recto/verso printing to ecologically minded business travel planning – is everyday practice at Kommunalkredit. Energy efficiency and the use of renewable resources, e.g. through a pellet-fired heating system in Kommunalkredit's office building and the use of green electricity as well as continuous optimisation of the IT infrastructure with regard to its energy consumption, is another priority. In addition, KPC offsets the CO_2 emissions caused by business travel via www.climateaustria.at.
Within the framework of the ongoing stakeholder dialogue, Kommunalkredit and KPC carried on with a number of cooperation projects in 2017, such as the series of events on "The Courage to be Sustainable" organised by the Austrian Environment Agency. Other cooperating partners include the Austrian Water and Waste Management Association and IG Lebenszyklus Bau, an organisation promoting the life-cycle approach in building construction, as well as the Austrian Society for Environment and Technology.

Internally, the Sustainability Team is a point of contact and a platform for the discussion of all topics and concerns relating to sustainability at the workplace and beyond. These include compliance with EMAS guidelines, a newsletter and information events, sustainability-related film viewings, the book and video lending library, and the sustainability award for private commitment.

Kommunalkredit's externally audited Sustainability Report for the business year 2016 was published in accordance with the GRI G4 standards on sustainability reporting. The Sustainability Report qualifies as an EMAS environmental declaration and can be downloaded at www.kommunalkredit.at. The Sustainability Report for 2017 will be available from June 2018.

COMPLIANCE AND MONEY LAUNDERING

The Standard Compliance Code of the Austrian banking sector (SCC) signed by Kommunalkredit specifies requirements of fairness and mutual confidence in the relations of banks with their customers that partly go beyond the provisions of the law.

Pursuant to the provisions of the law and the SCC, Kommunalkredit adopted an internal compliance code and introduced a compliance organisation headed by a compliance officer who reports to the Executive Board. In line with the SCC and the relevant legal provisions, the compliance code is primarily aimed at ensuring compliance with the relevant provisions of the Securities Supervision Act and the provisions on market abuse, especially through measures to prevent the abuse of inside information or market manipulation.

In addition, the compliance organisation of Kommunalkredit is responsible for taking the necessary measures to prevent any violation of legal provisions or internal policies that might jeopardise the reputation of the company. It also ensures that the compliance code is kept up to date and observed throughout the Group. The compliance officer of Kommunalkredit acts as a point of contact for all staff members, informing them regularly about the rules and regulations in effect.

In his capacity as anti-money-laundering officer, the compliance officer is also responsible for ensuring compliance with the provisions of the Financial Markets Money-Laundering Act.

OUTLOOK

The European Commission expects GDP growth in the euro zone to remain almost unchanged at 2.3% in 2018 (compared to 2.4% in 2017). [13] It projects a growth rate of 2.3% for Germany (2.2% in 2017) and 1.7% for France (1.6% in 2017). Forecasts for the UK are somewhat muted due to Brexit, with a growth rate of 1.3% (down from 1.5% in 2017).

These figures reflect a stable trend for the European economy, with balanced risks to the growth outlook. External risks relate to an overshooting of the euro exchange rate, geopolitical tensions, trade protectionism, vulnerability of emerging markets to global monetary policy tightening, adverse implications of the looming Brexit as well as the rebalancing of crude oil markets. Especially in the euro zone, however, economic growth momentum continues to be robust and broad-based, driven by private consumption and business investment. Furthermore, growth is supported by steadily rising income and profits as well as expanded lending spurred by favorable financing conditions. Additionally, euro zone exports benefit from stronger foreign demand which partially offsets the effect of the euro appreciation.

A major change of the interest rate landscape is not foreseen in the short term and rates are expected to remain at low levels throughout 2018, with an increasing trend anticipated in the medium term. In December 2017, the European Central Bank (ECB) signalled its intention to maintain its expansionary monetary policy for the euro zone. It will reduce its bond purchases by half to EUR 30bn per month, but continue the programme at least until September 2018.[14] The Bank of England announced that its interest-rate policy will depend largely on the outcome of the Brexit negotiations.[15] The Fed intends to continue its policy of step-by-step interest rate hikes and has announced three upward adjustments each for 2018 and 2019.

[13] European Commission, The autumn 2017 forecast.
[14] ECB, 14 September 2017.
[15] Bank of England, 2 November 2017.

In view of the above, conditions for the European infrastructure market are expected to be largely unchanged in 2018. After the steep rise in the previous year, Kommunalkredit expects demand for European infrastructure assets to remain high in 2018. The bank foresees numerous transactions in markets such as Germany, France, Spain, the UK and Scandinavia.

The progress achieved in the business year 2017 provides the bank with an excellent foundation for further business growth in 2018. The major objectives for 2017 were met or exceeded. New business volume contracted amounted to EUR 635.2m. The bank distributed a total volume of EUR 373.2m to institutional investors and banks, including EUR 194.2m from new business and EUR 179.0m from its historic portfolio. The majority of this was placed with asset managers, insurance companies and pension funds. The successful placement with such a variety of leading international investors from different market segments is a clear recognition of the bank's strengthened strategic position combined with an expanded geographic scope as well as project type, especially in the transportation sector. In parallel, the deposit base of the bank could be significantly expanded and with the launch of its online retail platform KOMMUNALKREDIT INVEST, the bank now also operates in the retail market for the first time. The progress on the business generation side goes hand in hand with an increase in efficiency of internal processes, which will lead to a reduction of the cost base in 2018.

Kommunalkredit has started the new business year with well-defined strategic and operative parameters. A dynamic project pipeline promises a continuation of a successful year in business origination and distribution. With a rising operating result and a continued decline in extraordinary income, Kommunalkredit expects its annual result for 2018 to be above the previous year's level. The evolution of the operating structure will depend on the outcome of the tender by KA Finanz AG for services currently provided by Kommunalkredit Austria AG. The bank intends to submit an offer for the continuation of such services. A decision by KA Finanz AG is expected by midyear 2018. Should the bank not be awarded with a continuing contract, the service contract with KA Finanz AG will expire in the first half of 2019. In such case the operative capacity will be adjusted during a contractually existing transition period of 12 months. In the medium term the bank targets a cost income ratio below 50%.

As of 1 January 2018, the new IFRS 9 accounting standard introducing new rules on the recognition and valuation of financial instruments (loans, securities etc.) has come into effect. Kommunalkredit applies the new rules according to the standard; first adoption of IFRS 9 is expected to result in an increase in IFRS equity by approx. EUR 10m to around EUR 294m compared to 31 December 2017.

Following a positive year 2017, Kommunalkredit Austria AG had a strong start into 2018 and is looking confidently forward to the opportunities and positive challenges of the current business year 2018.

Vienna, 5 March 2018

The Executive Board of
Kommunalkredit Austria AG

Alois Steinbichler	**Jörn Engelmann**	**Karl-Bernd Fislage**	**Wolfgang Meister**
Chief Executive Offer	Member of the Executive Board	Member of the Executive Board	Member of the Executive Board

REPORT OF THE SUPERVISORY BOARD TO THE SHAREHOLDERS' MEETING

The Supervisory Board of Kommunalkredit Austria AG (Kommunalkredit) submits its report on the business year 2017 to the Shareholders' Meeting.

The Supervisory Board comprises four capital representatives, two independent representatives and three employee representatives. As in the previous year, Patrick Bettscheider, delegated by Gesona Beteiligungsverwaltung GmbH, holds the position of Chairman of the Supervisory Board. The three other capital representatives, as in the previous year, are Christopher Guth, Deputy Chairman of the Supervisory Board and delegated by Attestor Capital, Katharina Gehra, Chief Operating Officer of Interritus Limited and Managing Director of Gesona Beteilgungsverwaltung GmbH, and Friedrich Andreae, Managing Director of Gesona Beteiligungsverwaltung GmbH. Jürgen Meisch, Managing Director of Achalm Capital GmbH, continues to exercise his mandate as an independent member of the Supervisory Board. Werner Muhm's mandate expired on 10 March 2017. Subsequently, Martin Rey, Managing Director of Maroban GmbH, was newly appointed to the Supervisory Board on 24 July 2017. The Supervisory Board members delegated by the Staff Council are Patrick Höller and Renate Schneider, as well as Franz Hofer, who resigned from the Supervisory Board on 6 November 2017. As successor to Franz Hofer, Paul Matousek was delegated to the Supervisory Board by the Staff Council as of 6 November 2017. The Supervisory Board wishes to thank all former members who resigned in the course of 2017 for their trust and cooperation.

As of 1 February 2016, Karl-Bernd Fislage was appointed Member the Executive Board responsible for Banking & Markets. At the time of reporting, the Executive Board consists of Chairman Alois Steinbichler (Chief Executive Officer), Wolfgang Meister (Chief Operating Officer), Jörn Engelmann (Chief Risk Officer) and Karl-Bernd Fislage (Banking & Markets).

Kommunalkredit looks back on a successful year. The bank has made substantial progress in its efforts to position itself as a strong market participant for infrastructure finance in Europe. Kommunalkredit succeeded in significantly expanding its new business, strengthening its funding base and investing in new strategic initiatives, such as the online retail platform KOMMUNALKREDIT INVEST. Kommunalkredit Public Consulting (KPC), a 90% subsidiary of Kommunalkredit, continues to operate in the field of support programme management.

The Supervisory Board performed its tasks, as defined in the Articles of Association and the Rules of Procedure, within the framework of four ordinary meetings and one constituent meeting. Moreover, the statutory committees (Nomination Committee, Audit Committee, Risk Committee, Remuneration Committee and Credit Committee) held their meetings and performed their tasks. The Rules of Procedure of the Supervisory Board were amended to allow for the exchange of Supervisory Board communication (i.e. circular resolutions, convocation of meetings, distribution of meeting documents/information) by secure electronic means. Moreover, on account of the enlargement of the Executive Board and the reorganisation of business units, the division of tasks and responsibilities among the Executive Board members was newly defined and adopted.

In the course of the meetings of the Supervisory Board and its committees, as well as through regular information obtained orally and in writing, the Supervisory Board was continuously updated on the development of business, the position and performance of the company and its business policy plans. In exercising its tasks conferred upon it by law, the Articles of Association and the Rules of Procedure, the Supervisory Board advised and supervised the Executive Board in the management of the company. In accordance with the fit-and-proper guideline (based on the European Banking Authority Guideline), the members of the Boards of the bank underwent comprehensive fit-and-proper training covering regulatory changes and/or innovations in the autumn of 2017.

These Financial Statements and the Management Report were audited by PwC Wirtschaftsprüfung GmbH Wirtschaftsprüfungs- und Steuerberatungsgesellschaft, Vienna. The audit did not result in any findings. Given that all legal requirements were complied with by the bank and the annual financial statements present a true and fair view of the assets and the financial position of the company as at 31 December 2017, the auditors issued an unqualified audit opinion. Having examined the financial statements, the Supervisory Board endorsed the result of the audit and approved the 2017 Financial Statements at its meeting on 6 March 2018, which were thus formally adopted. Moreover, the Consolidated Financial Statements as at 31 December 2017, including the Management Report, were examined and taken note of by the Supervisory Board.

Vienna, 5 March 2018

The Supervisory Board

Patrick Bettscheider
Chairman

SEPARATE FINANCIAL STATEMENTS OF KOMMUNALKREDIT AUSTRIA AG, VIENNA, FOR THE BUSINESS YEAR 2017

I. BALANCE SHEET (pursuant to the AUSTRIAN BANKING ACT)

	Assets in EUR	Notes		31/12/2017	31/12/2016
1.	**Cash and balances with central banks**			**318,108,147.58**	**310,456,734.99**
2.	**Public-sector debt instruments eligible as collateral for central bank funding**	4.1.		**196,613,929.01**	**108,082,753.04**
	Public-sector debt instruments		196,613,929.01		108,082,753.04
3.	**Loans and advances to banks**	4.2.		**139,452,580.85**	**100,048,911.29**
	a) repayable on demand		101,097,839.01		100,048,911.29
	b) other loans and advances		38,354,741.84		0.00
4.	**Loans and advances to customers**	4.3.		**2,439,396,863.31**	**2,556,794,611.57**
5.	**Bonds and other fixed-income securities**	4.4.		**88,784,895.58**	**96,257,372.41**
	a) of public issuers		81,746,822.44		80,752,135.67
	b) of other issuers		7,038,073.14		15,505,236.74
	including own bonds		*0.00*		*0.00*
6.	**Participations**	4.5.		**2,014,095.00**	**2,425,070.00**
	of which in banks		*0.00*		*0.00*
7.	**Investments in affiliated companies**	4.5.		**32,612,865.00**	**6,339,848.12**
	of which in banks		*0.00*	***0.00***	*0.00*
8.	**Intangible non-current assets**	4.6.		**191,401.59**	**288,747.33**
9.	**Property, plant and equipment**	4.6.		**2,960,788.45**	**1,904,193.39**
	of which land and buildings used by the credit institution within the framework of its own activities		*0.00*		*0.00*
10.	**Other assets**	4.7.		**38,650,054.90**	**74,242,221.64**
11.	**Accruals/deferrals**	4.8.		**7,271,187.41**	**4,818,489.93**
12.	**Deferred tax assets**	4.9.		**7,432,406.33**	**7,141,210.75**
	Total assets			**3,273,489,215.01**	**3,268,800,164.46**

	Off-balance-sheet items			
1.	Foreign assets		**1,078,432,821.01**	653,645,232.98

	Liabilities in EUR	Note		31/12/2017	31/12/2016
1.	**Amounts owed to banks**	4.10.		**534,704,697.44**	**795,561,529.21**
	a) repayable on demand		116,632,310.77		227,140,643.25
	b) with fixed maturity or period of call		418,072,386.67		568,420,885.96
2.	**Amounts owed to customers**	4.11.		**1,038,874,555.94**	**538,202,229.94**
	a) Other liabilities				
	aa) repayable on demand		213,537,338.01		6,855,252.88
	bb) with fixed maturity or period of call		825,337,217.93		531,346,977.06
3.	**Securitised liabilities**	4.12.		**1,289,836,740.95**	**1,535,524,848.46**
	a) bonds issued		862,466,869.06		1,052,395,150.03
	b) other securitised liabilities		427,369,871.89		483,129,698.43
4.	**Other liabilities**	4.13.		**65,728,797.76**	**42,489,869.38**
5.	**Accruals/deferrals**	4.14.		**12,413,614.20**	**4,897,579.25**
6.	**Provisions**	4.15.		19,748,299.93	**26,807,079.93**
	a) provisions for severance pay		4,154,224.64		4,482,116.51
	b) provisions for pensions		1,360,466.82		1,198,761.00
	c) tax provisions		7,602.76		0.00
	d) other		14,226,005.71		21,126,202.42
6.A	**Fund for general banking risks (§ 57 (3) Austrian Banking Act)**	4.16.		**40,000,000.00**	**40,000,000.00**
7.	**Supplementary capital**	4.17.		**67,527,328.62**	**67,527,648.04**
8.	**Subscribed capital**	4.18.		**159,491,290.16**	**159,491,290.16**
9.	**Revenue reserves**			**4,241,468.85**	**3,298,178.85**
	a) statutory reserve	4.19.	4,241,468.85		3,298,178.85
10.	**Statutory reserve pursuant to § 57 (5) Austrian Banking Act**	4.20.		**10,000,000.00**	**10,000,000.00**
11.	**Net profit**	4.21.		**30,922,421.16**	**44,999,911.24**
	Total liabilities			**3,273,489,215.01**	**3,268,800,164.46**

	Off-balance-sheet items				
1.	Contingent liabilities	5.1.		6,291,083.78	9,530,864.95
	of which:				
	liabilities from sureties and guarantees and				
	liabilities from the assignment of collateral		*6,291,083.78*		*9,530,864.95*
2.	Credit risk	5.2.		135,370,887.50	40,364,091.28
	of which:				
	liabilities from repo transactions		*0.00*		*0.00*
3.	Liabilities from trust transactions	5.3.		435,245,981.35	214,824,538.81
4.	Eligible own funds pursuant to Part 2 of Regulation (EU) No 575/2013	6.1.		286,033,594.94	259,825,382.29
	of which tier 2 capital pursuant to Part 2 Title I Chapter 4 of Regulation (EU) No. 575/2013		*60,435,616.44*		*64,832,876.71*
5.	Own funds requirements pursuant to Art. 92 of Regulation (EU) No. 575/2013	6.1.		992,393,514.16	686,130,553.43
	of which own funds requirements pursuant to Art. 92.1.a of Regulation (EU) No. 575/2013 CET 1 capital ratio	*6.1.*	*22.73%*		*28.42%*
	of which own funds requirements pursuant to Art. 92.1.b of Regulation (EU) No 575/2013 tier 1 capital ratio	*6.1.*	*22.73%*		*28.42%*
	of which own funds requirements pursuant to Art. 92.1.c of Regulation (EU) No 575/2013 total capital ratio	*6.1.*	*28.82%*		*37.87%*
6.	Foreign liabilities			1,909,809,665.05	2,158,251,671.74

II. INCOME STATEMENT (pursuant to the AUSTRIAN BANKING ACT)

in EUR		Note			1/1-31/12/2017	1/1-31/12/2016
1.	Interest and similar income				153,394,125.01	171,923,809.45
	of which from fixed-income securities			*9,414,675.59*		*11,236,227.83*
2.	Interest and similar expenses				-120,583,632.51	-135,712,952.69
I.	**NET INTEREST INCOME**	7.1.1.			**32,810,492.50**	**36,210,856.76**
3.	Income from securities and investments	7.1.2.			836,512.95	487,350.00
	a) Income from participations			23,400.00		0.00
	b) Income from investments in affiliated companies			813,112.95		487,350.00
4.	Fee and commission income	7.1.3.			10,103,319.86	1,078,236.70
5.	Fee and commission expenses	7.1.3.			-1,651,578.27	-522,572.86
6.	Income/expenses from financial transactions				9,412.81	-5,470.57
7.	Other operating income	7.1.5.			23,697,276.31	14,020,769.37
II.	**OPERATING INCOME**				**65,805,436.16**	**51,269,169.40**
8.	General administrative expenses	7.1.4.			-45,712,282.20	-38,703,805.75
	a) Personnel expenses	7.1.4.1.		-29,827,116.15		-23,243,073.28
	aa) Salaries		-24,058,118.74			-17,520,581.93
	bb) Expenses for statutory social charges, salary-dependent charges and compulsory contributions		-4,468,631.67			-3,838,382.45
	cc) Other social expenses		-619,562.73			-562,306.55
	dd) Expenses for pension costs		-560,872.86			-709,820.61
	ee) Appropriation / release of pension provisions		-161,705.82			123,473.27
	ff) Expenses for severance pay and contributions to company pension plans		41,775.67			-735,455.01
	b) Other administrative expenses (non-personnel expenses)	7.1.4.2.		-15,885,166.05		-15,460,732.47
9.	Impairment charges to assets reported under asset items 8 and 9				-861,517.07	-273,184.13
10.	Other operating expenses	7.1.6.			-675,587.58	-11,578,631.68
III.	**OPERATING EXPENSES**				**-47,249,386.85**	**-50,555,621.56**
IV.	**OPERATING RESULT**				**18,556,049.31**	**713,547.84**
11.	Balance of income/expenses from the impairment of receivables and contingent liabilities and the sale a valuation of securities held as current assets				-3,662,905.65	2,011,154.19
12.	Income from valuation adjustments of investment securities and from participations and investments in affiliated companies	7.1.7.			3,415,578.98	52,781,780.19
V.	**PROFIT ON ORDINARY ACTIVITIES**				**18,308,722.64**	**55,506,482.22**
13.	Extraordinary income/expenses				702,745.23	-25,000,000.00
	of which appropriations to the fund for general banking risks	7.1.8.			*0.00*	*-25,000,000.00*
14.	**Extraordinary results**				**702,745.23**	**-25,000,000.00**
15.	Taxes on income	7.1.9.			-115,583.56	7,045,540.16
16.	Other taxes not reported under item 16	7.1.9.			-30,084.39	-43,895.20
VI.	**PROFIT FOR THE YEAR**				**18,865,799.92**	**37,508,127.18**
17.	Appropriations to reserves					
	a) Statutory revenue reserve				-943,290.00	-1,875,406.36
18.	Profit carried forward				12,999,911.24	9,367,190.42
VII.	**NET PROFIT**				**30,922,421.16**	**44,999,911.24**

NOTES TO THE SEPARATE FINANCIAL STATEMENTS OF KOMMUNALKREDIT AUSTRIA AG, VIENNA, FOR THE BUSINESS YEAR 2017

1. GENERAL INFORMATION

Kommunalkredit Austria AG (Kommunalkredit), with its registered office in Vienna, Tuerkenstrasse 9, is a specialist bank for infrastructure finance. It acts as a link between project sponsors (developers and operators of infrastructure facilities), on the one hand, and institutional investors, such as insurance companies and pension funds, on the other hand. It is registered with the Commercial Court of Vienna under Companies Register number 439528s.

Kommunalkredit was established on 26 September 2015 through the demerger for new incorporation of the former Kommunalkredit. The entire business operation of the former Kommunalkredit (including all its subsidiaries) was transferred to a newly established company (Kommunalkredit) by way of a proportionate demerger for new incorporation. The part of the former Kommunalkredit remaining after the demerger was merged into KA Finanz AG (KF).

Gesona Beteiligungsverwaltung GmbH (Gesona) owns 99.78% of Kommunalkredit. The remaining 0.22% is held by the Association of Austrian Municipalities. Gesona is a holding company through which Interritus Limited (Interritus) and Trinity investments Designated Activity Company (Trinity) – via Satere Beteiligungsverwaltungs GmbH (Satere) – hold their participations in Kommunalkredit; Interritus and Trinity respectively hold 55% and 45% of Satere, which in turn holds 100% of Gesona.

The consolidated financial statements of Kommunalkredit, based on IFRS, are prepared pursuant to § 59a of the Austrian Banking Act in conjunction with § 245a of the Austrian Company Code. As an issuer of exchange-listed securities, Kommunalkredit publishes a Group Management Report pursuant to § 82 (4) of the Stock Exchange Act as part of this Annual Financial Report.

The consolidated financial statements of Kommunalkredit, the company which prepares the consolidated financial statements for the smallest scope of consolidation, are registered with the Commercial Court of Vienna under Companies Register number 439528s. Kommunalkredit is an affiliated company of Satere, with its registered office in Vienna, which prepares the consolidated financial statements for the largest scope of consolidation. The consolidated financial statements of Satere are deposited with the Companies Register of the Commercial Court of Vienna under Companies Register number 428981f.

2. ACCOUNTING RULES APPLIED

These financial statements were prepared in accordance with the relevant provisions of the Austrian Banking Act (*Bankwesengesetz – BWG*) and the provisions of the Austrian Company Code (*Unternehmensgesetzbuch – UGB*) applicable to financial institutions.

3. ACCOUNTING AND MEASUREMENT RULES

3.1. General remarks

The financial statements were prepared in compliance with generally accepted accounting principles and the general standard requiring the presentation of a true and fair view of the assets, the financial position and the income of the company.

The principle of completeness was complied with in the preparation of the financial statements. The assets and liabilities were measured on an item-by-item basis on the assumption of a going concern. The principle of prudence, considering the specificities of the banking business, was observed insofar as only profits realised on the balance sheet date were recognised and all identifiable risks and impending losses were taken into account.

Income and expenses are accrued/deferred pro-rata-temporis and recognised in the profit or loss of the period to which they are economically attributable. Interest is recognised as it accrues in net interest income, considering all contractual arrangements made in connection with the financial assets or liabilities. Dividend income is booked on the date on which the legal claim to payment arises.

Fees and commissions for services provided over a certain period of time are recognised over the period of service provision. Fees related to the completion of service provision are booked as income at the time of completion. Contingent commissions are recognised when the required performance criteria are met.

All purchases and sales of financial instruments are recognised on the trade date.

3.2. Currency translation

The reporting and functional currency is the euro. Assets and liabilities denominated in foreign currencies are translated at the rates notified by the European Central Bank (ECB) on the balance sheet date pursuant to § 58 (1) of the Austrian Banking Act. Forward transactions not yet settled are translated at the forward rate on the balance sheet date.

3.3. Receivables

Receivables purchased from third parties are recognised at amortised cost. All other loans and advances to banks and loans and advances to customers are recognised at their nominal value. For receivables with an intention of syndication, the book value is reduced by the expected syndication expense.

Specific loan loss provisions are set up for identifiable borrower risks.

In addition, a portfolio loan loss provision is calculated. For this purpose, the financial assets are classified in comparable groups according to their risk profiles. On the basis of empirical values and the monitoring processes in place, the loan loss provisioning requirement is calculated for these groups, considering the loss identification period (LIP), the probability of default (PD) and loss given default (LGD).

Moreover, for reasons of prudence and in view of the special risks of the banking business, a provision pursuant to § 57 (1) of the Austrian Banking Act has been set up, which is recognised under loans and advances to customers.

3.4. Securities

Securities to be held for the company's business operations on a permanent basis are classified as non-current assets. Securities acquired with the intention to trade are assigned to the trading book. Securities that are neither classified as non-current assets nor assigned to the trading portfolio are classified as current assets. As at 31 December 2017, all securities were classified as non-current assets. Securities are recognised at cost, based on the mitigated lower-of-cost-or-market principle for non-current assets and the strict lower-of-cost-or-market principle for current assets. Securities of the trading portfolio are recognised at their market value on the balance sheet date.

For securities classified as non-current assets, the company has elected to write off pro-rata temporis the acquisition cost exceeding the amount repayable. The possibility of writing up the amount exceeding the amount repayable on a pro-rata temporis basis is used as well.

The temporary differences pursuant to § 56 (2) and § 56 (3) of the Austrian Banking Act are as follows:

Differences pursuant to § 56 (2) and § 56 (3) Austrian Banking Act in EUR	31/12/2017	31/12/2016
Difference pursuant to § 56 (2) Austrian Banking Act (Difference between the higher acquisition cost and The amount repayable for the securities)	3,179,429.40	1,857,477.04
Difference pursuant to § 56 (3) Austrian Banking Act (Difference between the lower acquisition cost and the amount repayable for the securities)	5,617.50	140,700.00

Moreover, securities classified as non-current assets include the following hidden reserves and/or hidden burdens (not considering the related interest rate swaps):

Calculation of hidden reserves in EUR	31/12/2017	31/12/2016
Book value	484,784,760.50	487,354,790.91
Fair value	537,179,755.57	564,901,675.38
Hidden reserves	**52,394,995.07**	**77,546,884.47**

Calculation of hidden burdens in EUR	31/12/2017	31/12/2016
Book value	50,615,109.36	0.00
Fair value	50,344,349.99	0.00
Hidden burdens	**-270,759.37**	**0.00**

Hidden reserves mainly result from fixed-income securities, the high fair value being due to the low level of interest. Hidden reserves and hidden burdens are booked against the fair values of interest rate derivatives concluded for hedging purposes. The hidden burdens reported primarily result from changes in credit spreads since the securities were purchased. Securities with hidden burdens are regularly analysed and measured with a view to the credit risk. On the basis of these analyses, an extraordinary write-down pursuant to § 204 (1.2) of the Austrian Company Code was not required, as the impairment is assumed to non-permanent.

Fair value measurement

In general, the methods used to measure the fair value can be classified in three categories:

Level 1: Prices are quoted in an active market for identical financial instruments. In this category, asset bid quotes from Bloomberg and Reuters are used.

Level 2: The inputs for fair value measurement are observable in the market. This category includes the following pricing methods:
- Pricing on the basis of similar instruments
- Pricing on the basis of market-derived spreads (benchmark spreads)

Level 3: The inputs cannot be observed in the market. This category includes, above all, prices based mainly on expert estimates.

Broken down by the above categories, the temporary differences between the fair values and the book values of securities are as follows:

31/12/2017 in EUR	Level 1	Level 2	Level 3
Fair value	204,866,857.48	379,726,237.05	2,931,011.03
Book value	202,035,676.01	330,564,194.18	2,800,000.00
Temporary difference	**2,831,181.47**	**49,162,042.87**	**131,011.03**

31/12/2016 in EUR	Level 1	Level 2	Level 3
Fair value	139,499,322.52	425,402,352.86	0.00
Book value	130,574,861.01	356,779,930.11	0.00
Temporary difference	**8,924,461.51**	**68,622,422.75**	**0.00**

No securities were reclassified in the current reporting period.

3.5. Merger of Kommunalkredit Beteiligungs- und Immobilien GmbH and transfer of real estate

In the business year 2017, real estate and participations, previously held by Kommunalkredit Beteiligungs- und Immobilien GmbH (KBI), were separated under company law.

The merger of KBI into Kommunalkredit as of 30 June 2017, as the merger date under trade and tax law, took effect as of 9 November 2017, the date of the merger agreement. The merger balance sheet as of 30 June 2017 is as follows:

	Assets	Kommunalkredit Austria AG 30/06/2017	Closing balance sheet KBI 30/06/2017	Consolidation 30/06/2017	Merger balance sheet 30/06/2017
1.	Cash and balances with central banks	217,804,875.00	0.00	124,126.90	217,929,001.90
2.	Public-sector debt instruments eligible as collateral for central bank funding	105,189,259.90	0.00	0.00	105,189,259.90
3.	Loans and advances to banks	117,201.410.49	1,472,802.62	-1,474,859.92	117,199,353.19
4.	Loans and advances to customers	2,341,282,914.89	0.00	-19,573,368.76	2,321,709,546.13
5.	Bonds and other fixed-income securities	129,955,722.53	0.00	0.00	129,955,722.53
6.	Participations	2,625,070.00	344,025.00	0.00	2,969,095.00
7.	Investments in affiliated companies	6,339,848.12	150,000.00	-5,943,348.12	546,500.00
8.	Intangible non-current assets	245,167.38	0.00	0.00	245,167.38
9.	Property, plant and equipment	1,915,417.07	24,357,728.72	0.00	26,273,145.79
	including land and buildings used by the bank within the framework of its own activities	*0.00*	*23,294,657.16*	*0.00*	*23,294,657.16*
10.	Other assets	29,298,771.66	82,669.63	-124,126.90	29,257,314.39
11.	Accrual and deferral items	6,669,113.83	10,616.52	0.00	6,679,730.35
12.	Deferred tax assets	7,665,952.73	133,928.58	0.00	7,799,881.31
	Total assets	**2,966,193,523.60**	**26,551,771.07**	**-26,991,576.80**	**2,965,753,717.87**

	Liabilities	30/06/2017	30/06/2017	30/06/2017	30/06/2017
1.	Amounts owed to banks	712,539,568.76	19,573,368.75	-19,573,368.75	712,539,568.76
2.	Amounts owed to customers	799,937,302.19	0.00	-1,444,832.12	798,492,470.07
3.	Securitised liabilities	1,085,291,214.52	0.00	0.00	1,085,291,214.52
4.	Other liabilities	35,476,226.18	150,638.30	-38,816.29	35,588,048.19
5.	Deferral and accrual items	8,485,517.16	0.00	0.00	8,485,517.16
6.	Provisions	21,812,314.35	190,459.17	0.00	22,002,773.52
6a.	Fund for general banking risks (§ 57 (3) Austrian Banking Act)	40,000,000.00	0.00	0.00	40,000,000.00
7.	Supplementary capital	66,041.966.75	0.00	0.00	66,041,966.75
8.	Subscribed capital	159,491,290.16	1,816,820.85	-1,816,820.85	159,491,290.16
9.	Capital reserves	0.00	3,444,935.03	-3,444,935.03	0.00
	a) tied	*0.00*	*0.00*	*0.00*	*0.00*
	b) free	*0.00*	*3,444,935.03*	*-3,444,935.03*	*0.00*
10.	Revenue reserves	16,298,090.09	978,195.41	-978,195.41	16,298,090.09
	a) statutory reserve	*3,298,178.85*	*0.00*	*0.00*	*3,298,178.85*
	b) other reserves	*12,999,911.24*	*978,195.41*	*-978,195.41*	*12,999,911.24*
11	Statutory reserve pursuant to § 57 (5) Austrian Banking Act	10,000,000.00	0.00	0.00	10,000,000.00
12.	Result for the period	10,820,033.44	397,353.56	305,391.67	11,522,778.65
	Total liabilities	**2,966,193,523.60**	**26,551,771.07**	**-26,991,576.80**	**2,965,753,717.87**

The merger gain amounted to EUR 702,745.23, resulting from the difference between the equity of the transferring company (KBI) of EUR 6,646,093.34 and the carrying amount of the participation of EUR 5,943,348.12 reported by the receiving company; the amount is recognised in the extraordinary result.

By way of the transfer agreement of 25 October 2017, the property was transferred to the newly established Kommunalkredit TLI Immobilien GmbH & Co KG (TLI). The transfer was made pursuant to § 202 (1) of the Austrian Company Code at a fair value of EUR 31,629,272.00. The resulting transfer gain of EUR 8,622,163.05 is shown under the other operating result.

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3.6. Participations and investments in affiliated companies

Participations and investments in affiliated companies are measured at cost, unless persistent losses or a reduction in equity require their values to be written down to the pro-rata equity held or the value of the income generated; the analysis is performed annually on the basis of projections.

3.7. Intangible assets

Intangible assets exclusively comprise purchased software. Depreciation is based on an assumed useful life of three years.

3.8. Property, plant and equipment

Property, plant and equipment comprise buildings on third-party land, office furniture and equipment, and works of art. Property, plant and equipment are measured at acquisition or production cost after deduction of linear depreciation in prior years and in the reporting year. The period of depreciation is 3 years for technical equipment and 5 and/or 10 years for other mobile equipment. Investments in third-party buildings are depreciated over 15 and/or 20 years. Works of art are not subject to straight-line depreciation.

1.

2. Minor-value assets up to single-item acquisition costs of EUR 400.00 are reported in the Schedule of Non-current Asset Transactions as additions in the year of acquisition and depreciated fully in the year of purchase. They are derecognised after three years.

3.9. Deferred tax assets

The 2014 Accounting Reform Act abolished the right to elect for capitalisation of deferred tax assets from temporary differences between their carrying amount and their tax base and introduced obligatory capitalisation. The difference resulting from this new rule as at 1 January 2016 and will be distributed over five years. Kommunalkredit did not elect to capitalise tax loss carryforwards (tax loss carryforward of Kommunalkredit as at 31 December 2017: EUR 128,642,595.18 (31/12/2016: EUR 144,648,858.34)).

Pursuant to § 235 (2) of the Austrian Company Code, the capitalised amount is subject to a dividend payout block.

3.10. Liabilities

Liabilities are recognised at the amount repayable. Differences between the issuing amount and the repayable amount (discount/premium) are recognised as accrual and deferral items in the net interest result, distributed on a linear basis as an interest component over the term of the liability.

3.11. Securitised liabilities

Securitised liabilities are recognised at the amount repayable. Costs incurred through an issuance, which are directly related to funding, are booked as fee and commission expenses. The remaining difference between the proceeds from the issuance and the amount repayable (premium/discount) is booked as accrued/deferred income/expenses and recognised in the net interest result as an interest component distributed on a linear basis over the term of the liability.

3. Zero bonds are recognised according to the equity method.

Own bonds which were not placed externally but issued as collateral for the liability arising from the demerger, as outlined in Note 6.5, are recognised on a net basis (§ 51 (5) Austrian Banking Act).

3.12. Provisions

Provisions for pensions, severance pay and jubilee bonus obligations are calculated annually by an independent actuary according to the projected-unit-credit method pursuant to § 211 (1) of the Austrian Company Code in accordance with IAS 19 and recognised in personnel expenses. The “AVÖ 2008-P calculation bases for pension insurance – Pagler & Pagler”, in their version for salaried employees, are used as a calculation basis. The actuarial discount rate was determined on the basis of the yields of prime fixed-income corporate bonds, with due consideration given to the terms of the obligations to be met.

The most important parameters underlying the calculation are:

- an actuarial discount rate of 2.00% (2016: 2.25%) for pension obligations, 1.50% (2016: 1.50%) for obligations from severance pay, and 0.50% (2016: 0.50%) for obligations from jubilee bonuses;
- an incremental rate of active salary and pension payments of 2%;
- a career trend of 1.5%;
- assumed pensionable ages of 60 for women and 65 for men, taking into account the transitional provisions of the 2003 Budget Framework Act and the provisions on age limits for women of the Act on Occupational Old-Age Provision, and
- a fluctuation discount calculated on the basis of statistically recorded leaves.

All pension obligations to active employees have been transferred to a pension fund. The provisions reported therefore only contain entitlements from defined-benefit pension obligations for eight employees not covered by the pension fund, resulting from direct commitments within the framework of the collective bargaining agreement (1961 pension reform, as amended on 1 January 1997) made prior to the transfer to the pension fund, or from individual contracts. The pension plan is a defined-benefit plan under which benefits for active staff, relative to the risk of death and invalidity, depend on the salary earned. Benefits for employees reaching retirement age are already fixed and therefore only subject to adjustment in line with the annual increase agreed upon through collective bargaining. As the defined-benefit components are fully funded, supplementary allocations will only be required in the event of underperformance or “premature” payment of benefits. The full actuarial obligation for pensions amounts to EUR 1,811,006.93 (31/12/2016: EUR 1,620.290.46), of which entitlements in the amount of EUR 450,540.11 (31/12/2016: EUR 421,529.46) have been outsourced to the pension fund. The resulting provisioning requirement amounts to EUR 1,360,466.82 (31/12/2016: EUR 1,198,761.00). Provisions for entitlements to severance pay amount to EUR 4,154,224.64 (31/12/2016: EUR 4,482,116.51); provisions for jubilee bonuses amount to EUR 188,486.46 (31/12/2016: EUR 233,275.72).

All actuarial gains and losses immediately carry through profit or loss. The reduced provision for severance pay in 2017 includes actuarial gains of EUR 639,272.88 (2016: actuarial loss of EUR 205,545.54). The change in pension provisions includes actuarial gains of EUR 85,447.10 (2016: EUR 2,695.33) and valuation-related gains on plan assets of EUR 20,580.06 (2016: EUR 2,699.31).

Other provisions were set up in the amount of their expected use in accordance with the principle of prudence, based on all identifiable risks and on liabilities not yet quantifiable. Non-current provisions set up for periods of more than one year are discounted in accordance with the provisions of the 2014 Accounting Reform Act.

3.13. Fund for general banking risks pursuant to § 57 (3) of the Austrian Banking Act

As at 31 December 2017, an amount of EUR 40,000,000.00 (31/12/2016: EUR 40,000,000.00) was appropriated to the fund for general banking risks. Provisions set up pursuant to § 57 (3) of the Austrian Banking Act are recognised in the extraordinary result, as required under the Austrian Banking Act.

3.14. Derivatives

Swap transactions of the banking book are made by Kommunalkredit primarily to hedge interest-rate and/or currency risks, with the hedges accounted for either at single-transaction level (recognition as units of account) or at aggregate level (accounting as macro-hedges). For derivatives that are neither micro-hedges nor macro-hedges, the principle of single measurement applies, with a provision for impending losses set up in the event of a negative fair value on the day of closing and recognised under other provisions.

- Units of account

  For hedge accounting (units of account), the AFRAC (Austrian Financial Reporting and Auditing Committee) Opinion on "Derivatives and Hedging Instruments (Austrian Company Code) (version of December 2015)" contains provisions aimed at avoiding economically unjustified effects on the Income Statement due to the different measurement of hedged underlying transactions and hedging instruments. Underlying transactions are individually recognised assets and liabilities at fixed interest rates as well as pending transactions already concluded at the time of classification. The rules on units of account permit the changes in the value of hedging instruments and the hedged transactions to be recognised mostly as mutually offsetting. Proof of an effective hedging relationship between the underlying transaction and the hedging transaction is required as a prerequisite for the application of these rules. A hedging relationship is considered effective if the results from the hedging instrument and the compensatory results from the hedged underlying transaction – relative to the hedged risk – offset each other within a range of 80% to 125%. Kommunalkredit verifies compliance with these requirements through prospective (matching of the components determining the market value) and retrospective effectiveness tests. In a prospective effectiveness test, all parameters of the underlying transaction and the hedging transaction that determine the extent of the hedged value change are compared in order to verify whether the hedged fair value of the structure (underlying and hedging transactions) is within a range of 80% to 125% maximum. A retrospective effectiveness test verifies whether the hedged fair value of the structure (underlying and hedging transactions) fluctuates within a range of 80% to 125% maximum between two specified dates. Hedging transactions at Kommunalkredit are concluded until maturity of the underlying transaction.

- Macro-hedge

  Interest rate derivatives serving to manage the interest rate risk of the banking book and/or a clearly defined sub-portfolio are accounted for according to the "Circular Letter of the FMA on accounting issues relating to interest rate derivatives and valuation adjustments of derivatives pursuant to § 57 of the Austrian Banking Act" (version of December 2012). As an exception to the principle of individual measurement, compensatory interest-rate-induced earning effects or value increases from the hedged underlying transactions are considered in the assessment of provisioning requirements. If negative swap market values are not fully offset by the compensatory interest-rate-induced earning effects of the underlying transactions, a provision for impending losses is set up for the remaining negative value.

As a basis for risk management and limitation decisions concerning the interest rate risk in the banking book, the fixed-interest gap and its sensitivity to interest rate changes affecting the market value of the banking book position are identified. The risk of fixed-interest gaps is highlighted through gap analyses and sensitivity analyses with annual maturity bands.

Based on the information thus obtained, the risk of interest rate changes is assessed, managed and limited for assets and liabilities relative to the risk appetite and the risk-carrying capacity of the bank, and/or a management instrument is designated.

When a new interest rate derivative contract is concluded, the quantitative suitability of the derivative as an instrument to hedge and limit the risk of interest rate changes for assets and liabilities is verified through a prospective test of the hedging effect using scenario analyses. The net-present-value risk of the position as a whole as well as broken down by currency is quantified for a parallel shift and for two turn-around scenarios (steeper – flatter).

Owing to its exceptional character, application of this measurement method is conditional on compliance with formal and substantive conditions, such as:

- a need for hedging in view of fixed-interest gaps;
- the existence of a hedging strategy and proof of compliance with this strategy;
- the qualitative suitability of the derivative as a hedging instrument.

The above prerequisites are met and documented by Kommunalkredit.

If fixed-interest gaps are closed through derivatives at macro-level, prospective scenario analyses (net-present-value changes in the event of changes in interest level) are performed to determine the hedging effect and the effectiveness of the derivative and, thus, its suitability for allocation to the macro-position. On account of the net-present-value approach, the hedging period extends over the entire terms of the underlying transaction.

The interest claims related to the swap contracts are accrued at matching maturities and recognised on a gross basis in the Income Statement. Payments made to compensate for contracts not in accordance with prevailing market terms are also accrued at matching maturities.

Derivatives are measured by means of an internal model based on the discounted cash flow method, considering all current yield and basis spread curves. Embedded options are measured by means of commonly used option pricing models. For the measurement of interest-sensitive products with variable indicators, yield curves with different spread premiums are used, depending on the indicator (e.g. 3-month Libor, 12-month Libor). These refer to the indicator concerned and are used to derive forward rates for cash flow determination. In the case of derivatives in several currencies (e.g. cross-currency swaps), a cross-currency basis is used according to prevailing standards, in addition to the adaptation of forwards by basis swap spreads. OIS curves (overnight index swaps) are used for discounting the cash flows of OTC (over-the-counter) derivatives. To determine the fair value of derivatives, counterparty and own risks (credit value adjustment (CVA) and debt value adjustment (DVA)) are also taken into consideration. To this end, the net present value is adjusted by the BCVA (bilateral CVA adjustment). Kommunalkredit determines the BCVA for all derivatives without bilateral daily cash collateral margin calls at counterparty level. A provision for impending losses is set up for negative BCVAs, whereas positive BCVAs are not taken into consideration. For collateralised derivatives with daily margin calls the BCVA is considered to be immaterial. The BCVA is calculated by the potential exposure method.

Swap transactions of the trading book, if any, are measured at their fair values, determined according to the principles outlined above, and recognised under other receivables and other liabilities. At present, Kommunalkredit has no swap transactions in the trading book.

3.15. Residual maturities

Residual maturity is defined as the period of time between the balance sheet date and the contractual maturity of the receivable or liability; in the case of partial amounts, residual maturity is shown for each partial amount. Collaterals for market values from derivatives are shown under "repayable on demand" (daily payment dates); interest accruals/deferrals are shown under "up to 3 months".

4. NOTES TO THE BALANCE SHEET

4.1. Public-sector debt instruments eligible as collateral for central bank funding

Securities of public bodies eligible as collateral for funding from the ECB (European Central Bank) are shown under this item; their book value as at 31 December 2017 amounted to EUR 196,613,929.01 (31/12/2016: EUR 108,082,753.04). As in the previous year, all securities shown under this item were classified as non-current assets. The increase compared to the previous year results from the build-up of a portfolio of high-quality liquid assets (HQLA) as a liquidity reserve. Of the public-sector debt instruments, two instruments with a nominal value of EUR 105,000,000.00 will fall due in 2018 (2017: zero).

4.2. Loans and advances to banks

Loans and advances to banks include the following:

Loans and advances to banks in EUR	31/12/2017	31/12/2016
Collateral for negative market values from derivative transactions	87,362,165.16	91,081,642.54
Collateral for loan disbursement obligations	38,353,033.51	0.00
Cash balances with banks	9,165,070.29	8,967,268.75
Other	4,572,311.89	0.00
Total	**139,452,580.85**	**100,048,911.29**

4. As in the previous year, loans and advances to banks do not include any bills receivable. As at 31 December 2017, no subordinated claims were held against banks.
5.

Broken down by maturity (residual maturity), loans and advances to banks are as follows:

Loans and advances to banks in EUR	31/12/2017	31/12/2016
Loans and advances repayable on demand	101,097,839.01	100,048,911.29
Other loans and advances		
a) up to 3 months	11,737.92	0.00
b) more than 3 months up to 1 year	0.00	0.00
c) more than 1 year up to 5 years	38,343,003.92	0.00
d) more than 5 years	0.00	0.00
	38,354,741.84	0.00
Total	**139,452,580.85**	**100,048,911.29**

4.3. Loans and advances to customers

Loans and advances to customers comprise the following:

Loans and advances to customers in EUR	31/12/2017	31/12/2016
Loans	2,088,765,307.88	2,222,851,356.27
Non-listed securities	257,760,921.11	291,041,235.30
Collateral for negative market values from derivative transactions	97,078,987.32	43,050,000.00
Provision pursuant to § 57 (1) Austrian Banking Act	-3,760,000.00	0.00
Portfolio loan loss provisions	-448,353.00	-147,980.00
Total	**2,439,396,863.31**	**2,556,794,611.57**
of which loans and advances to affiliated companies	*0.00*	*20,075,388.89*
of which loans and advances to companies in which an equity investment is held	*37,246,353.95*	*42,191,367.50*

As in the previous year, non-listed securities included in this item in the amount of EUR 257,760,921.11 (31/12/2016: EUR 291,041,235.30) are classified in their entirety as non-current assets.

Broken down by maturity (residual maturity), loans and advances to customers are as follows:

Loans and advances to customers in EUR	31/12/2017	31/12/2016
Loans and advances repayable on demand	98,228,767.30	42,182,541.02
Other loans and advances		
a) up to 3 months	103,129,891.30	56,316,710.60
b) more than 3 months up to 1 year	157,078,365.70	255,336,037.33
c) more than 1 year up to 5 yeas	1,022,559,358.76	871,012,780.28
d) more than 5 years	1,062,608,833.25	1,332,094,522.34
	2,345,376,449.01	2,514,760,050.55
Provision pursuant to § 57 (1) Austrian Banking Act and portfolio loan loss provision	-4,208,353.00	-147,980.00
Total	**2,439,396,863.31**	**2,556,794,611.57**

4.4. Bonds and other fixed-income securities

Bonds in EUR	31/12/2017	31/12/2016
Securities of public issuers	81,746,822.44	80,752,135.67
Securities of other issuers	7,038,073.14	15,505,236.74
of which own issues	*0.00*	*0.0*
Total	**88,784,895.58**	**96,257,372.41**

All instruments reported under bonds and other fixed-income securities are exchange-listed; none of them will fall due in 2018 (2017: EUR 15,505.236.74).

Own bonds which were not placed externally but issued as collateral for the liability arising from the demerger, as outlined in Note 6.5, are recognised on a net basis (§ 51 (5) Austrian Banking Act).

As in the previous year, all securities reported under this item were classified as non-current assets at the balance sheet date. As in the previous year, none of the bonds and other fixed-income securities held in the portfolio are subordinated.

4.5. Participations and investments in affiliated companies

As at 31 December 2017, the book value of participations amounted to EUR 2,014,095.00 (31/12/2016: EUR 2,425,070.00). Investments in affiliates amounted to EUR 32,612,865.00 (31/12/2016: EUR 6,339,848.12). The book value of the participation in KBI of EUR 5,943,348.12 included in the total as at 31 December 2016 was substituted by the assets of KBI as the transferring company within the framework of the merger in 2017. The transfer of real estate to TLI, as described in Note 3.5, resulted in a corresponding book value of the participation as at the effective date of transfer.

The composition of participations and investments in affiliates (all of them non-listed), including their economic position, is shown in Annex 1.

4.6. Intangible non-current assets and property, plant and equipment

The development of property, plant and equipment and intangible non-current assets is shown in the Schedule of Non-current Asset Transactions (Annex 2). The increase in property, plant and equipment to EUR 2,960,788.45 in 2017 (31/12/2016: EUR 1,904,193.39) results from the transfer of furnishings and equipment, previously held and managed centrally by KBI, to Kommunalkredit within the framework of the merger.

4.7. Other assets

Other assets in EUR	31/12/2017	31/12/2016
Interest accruals from derivatives in the banking book	30,401,409.28	38,729,777.42
Receivables from services invoiced to KA Finanz AG	3,678,787.85	10,504,074.48
Receivables from deferred interest	2,244,314.62	2,516,440.91
Claims against the tax authorities	389,148.64	3,187,579.03
Accruals/deferrals between spot rate and forward rate in FX swaps	322,035.80	17,925,824.40
Other	1,614,358.71	1,378,525.40
Total	**38,650,054.90**	**74,242,221.64**
of which recognised as cash items after the closing date	*38,328,019.10*	*56,316,397.24*

4.8. Accrued income and prepaid expenses

Accrued income and prepaid expenses comprise the following items:

Accrued income and prepaid expenses in EUR	31/12/2017	31/12/2016
Accrued fees from derivative transactions	4,536,874.44	2,251,942.61
Capitalised offering discounts of bond issues	1,689,646.55	1,126,822.16
Other	1,044,666.42	1,439,725.16
Total	**7,271,187.41**	**4,818,489.93**

4.9. Deferred tax assets

The 2014 Accounting Reform Act introduced the obligation to capitalise deferred tax assets resulting from temporary differences between the carrying value of an asset and its tax base. As at 31 December 2017, the asset item amounted to EUR 7,432,406.33 (31/12/2016: EUR 7,141,210.75). Temporary differences under tax law and trade law result primarily from the fund for general banking risks pursuant to § 57 (3) Austrian Banking Act, the general risk provision pursuant to § 57 (1) Austrian Banking Act, personnel provisions, and the tax-neutral transfer of real estate to TLI in 2017 (see Note 3.5.).

The temporary difference of EUR 4,429,968.01 as at 1 January 2016, resulting from the new legal provision, is written up over a period of five years. The remaining difference as at 31 December 2017 amounts to EUR 2,657,980.81.

4.10. Amounts owed to banks

Amounts owed to banks include the following:

Amounts owed to banks in EUR	31/12/2017	31/12/2016
TLTRO II programme (Targeted Longer Term Refinancing Operation) of the ECB	313,930,000.00	313,930,000.00
Collateral for positive market values of derivatives	96,216,035.57	216,491,644.72
Collateralised loans of the European Investment Bank	62,209,423.12	64,638,903.73
Money market transactions	43,043,836.14	170,000,316.67
Other loans	18,929,896.57	29,851,840.57
Other	375,506.04	648,823.52
Total	**534,704,697.44**	**795,561,529.21**

Broken down by maturity (residual maturity) amounts owed to banks are as follows:

Amounts owed to banks in EUR	31/12/2017	31/12/2016
Repayable on demand	116,632,310.77	227,140,643.25
Other liabilities		
a) up to 3 months	21,476,228.98	160,995,709.67
b) more than 3 months up to 1 year	5,850,201.00	375,816,620.61
c) more than 1 year up to 5 years	386,398.132.57	21,068,048.43
d) more than 5 years	4,347,824.12	10,540,507.25
	418,072,386.67	568,420,885.96
Total	**534,704,697.44**	**795,561,529.21**

4.11. Amounts owed to customers

Amounts owed to customers in EUR	31/12/2017	31/12/2016
Deposits by corporates, municipalities and quasi-municipal enterprises	532,977,112.45	214,440,399.98
Deposits by retail customers – KOMMUNALKREDIT INVEST	115,653,652.26	0.00
Cash collateral received for positive market values of derivatives	63,715,823.57	0.00
Other long-term liabilities to customers	326,527,967.66	323,761,829.96
Total	**1,038,874,555.94**	**538,202,229.94**

Broken down by maturity (residual maturity), amounts owed to customers are as follows:

Amounts owed to customers in EUR	31/12/2017	31/12/2016
Liabilities repayable on demand	213,537,338.01	6,855,252.88
Other liabilities		
a) up to 3 months	164,154,802.00	93,602,768.40
b) more than 3 months up to 1 year	243,240,964.79	94,490,392.12
c) more than 1 year up to 5 years	111,251,114.71	41,152,739.77
d) more than 5 years	306,690,336.43	302,101,076.77
	825,337,217.93	531,346,977.06
Total	**1,038,874,555.94**	**538,202,229.94**

4.12. Securitised liabilities

Securitised liabilities are broken down as follows:

in EUR	31/12/2017	31/12/2016
Bonds issued	862,466,869.06	1,052,395,150.03
Other securitised liabilities	427,369,871.89	483,129,698.43
Securitised liabilities	**1,289,836,740.95**	**1,535,524,848.46**

The bonds issued are exchange-listed; the securities reported under other securitised liabilities are non-listed.

Bonds issued with book values of EUR 18,000,000.00 (2017: EUR 301,261,546.70) and other securitised liabilities in the amount of EUR 3,703,429.38 (2017: EUR 16,910,160.33) will fall due in 2018. As in the previous year, securitised liabilities do not include any subordinated liabilities.

4.13. Other liabilities

Other liabilities in EUR	31/12/2017	31/12/2016
Accruals/deferrals between spot rate and forward rate of FX swaps	36,654,164.71	13,499,215.48
Interest accruals from derivatives	20,032,273.37	20,282,125.91
Foreign currency valuation of derivatives in the banking book	4,741,193.97	4,358,833.31
Other	4,301,165.71	4,349,694.68
Total	**65,728,797.76**	**42,489,869.38**
of which recognised as cash items after the closing date	*24,333,439.08*	*24,631,820.59*

The valuation of foreign-currency derivatives in the banking book is based on exchange-rate fluctuations between the closing date of currency swaps and the balance sheet date. This valuation is booked against foreign-currency valuations of assets and liabilities as well as positive foreign-currency valuations of derivatives shown under other assets. Kommunalkredit’s open foreign-currency position is continuously monitored and strictly limited. Therefore, there are no material currency risks.

4.14. Deferred income and accrued expenses

Deferred income and accrued expenses in EUR	31/12/2017	31/12/2016
Deferred fees from derivative transactions	9,498,978.39	1,370,679.00
Issuing premiums of bonds issued	1,549,321.72	1,985,125.96
Loan fees deferred over the term	1,365,314.09	1,541,774.29
Total	**12,413,614.20**	**4,897,579.25**

4.15. Provisions

For details on personnel provisions, see Note 3.12 Provisions.

Other provisions mainly include provisions for personnel-related expenses in the amount of EUR 7,991,668.24 (31/12/2016: EUR 5,624,049.43) and provisions for auditing, legal and consulting expenses in the amount of EUR 833,700.15 (31/12/2016: EUR 642,289.38). In connection with derivatives, provisions in the amount of EUR 214,022.20 (31/12/2016: EUR 1,946,484.31) were set up.

4.16. Fund for general banking risks pursuant to § 57 (3) of the Austrian Banking Act

For prudential reasons and to cover special banking risks, Kommunalkredit, in previous years, appropriated provisions to the fund for general banking risks. As at 31 December 2017, the fund for general banking risks amounted to EUR 40,000,000.00, unchanged from the previous year.

4.17. Tier 2 capital pursuant to Part 2, Title 1, Chapter 4 of Regulation (EU) No. 575/2013

As at 31 December 2017, tier 2 capital items comprised eight (31/12/2016: eight) EUR-denominated issues in a total nominal amount of EUR 65,000,000.00 (31/12/2016: EUR 65,000,000.00) with residual maturities of up to 29 years. None of these issues will fall due in 2018.

The tier 2 capital items meet the conditions of Part 2, Title I, Chapter 4 of the Regulation (EU) No. 575/2013:

ISIN	Interest rate as at 31/12/2017 in %	Maturity	Currency	Nominal in EUR	Right to call	Conversion to capital
Subordinated liabilities pursuant to § 23 (8) Austrian Banking Act old version						
Subordinated bond 2006-2021	5.4	30/10/2021	EUR	5,000,000.00	Issuer in case of tax event	no
Subordinated bonded loan 2007-2022	4.67	23/02/2022	EUR	10,000,000.00	no	no
Subordinated bonded loan 2007-2022	4.67	23/02/2022	EUR	10,000,000.00	no	no
Subordinated bonded loan 2007-2037	5.08	09/02/2037	EUR	10,000,000.00	Issuer	no
Subordinated bonded loan 2007-2037	5.08	09/02/2037	EUR	800,000.00	Issuer	no
Subordinated bonded loan 2007-2037	5.08	09/02/2037	EUR	10,200,000.00	Issuer	no
Subordinated bonded loan 2007-2047	5.0175	07/03/2047	EUR	10,000,000.00	Issuer	no
Subordinated bonded loan 2007-2047	5.0175	07/03/2047	EUR	9,000,000.00	Issuer	n

Expenses for all subordinated liabilities in 2017 amounted to EUR 3,223,805.58 (2016: EUR 3,226,578.14).

4.18. Subscribed capital

The share capital as at 31 December 2017, unchanged from the previous year, amounted to EUR 159,491,290.16. 30,938,843 no-par-value shares, i.e. 99.78% of the share capital, are held by Gesona Beteiligungsverwaltung GmbH; 68,216 no-par-value shares, i.e. 0.22% of the share capital, are held by the Association of Austrian Municipalities. Each no-par-value share represents an equal part of the share capital. There are no shares that have been issued but not fully paid in. Each no-par-value share represents a share of EUR 5.14 in the share capital. By a resolution adopted by the Annual General Meeting of 10 March 2017, the Executive Board was authorized to increase the share capital through the issue of up to 15,503,529 new no-par-value registered shares by a maximum amount of EUR 79,745,642.51 (authorized capital), subject to approval by the Supervisory Board, within a period of five years after registration of the amendment to the Articles of Association.

4.19. Revenue reserve

As at 31 December 2017, the statutory revenue reserve amounted to EUR 4,241,468.85 (31/12/2016: EUR 3,298,178.85).

4.20. Statutory reserve pursuant to § 57 (5) of the Austrian Banking Act

As at the balance sheet date, the statutory reserve, unchanged from the previous year, stood at EUR 10,000,000.00, thus meeting the legal requirements.

4.21. Net profit / Profit distribution

The Executive Board will propose to the Shareholders‘ Meeting on 6 March 2018 that from the 2017 net profit of EUR 30,922,421.16 an amount of EUR 11,500,000.00 be distributed and the balance of EUR 19,422,421.16 be carried forward to new account.

5. OFF-BALANCE-SHEET ITEMS

5.1. Contingent liabilities

The off-balance-sheet item of contingent liabilities in the amount of EUR 6,291,083.78 (31/12/2016: EUR 9,530,864.95) exclusively concerns guarantee lines granted, including a guarantee in the amount of EUR 1,350,000.00 (31/12/2016: EUR 1,350,000.00) for companies in which an equity investment is held.

5.2. Credit risks

Credit risks in the amount of EUR 135,370,887.50 (31/12/2016: EUR 40,364,091.28) relate to loan commitments and unused lines from the current lending business in the amount of EUR 133,220,887.50 (31/12/2016: EUR 37,789,091.28) and a payout obligation for an investment in equity instruments in the amount of EUR 2,150,000.00 (31/12/2016: EUR 2,575,000.00). For companies in which an equity investment is held, unused credit lines granted amount to EUR 1,420,439.15 (31/12/2016: EUR 1,580,992.48).

5.3. Trust transactions

Kommunalkredit holds financial instruments with a nominal value of EUR 435,245,981.35 (31/12/2016: EUR 214,824,538.81) in trust in its own name but at third parties' cost and risk.

6. SUPPLEMENTARY DISCLOSURES

6.1. Own funds and own funds requirements

Kommunalkredit is subject to the own funds requirements pursuant to Article 92 CRR (CET 1 ratio 4.5%, core capital ratio 6%, total capital ratio 8%). Taking into account the capital conservation buffer, the anticyclical buffer and the surcharge from the supervisory review and evaluation process (SREP), a common equity tier 1 ratio of 6.05%, a core capital ratio of 7.65% and a total capital ratio of 9.85% % are required. The statutory requirements were met at all times during the reporting year.

Own funds and own funds requirements calculated in accordance with CRR rules, as reported in the separate financial statements of Kommunalkredit pursuant to the Austrian Company Code/Austrian Banking Act, show the following composition and development:

Assessment base in EUR	31/12/2017	31/12/2016
Total risk exposure amount pursuant to Art. 92 CRR	992,393,514.16	686,130,553.43
of which credit risk	*874,843,851.80*	*525,827,545.93*
of which operational risk	*99,943,426.49*	*108,947,442.63*
of which CVA charge	*17,502,059.50*	*51,247,815.00*
of which default fund of a qualifying counterparty	*104,176.38*	*107,749.88*

Own funds in EUR	31/12/2017	31/12/2016
Common equity tier 1 after deductible items	232,963,778.42	225,500,632.76
Additional own funds after deductible items	64,195,616.44	64,832,876.71
Eligible own funds (tier 1 and tier 2)	**297,159,394.86**	**290,333,509.47**
Own funds ratio	29.9%	42.3%
CET 1 ratio	23.5%	32.9%

The eligible own funds reported include the 2017 net profit of EUR 18,865,799.92 (2016: EUR 37,508,127.18), less the proposed dividend of EUR 11,500,000.00 (2016: EUR 32,000,000.00).

6.2. Total of assets and liabilities denominated in foreign currencies

As at 31 December 2017, assets denominated in foreign currencies in the amount of EUR 176,800,614.76 (31/12/2016: EUR 160,939,182.25) were shown on the balance sheet. Liabilities in foreign currencies amounted to EUR 708,965,784.88 (31/12/2016: EUR 1,110,043,793.84). Open currency positions are closed through corresponding swap contracts. Kommunalkredit's open foreign currency position is continuously monitored and strictly limited; therefore, there are no material currency risks.

6.3. Derivative transactions not yet settled at the balance sheet date

To hedge currency and interest rate risks, the following derivative transactions were made in the banking book (fair values including interest accruals), which were not yet settled on the balance sheet date:

31/12/2017 in EUR	Nominal	Positive fair value	Negative fair value
Interest-rate swaps	3,071,726,544	231,392,016	-205,016,724
of which in macro-hedge	*871,759,299*	*10,487,060*	*-130,603,800*
of which in unit of account	*2,199,967,245*	*220,904,955*	*-74,412,924*
Currency swaps	27,424,023	923,069	-2,991,166
of which in unit of account	*27,424,023*	*923,069*	*-2,991,166*
FX forward transactions	740,221,767	301,735	-36,701,481
Total	**3,839,372,334**	**232,616,819**	**-244,709,372**

31/12/2016 in EUR	Nominal	Positive fair value	Negative fair value
Interest-rate swaps	3,300,748,938	318,641,774	-248,296,529
of which in macro-hedge	*916,768,838*	*8,833,778*	*-156,512,596*
of which in unit of account	*2,383,980,100*	*309,807,996*	*-91,783,934*
Currency swaps	25,598,826	855,582	-1,453,082
of which in unit of account	*25,598,826*	*855,582*	*-1,453,082*
FX forward transactions	1,067,469,633	17,659,018	-13,597,887
Total	**4,393,817,398**	**337,156,374**	**-263,347,499**

Interest accruals/deferrals, foreign currency valuations and accrued/deferred fees from derivative transactions in the amount of EUR 35,260,319.52 (31/12/2016: EUR 58,907,544.43) are reported under other assets and accrued income and prepaid expenses on the assets side, and EUR 70,926,610.44 (31/12/2016: EUR 39,510,853.70) under other liabilities and deferred income and accrued expenses on the liabilities side of the balance sheet. Moreover, provisions in the amount of EUR 214,022.20 (31/12/2016: EUR 1,946,484.31) relating to derivatives are recognised under other provisions. As in the previous year, no provision for impending losses from macro-swaps was required as at 31 December 2017.

6.4. Trading book

In line with its business strategy, Kommunalkredit does not engage in any relevant trading activities. As in the previous year, Kommunalkredit therefore had no trading portfolio as at 31 December 2017.

6.5. Other obligations

a. Liability arising from the demerger

Pursuant to § 15 (1) of the Demerger Act, Kommunalkredit is liable jointly and severally with KA Finanz AG (KF) for obligations having arisen prior to the entry of the demerger in the Companies Register on 26 September 2015 and transferred from the former Kommunalkredit to KA Finanz AG. Equally, KA Finanz AG is liable jointly and severally with Kommunalkredit for the liabilities transferred to Kommunalkredit. This does not concern liabilities that have arisen after the effective date of the demerger. The liability arising from the demerger is limited to the net assets of the respective entity as at the effective date of the demerger.

b. Other obligations

Obligations in the amount of EUR 1,553,600.00 arise from rental contracts (with affiliated companies) in 2018. The corresponding obligations for the years 2018 to 2022 are expected to total EUR 8,001,000.00.

Pursuant to § 2 (3) ESAEG, Kommunalkredit is obliged to undertake proportional safeguarding of depositors' accounts within the framework of the deposit guarantee regime of Banken und Bankiers Gesellschaft mbH, Vienna.

6.6. Asset items pledged as collateral

Credit balances with banks with a nominal value of EUR 87,330,000.00 (31/12/2016: EUR 90,990,000.00) and credit balances with customers (central counterparties and/or non-bank financial institutions) with a nominal value of EUR 97,078,987.32 (31/12/2016: EUR 43,050,000.00) were pledged as collateral for negative market values from bilateral and cleared derivative contracts. Amounts owed to banks include collateral received in a nominal value of EUR 96,185,000.00 (31/12/2016: EUR 216,480,772.00). Amounts owed to customers include collateral received in a nominal value of EUR 63,694,933.36 (31/12/2016: EUR 0.00).

For funding raised through participation in the ECB tender, Kommunalkredit pledged securities and loans in a volume of EUR 349,905,202.81 (31/12/2016: EUR 540,248,636.60) as collateral as at 31 December 2017. The collateral taker has the right to realise the collateral only in the event of the debtor's default.

Kommunalkredit has assigned assets in the form of securities in a nominal amount of EUR 65,100,000.00 (31/12/2016: EUR 65,600,000.00) as collateral for global loans and other funding from the European Investment Bank in Luxembourg. The collateral taker has the right to realise the collateral only in the event of the debtor's default.

As collateral for the liability rising from the demerger for KA Finanz AG, which is liable jointly and severally with Kommunalkredit for the obligations which arose prior to the entry of the demerger in the Companies Register on 26 September 2015 and were transferred to Kommunalkredit, Kommunalkredit issued a covered bond with a nominal value of EUR 107,000,000.00 and pledged it to KA Finanz AG. Pursuant to § 51 (5) of the Austrian Banking Act, this financial instrument is recognised on the liabilities side after netting.

For covered Kommunalkredit issues with a nominal value of EUR 858,267,817.49 as at 31 December 2017 (31/12/2016: EUR 1,033,772,232.05) and for the aforementioned covered bond issued as collateral for KA Finanz AG with a nominal value of EUR 107,000,000.00 (31/12/2016: EUR 107,000,000.00), loans with a nominal value of EUR 1,005,668,230.70 (31/12/2016: EUR 1,111,510,008.06) and securities with a nominal value of EUR 251,633,367.02 (31/12/2016: EUR 230,362,736.02) were appropriated to a cover pool which can only be drawn on with the approval of a government commissioner.

Moreover, as at 31 December 2017, an amount of EUR 19,777,713.26 (31/12/2016: EUR 21,759,037.73) was put up as collateral for other funding.

7. NOTES TO THE INCOME STATEMENT

7.1. Presentation of material Income Statement items

7.1.1. Net interest income

Interest and similar income in EUR	2017	2016
Lending business	76,603,656.80	78,505,495.13
Investments in banks	-1,386,373.33	-239,852.84
Fixed-income securities	9,414,675.59	11,236,227.83
Swap income	68,762,165.95	82,421,939.33
Total interest income	**153,394,125.01**	**171,923,809.45**

Interest and similar expenses in EUR	2017	2016
Deposit business	-19,374,332.92	-24,977,609.71
Own issues	-47,570,619.95	-57,781,057.43
Swap expenses	-53,638,679.64	-52,954,285.55
Total interest expenses	**-120,583,632.51**	**-135,712,952.69**

Net interest income	**32,810,492.50**	**36,210,856.76**

In 2017, net interest income amounted to EUR 32,810,492.50 (2016: EUR 36,210,856.76), reflecting income above budget from new infrastructure financing business and a scheduled reduction through the run-off of the existing portfolio, including debt instruments issued for refinancing, taken over upon the demerger in 2015. Net interest income was depressed by the costs of liquidity; in 2017, negative interest in the amount of EUR 1,428,313.34 (2016: EUR 371,766.96) was paid for credit balances with the Austrian National Bank, which is recognised in interest income under investments in banks.

Interest income and interest expenses are recognised according to the accruals concept. Interest expenses and interest income from interest-rate swaps are recognised as gross amounts, broken down by incoming and outgoing payments, and not offset against interest income and expenses from the underlying transactions.

7.1.2. Income from securities and participations

Income from participations amounted to EUR 23,400.00 (2016: EUR 0.00), including the dividend paid out by Kommunalnet E-Government Solutions GmbH.

Income from investments in affiliated companies amounted to EUR 813,112.95 (2016: EUR 487,350.00), including the dividend of EUR 494,280.00 (2016: EUR 487,350.00) paid out by Kommunalkredit Public Consulting (KPC) and the dividend of EUR 318,832.95 (2016: EUR 0.00) paid out by KBI.

7.1.3. Net fee and commission income

Fee and commission income in EUR	2017	2016
Lending business	9,237,306.36	889,456.62
Other service business	866,013.50	188,780.08
Total fee and commission income	**10,103,319.86**	**1,078,236.70**

Fee and commission expenses in EUR	2017	2016
Lending business	-196,029.61	-33,054.08
Securities business	-1,262,409.40	-357,488.34
Money and X trading	-193,139.26	-132,030.44
Total fee and commission expenses	**-1,651,578.27**	**-522,572.86**

Net fee and commission income	**8,451,741.59**	**555,663.84**

In 2017, fee and commission income amounted to EUR 10,103,319.86 (2016: EUR 1,078,236.70), including mainly arrangement fees in the amount of EUR 8,702,734.00 (2016: EUR 615,150.90) from new infrastructure financing business generated in 2017 as well as income from other services for customers in the amount of EUR 866,013.50 (2016: EUR 188,780.08).

Fee and commission expenses in the amount of EUR 1,651,578.27 (2016: EUR 522,572.86) included transaction and payment transfer fees, especially transaction costs in connection with the issuance of the social covered bond in a nominal value of EUR 300,000,000.00.

7.1.4. General administrative expenses

General administrative expenses in EUR	2017	2016
Personnel expenses	-29,827,116.15	-23,243,073.28
Other administrative expenses	-15,885,166.05	-15,460,732.47
General administrative expenses	**-45,712,282.20**	**-38,703,805.75**

7.1.4.1. Personnel expenses

Personnel expenses in EUR	2017	2016
Salaries	-21,358,118.74	-17,520,581.93
Expenses for statutory social charges, salary-dependent charges and compulsory contributions	-4,468,631.67	-3,838,382.45
Expenses for efficiency programmes	-2,700,000.00	0.00
Other social expenses	-619,562.73	-562,306.55
Expenses for pension costs	-560,872.86	-709,820.61
Appropriation to/release of pension provision	-161,705.82	123,473.27
Expenses for severance pay and contributions to company pension funds	41,775.67	-735,455.01
Total personnel expenses	**-29,827,116.15**	**-23,243,073.28**

The increase in personnel expenses primarily results from the recruitment of personnel for the front-office teams and the establishment of the new branch office in Frankfurt am Main, which was opened at the beginning of 2017. At the same time, the bank implemented an efficiency programme to improve operational processes, which will lead to a reduction of the cost base in 2018. The related expenses, such as commitments to voluntary severance pay, are shown in the above table under “Efficiency programme expenses”, the major part of which was accounted for in 2017.

Personnel expenses include expenses for contributions to company pension plans in the amount of EUR 229,667.56 (2016: EUR 191,777.98), expenses for severance pay of EUR 56,448.64 (2016: EUR 0.0) and expenses in connection with provisioned personnel obligations of EUR 107,862.31 (2016: EUR 734,644.86).

7.1.4.2. Other administrative expenses

Other administrative expenses were as follows:

Other administrative expenses in EUR	2017	2016
Third-party services	-2,219,445.67	-2,689,193.84
Consultancy and audit services	-2,381,517.08	-2,051,929.22
Data processing	-1,902,675.31	-1,856,073.91
News services	-1,621,044.36	-1,547,386.59
Occupancy costs	-1,637,613.50	-2,206,789.54
Advertising and entertainment	-816,260.67	-847,306.47
Bank Resolution Fund	-949,493.71	-2,508,504.00
Other non-personnel expenses	-1,366,997.96	-1,241,702.16
Sub-total of other administrative expenses	**-12,895,048.26**	**-14,948,885.73**
Strategic initiatives	-2,990,117.79	-511,846.74
Total of other administrative expenses	**-15,885,166.05**	**-15,460,732.47**

Other administrative expenses increased by EUR 424,433.58 year on year to EUR 15,885,166.05 (2016: EUR 15,460,732.47). The total includes costs of new strategic initiatives in the amount of EUR 2,990,117.79, such as the establishment of the online platform KOMMUNALKREDIT INVEST, which is the first offer for private individuals to invest in Kommunalkredit and significantly broadens the bank's funding options. Apart from these one-off investments, current expenses were reduced by EUR 2,053,837.41 through targeted cost management and lower contributions to the Bank Resolution Fund.

Pursuant to § 238 (1.18) of the Austrian Company Code, audit expenses for the business year under review are not reported here, as Kommunalkredit is included in the consolidated financial statements and audit expenses are reported therein.

7.1.5. Other operating income

Other operating income in EUR	2017	2016
Income from services charged to KA Finanz AG and KPC	14,128,359.46	13,217,784.25
Other	9,568,916.85	802,985.12
Total of other operating income	**23,697,276.31**	**14,020,769.37**

Kommunalkredit acts as a service provider for other entities, including KA Finanz AG (for the management of banking operations) and KPC. The services to be provided are defined in service level agreements. An amount of EUR 14,128,359.46 (2016: EUR 13,217,784.25) was charged for services rendered in 2017. The amount also includes the profit of EUR 8,622,163.05 from the transfer of the property to the newly established TLI described in Note 3.5.

7.1.6. Other operating expenses

Other operating expenses of in the amount of EUR 675,587.58 (2016: EUR 11,578,631.68) exclusively comprise the stability tax payable by Austrian banks. In 2016, Kommunalkredit elected to make a non-recurrent special payment of EUR 7,718,418.12, which resulted in a notable reduction of this tax burden from 2017 onwards.

7.1.7. Net risk provisioning, valuation and sales result

The net risk provisioning, valuation and sales result (items 11 to 12 of the Income Statement) comprises the following items:

Net risk provisioning, valuation and sales result in EUR	2017	2016
Proceeds from the buyback of own issues	6,240,462.90	51,787,325.23
Provision pursuant to § 57 (1) Austrian Banking Act	-3,760,000.00	0.00
Provision for asset sales	-2,596,660.31	-3,000,858.00
Gains realised through the sale of derivatives in connection with the exercise of the right to call own issues	0.00	2,473,230.73
Change in portfolio loan loss provision	-300,373.00	64,569.00
Provision for the closure of derivatives	0.00	-1,475,000.00
Closure of strategic swaps	0.00	4,421,436.20
Other	169,243.74	522,231.22
Total	**-247,326.67**	**54,792,934.38**

The 2017 net risk provisioning, valuation and sales results amounted to EUR -247,326.67 (2016: EUR 54,792,934.38). The year-on-year reduction is primarily due to the fact that positive one-off effects from the buyback of own issues did not occur to the same extent as in the previous year (2017: EUR 6,240,462.90; 2016: EUR 51,787,325.23). Moreover, a general risk provision pursuant to § 57 (1) of the Austrian Banking Act was set up in 2017 in the amount of EUR -3,760,000.00 (2016: EUR 0,0).

The 2017 net risk provisioning result amounted to EUR -300,373.00 (2016: EUR 64,569.00), resulting exclusively from portfolio loan loss provisions. As in the previous year, there were no credit defaults in 2017; Kommunalkredit's non-performing-loan (NPL) ratio (definition of default according to Basel III) remained at 0.0%.

7.1.8. Extraordinary result

Extraordinary income in the amount of EUR 702,745.23 (2016: extraordinary expense of EUR 25,000,000.00 appropriated to the fund for general banking risks pursuant to § 57 (3) of the Austrian Banking Act) includes gains from the merger with KBI.

7.1.9. Taxes on income

Effective as of 2016, a tax group pursuant to § 9 of the Corporate Income Tax Act was formed, with Satere as the group parent and Gesona, Kommunalkredit, KBI, KPC and TrendMind IT Dienstleistung GmbH (TrendMind) as group members. On the basis of a group and tax contribution agreement, the stand-alone method was chosen for the calculation of the tax contributions. According to this method, the amount of the tax contributions of the group members depends on the amount of corporate income tax the group member would have had to pay if its tax result had not been counted toward the group parent. Tax loss carryforwards of a group member from periods prior to the formation of the group (pre-group losses) are credited up to the amount of the profit of the group member and diminish the tax contribution of the group member. If a group member's negative income is counted toward the group parent, this tax loss is kept on record for the group member (internal loss carryforward) and offset against the positive income of the group member in subsequent years up to 100%. Upon termination of the tax group or elimination of a group member, a final compensation has to be paid for tax losses not yet offset, multiplied by the corporate tax rate applicable at the time of termination of the agreement.

Owing to the formation of the tax group with Satere as the group parent, Kommunalkredit's tax loss carryforwards from periods before the establishment of the tax group (pre-group losses) are credited up to the amount of Kommunalkredit's own profit. Thus, the corporate tax expense exclusively results from the branch in Germany and amounts to EUR 11,559.00 (2016: EUR 0.00).

The income tax expense, which exclusively concerns the company's ordinary business operations, comprises the following items:

Corporate income tax in EUR	2017	2016
Corporate income tax expense Kommunalkredit	-11,559.00	0.00
Corporate income tax from previous years	-261,291.56	-95,670.59
Deferred tax assets	157,267.00	7,141,210.75
	-115,583.56	**7,045,540.16**

Deferred tax assets result from the obligatory capitalisation of temporary differences between the carrying amounts of assets and their tax base, introduced through the 2014 Accounting Reform Act.

7.1.10. Result for the year and return on assets

Kommunalkredit closed the year under review with a net profit of EUR 18,865,799.92 (31/12/2016: EUR 37,508,127.18). The return on assets, calculated as the after-tax profit for the year divided by total assets as at balance-sheet date, stood at 0.58% (31/12/201&: 1.15%).

7.2. Presentation of revenues by geographic market (§ 237 Austrian Company Code)

Interest and similar income in EUR	2017	2016
Austria	104,551,042.75	136,708,552.61
Western Europe	36,171,299.93	21,463,611.02
Central and Eastern Europe	12,182,328.90	13,751,645.83
Rest of the world	489,453.42	0.00
	153,394,125.01	**171,923,809.45**

Fee and commission income in EUR	2017	2016
Austria	225,880.11	252,846.79
Western Europe	4,743,807.55	825,389.91
Central and Eastern Europe	4,379,010.15	0.00
Rest of the world	754,622.05	0.00
	10,103,319.86	**1,078,236.70**

Other operating income in EUR	2017	2016
Austria	23,449,124.21	14,020,625.71
Western Europe	248,152.10	143.66
Central and Eastern Europe	0.00	0.00
Rest of the world	0.00	0.00
	23,697,276.31	**14,020,769.37**

8. DISCLOSURE PURSUANT TO PART 8 CRR

In accordance with the requirements of Part 8 CRR, material qualitative and quantitative information relating to the bank is published in a separate Disclosure Report, which can be accessed on the Kommunalkredit website (www.kommunalkredit.at) under "Investor Relations / Financial Information & Reports".

9. DISCLOSURES REGARDING THE BOARDS OF THE BANK AND ITS EMPLOYEES

9.1. Average number of employees during the business year

As at 31 December 2017, Kommunalkredit had 197 employees (31/12/2016: 195 employees).

The average number of employees during the year under review was 199 (2016: 178), including four (2016: three) Executive Board members and excluding employees on leave; part-time employees are weighted according to the extent of employment.

9.2. Remuneration, advances and loans to Executive Board and Supervisory Board members, guarantees provided for Board members

Total Executive Board and Supervisory Board remuneration in EUR	2017	2016
Active Executive Board members	1,983.341.72	1,299,222.97
Active Supervisory Board members	90,265.00	140,128.00
	2,073,606.72	**1,439,350.97**

As at 31 December 2017, no loans to members of the Executive Board or members of the Supervisory Board were outstanding. No guarantees were provided by Kommunalkredit for Board members.

As at 31 December 2017, the outstanding volume of loans to employees of the company amounted to EUR 409,945.13 (31/12/2016: EUR 372,053.52).

9.3. Expenses for severance pay and pensions

Expenses for severance pay and pensions include pension payments, changes in provisions for severance pay and pensions, statutory contributions to a staff pension plan and payments into a pension fund:

Expenses for severance pay and pensions in EUR	2017	2016
Executive Board, senior employees	355,525.26	680,565.82
Other employees	325,277.75	641,236.52
	680,803.01	**1,321,802.34**

The decrease in expenses for severance pay and pensions, as compared with the previous year, primarily results from changes in the provision for severance pay and pensions, which decreased by EUR 166,186.05 in 2017, whereas they increased by EUR 420,203.76 in the previous year due to lower market yields.

9.4. Related parties

Tax group

Effective as of 2016, a tax group pursuant to § 9 of the Corporate Income Tax Act was formed with Satere as the group parent and Gesona, Kommunalkredit, KBI, KPC and TrendMind as group members (for details see Note 7.1.9.).

Related parties

Related-party transactions are recognised under the balance-sheet items concerned. All related-party transactions are made in accordance with the arm's length principle. For current transactions, see Note 6.5.b.

9.5. Significant events after the balance sheet date

At the beginning of January 2018, Kommunalkredit introduced its online retail platform KOMMUNALKREDIT INVEST for retail clients also in Germany. KOMMUNALKREDIT INVEST offers sight deposits as well as term deposits for terms of up to ten years.

In February 2018, KA Finanz AG has launched a tender for services currently provided by Kommunalkredit. The bank intends to submit an offer for the continuation of such services. A decision by KA Finanz AG is expected by midyear 2018. Should the bank not be awarded with a continuing contract, the service contract with KA Finanz AG will expire in the first half of 2019. In such case the operative capacity will be adjusted during a contractually existing transition period of 12 months.

9.6. Disclosures relating to the Boards of the bank

<u>Members of the Executive Board</u>

Alois Steinbichler
Chief Executive Officer

Jörn Engelmann
Member of the Executive Board

Karl-Bernd Fislage
Member of the Executive Board
since 1 February 2017

Wolfgang Meister
Member of the Executive Board

Members of the Supervisory Board

Patrick Bettscheider
Chairman, delegated by Interritus Limited

Christopher Guth
Deputy Chairman, delegated by Attestor Capital

Friedrich Andreae
Delegated by Attestor Capital; Managing Director of Gesona Beteiligungsverwaltung GmbH and Satere Beteiligungsverwaltungs GmbH

Katharina Gehra
Delegated by Interritus Limited; Managing Director of Gesona Beteiligungsverwaltung GmbH and Satere Beteiligungsverwaltungs GmbH

Jürgen Meisch
Managing Director of Achalm Capital GmbH

Werner Muhm
Former Director of the Vienna Chamber of Labour and the Federal Chamber of Labour
until 10 March 2017

Martin Rey
Managing Director of Maroban GmbH
since 24 July 2017

Patrick Höller
Nominated by the Staff Council

Franz Hofer
Nominated by the Staff Council
until 6 November 2017

Paul Matousek
Nominated by the Staff Council
since 6 November 2017

Renate Schneider
Nominated by the Staff Council
since 20 February 2017

9.7. State Commissioner

Edeltraud Lachmayer
State Commissioner, Federal Ministry of Finance

Bettina Horvath
Deputy State Commissioner, Federal Ministry of Finance

9.8. Government Commissioner

Appointed to serve as Government Commissioner of the cover pool for covered bonds in 2017:

Karin Fischer
Government Commissioner, Federal Ministry of Finance

Sandra Kaiser
Deputy Government Commissioner, Federal Ministry of Finance

Vienna, 5 March 2018

The Executive Board of
Kommunalkredit Austria AG

Alois Steinbichler	**Jörn Engelmann**	**Karl-Bernd Fislage**	**Wolfgang Meister**
Chief Executive Officer	Member of the Executive Board	Member of the Executive Board	Member of the Executive Board

Schedule of Participations and Investments in Affiliated Companies as at 31 December 2017 (Annex 1)

Pursuant to § 238 (2) of the Austrian Company Code, the Schedule of Participations shows all direct companies in which Kommunalkredit holds a share of at least 20%.

Name and registered office in EUR	Investment in % 2017	Investment in % 2016	Equity	Acquisition cost	Book value 31/12/2017	Book value 31/12/2016	Profit for the period after tax	Latest audited financial statements
I. Participations								
Kommunalnet E-Government Solutions GmbH, Vienna	45.00%	-	1,032,224.75	344,025.00	344,025.00	-	166,720.40	31/12/2017
Kommunalleasing GmbH, Vienna	50.00%	-	-16,469,331.64	750,000.00	0.00	-	5.246.786,86	31/12/2017
II. Investments in affiliated companies								
Kommunalkredit Beteiligungs- und Immobilien GmbH, Vienna*	-	100.00%	-	-	-	5,943,348.12	-	31/12/2016
Kommunalkredit KBI Immmobilien GmbH & Co KG, Vienna*	100.00%	-	32,081,364.76	32,081,365.00	32,081,365.00	-	-	-
Kommunalkredit KBI Immobilien GmbH, Vienna*	100.00%	-	34,875.00	35,000.00	35,000.00	-	-125.00	-
Trendmind IT Dienstleistung GmbH, Vienna	100.00%	-	407,040.12	150,000.00	150,000.00	-	156,040.12	31/12/2017
Kommunalkredit Public Consulting GmbH, Vienna	90.00%	90.00%	1,528,105.27	346,500.00	346,500.00	346,500.00	661,364.34	31/12/2017

*Pursuant to the merger agreement dated 9 November 2017 with retrospective effect from 30 June 2017, the effective date of the merger, which has become effective as of 1 December 2017 with the entry in the Companies Register, Kommunalkredit Beteiligungs- und Immobilien GmbH, Vienna, whose business activities focused mainly on managing real estate assets and participations within the Kommunalkredit Group, was merged into Kommunalkredit Austria AG (for details see item 3.5). Real estate assets are now mainly managed by Kommunalkredit KBI Immobilien GmbH, Kommunalkredit KBI Immobilien GmbH & Co KG and Kommunalkredit TLI Immobilien GmbH & Co KG, which were founded in the second half of 2017 and which have no other operating activities.

Schedule of Non-current Asset Transactions pursuant to § 226 (1) of the Austrian Company Code as at 31 December 2017 (Annex 2)

		Acquisition costs							Cumulative write-downs						Book values			
	Non-current assets in EUR	as at 1/1/2017	Currency translation	as at 1/1/2017	Additions	Merger	Disposals	as at 31/12/2017	Cumulative depreciation and amortisation/ Additions as at 1/1/2017	Additions	Merger	Disposals	Cumulative depreciation and amortisation/ Additions 2017	Book value 31/12/2017	Book value 31/12/2016	Write-down 2017	Write-up 2017
1.	Public-sector debt instruments	105,000,000.00	0.00	105,000,000.00	87,811,710.00	0.00	0.00	192,811,710.00	0.00	52,622.06	0.00	0.00	52,622.06	192,759,087.94	105,000,000.00	52,622.05	0.00
2.	Loans and advances to customers	288,651,935.08	-1,036,383.53	287,615,551.55	2,800,000.00	0.00	35,982,184.53	254,433,367.02	1,473,713.45	0.00	0.00	-1,473,713.45	0.00	254,433,367.02	287,178,221.63	0.00	0.00
3.	Bonds and other fixed-income securities	95,119,760.39	0.00	95,119,760.39	9,276,882.50	0.00	16,094,540.16	88,302,102.72	-56,808.94	12,168.63	0.00	139,328.14	94,687.82	88,207,414.90	95,176,569.33	13,644.48	0.00
4.	Participations	2,425,070.00	0.00	2,425,070.00	426,000.00	1,094,025.00	0.00	3,945,095.00	0.00	1,181,000.00	750,000.00	0.00	1,931,000.00	2,014,095.00	2,425,070.00	1,181,000.00	0.00
5.	Investments in affiliated companies	6,339,848.12	0.00	6,339,848.12	32,116,365.00	-5,793,348.12	50,000.00	32,612,865.00	0.00	0.00	0.00	0.00	0.00	32,612,865.00	6,339,848.12	0.00	0.00
	Property																
6.	Intangible non-current assets	4,246,448.47	0.00	4,246,448.47	123,932.44	0.00	0.00	4,370,380.91	3,957,701.14	221,278.18	0.00	0.00	4,178,979.32	191,401.59	288,747.33	221,278.18	0.00
7.	Property, plant and equipment	0.00	0.00	0.00	89,496.99	37,333,087.80	36,682,656.91	739,927.88	0.00	316,028.56	13,689,134.85	-13,685,168.00	319,995.41	419,932.47	0.00	316,028.56	0.00
8.	Office furniture and equipment	1,943,667.77	0.00	1,943,667.77	247,097.15	5,372,174.93	11,422.63	7,551,517.22	39,474.38	324,210.33	4,658,399.16	-11,422.63	5,010,661.24	2,540,855.98	0.00	324,210.33	0.00
		503,726,729.83	-1,036,383.53	502,690,346.30	132,891,484.08	38,005,939.61	88,820,804.24	584,766,965.75	5,414,080.03	2,107,307.76	19,097,534.01	-15,030,975.94	11,587,945.85	573,179,019.90	496,408,456.41	2,108,783.60	0.00
	* of which minor-value assets according § 241 (1a) Austrian Company Code				22,645.84	354,913.07	5,081.45			22,645.84	354,913.07	5,081.45					

AUDIT OPINION

Report on the Financial Statements

Audit Opinion

We have audited the financial statements of Kommunalkredit Austria AG, Vienna, which comprise the balance sheet as at December 31, 2017, the income statement for the fiscal year then ended and the notes.

In our opinion, the accompanying financial statements comply with legal requirements and give a true and fair view of the financial position of the Company as at December 31, 2017, and of its financial performance for the fiscal year then ended in accordance with the Austrian Commercial Code and the Austrian banking regulations.

Basis for Opinion

We conducted our audit in accordance with Regulation (EU) No. 537/2014 (hereinafter EU Regulation) and Austrian generally accepted auditing standards. Those standards require the application of the International Standards on Auditing (ISAs). Our responsibilities under those provisions and standards are further described in the "Auditor's Responsibilities for the Audit of the Financial Statements" section of our report. We are independent of the Company in accordance with Austrian Generally Accepted Accounting Principles and professional requirements and we have fulfilled our other ethical responsibilities in accordance with these requirements. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.

Key Audit Matters

Key audit matters are those matters that, in our professional judgment, were of most significance in our audit of the financial statements of the fiscal year. These matters were addressed in the context of our audit of the financial statements as a whole, and in forming our opinion thereon, and we do not provide a separate opinion on these matters.

We have structured key audit matters as follows:
- Description
- Audit approach and findings
- Reference to related disclosures

1. Project financing

- Description

In 2016, Kommunalkredit Austria AG, Vienna, reoriented its business model in the area of infrastructure financing. The consolidated financial statements as at December 31, 2017 include a total lending volume of EUR 2.2 billion (loans and advances to customers and credit institutions as well as contingent liabilities), of which EUR 635 million pertains to project financing newly agreed in 2017 (prior year: EUR 146 million). Whether these pro-ject financing loans – which are highly complex given their particularly individual nature – are recoverable or not depends on the expectations placed on the economic development of the financed projects as well as on the assumptions used in the measurement of the loans.

In the reporting year, Kommunalkredit Austria AG, Vienna, revised the existing loan processes particularly with regard to the project financing business and carried out adjustments to the organizational structure particularly by increasing the number of front office staff as well as by appointing a new management board member.

Given the change in the business model, the complexity of the transactions and the high degree of assumptions and expectations required in the measurement of the loans and advances, we determined the recoverability of the new transactions to be a key audit matter.

- Audit approach and findings

With a view to evaluate the appropriateness of the processes and the measurement of the project financing, we
- evaluated the significant lending business processes and their appropriateness,
- identified and tested the internal control system, particularly the key controls involved in approving loans, in the ongoing monitoring and the early detection process, as well as critically assessed the internal control system for the correct use of the rating models and valuation of collateral, and evaluated the appropriateness of the loan processes; we found that we can rely on the controls in place in the course of our audit,
- tested, on a sample basis, whether events occurred or will occur that significantly affect the borrower’s repayment ability with regard to loans and advances that are not considered as defaulted, in particular with a view to the assumptions made by the credit institution in the course of scenario analyses,
- evaluated the appropriateness of the risk assessment made by Kommunalkredit Austria AG, Vienna, for a sample of loans and advances. With regard to these loans and advances, we critically assessed the cash flows estimated by Kommunalkredit Austria AG, Vienna, to be received from interest, repayments and collateral so as to be able to assess the appropriateness of the risk assessments made by the credit institution stated in the financial statements,
- with a view to assess the reliability of the processes used to calculate the collective loan loss provisions, evaluated the method applied as well as the backtesting of the collective loan loss provisions by using a sample and found that the parameters used – when being considered retrospectively – were in an appropriate range,

- assessed the information regularly brought to management's attention at the meetings of the Risk Management Committee ("RMC") as well as in quarterly valuation meetings held at fixed dates and continuously monitored the decisions of these Committees. At the valuation meetings held at fixed dates, crucial decisions regarding the necessary credit spread adjustments in the course of changes made to models are taken.

- Reference to related disclosures

Please refer to statements made by management in items 3.3., 4.3., 5.1., 5.2., 7.1.1. and 7.1.3. in the notes as well as in the management report.

2. Deposit business process – Online retail funding

- Description

In the fiscal year 2017, Kommunalkredit Austria AG, Vienna, implemented the online retail platform "Kommunalkredit Invest" (online retail funding). Kommunalkredit Austria AG, Vienna, offers the depositing of funds available on a daily basis or of fixed-term deposits of a period of up to 10 years to private individuals. The platform has been available to customers in Austria since September 2017 and to customers in Germany since the beginning of 2018. The volume of deposits of private customers made via the online retail platform stands at EUR 116 million as at December 31, 2017.

Kommunalkredit Austria AG, Vienna, decided to outsource material process steps regarding the acquisition and processing of transactions made via the online retail platform to FinTech Group Bank AG, Willich, Germany.

- Audit approach and findings

We

- evaluated the business processes implemented at Kommunalkredit Austria AG, Vienna, with regard to outsourcing online retail funding to meet the requirements under Section 25 Austrian Banking Act (BWG) and found them appropriate,
- tested the interfaces set up in the system between Kommunalkredit Austria AG, Vienna, and the service organisation,
- evaluated the presentation of the online retail funding (ORF) deposit business and the corresponding deferred interest in the balance sheet and statement of profit and loss of Kommunalkredit Austria AG, Vienna,
- assessed the agreements with the service organisation (Service Level Agreement dated May 12, 2017, service tickets, operating procedures, etc.),
- satisfied ourselves of the effectiveness of the implemented processes and controls in the course of an on-site visit to the service organisation,
- critically assessed the process and the controls for the automated interest calculation and establishing the customers' quarterly information (account notifications) and reperformed the calculation,
- inspected the internal audit reports as well as the audit reports of the Federal Financial Supervisory Authority (*Bundesanstalt für Finanzdienstleistungsaufsicht*, BaFin) on "money laundering and compliance" of the service organisation and with regard to serious deficiencies.

- Reference to related disclosures

Please refer to statements made by management in items 4.11., 7.1.4.2. and 9.5. in the notes and in the management report.

Responsibilities of Management and the Audit Committee for the Financial Statements

Management is responsible for the preparation and fair presentation of these financial statements in accordance with the Austrian Commercial Code and the banking regulations, and for such internal control as management determines is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error.

In preparing the financial statements, management is responsible for assessing the Company's ability to continue as a going concern, disclosing, as applicable, matters related to going concern and using the going concern basis of accounting unless management either intends to liquidate the Company or to cease operations, or has no realistic alternative but to do so.

The audit committee is responsible for overseeing the Company's financial reporting process.

Auditor's Responsibilities for the Audit of the Financial Statements

Our objectives are to obtain reasonable assurance about whether the financial statements as a whole are free from material misstatement, whether due to fraud or error, and to issue an auditor's report that includes our opinion. Reasonable assurance is a high level of assurance, but is not a guarantee that an audit conducted in accordance with the EU Regulation and with Austrian generally accepted auditing standards, which require the application of ISAs, will always detect a material misstatement when it exists. Misstatements can arise from fraud or error and are considered material if, individually or in the aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of these financial statements.

As part of an audit in accordance with the EU Regulation and with Austrian generally accepted auditing standards, which require the application of ISAs, we exercise professional judgment and maintain professional skepticism throughout the audit.

We also

- identify and assess the risks of material misstatement of the financial statements, whether due to fraud or error, design and perform audit procedures responsive to those risks, and obtain audit evidence that is sufficient and appropriate to provide a basis for our opinion. The risks of not detecting a material misstatement resulting from fraud is higher than for one resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal control.
- obtain an understanding of internal control relevant to the audit in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Company's internal control.
- evaluate the appropriateness of accounting policies used and the reasonableness of accounting estimates and related disclosures made by management.
- conclude on the appropriateness of management's use of the going concern basis of accounting and, based on the audit evidence obtained, whether a material uncertainty exists related to events or conditions that may cast significant doubt on the Company's ability to continue as a going concern. If we conclude that a material uncertainty exists, we are required to draw attention in our auditor's report to the related disclosures in the financial statements or, if such disclosures are inadequate, to modify our opinion. Our conclusions are based on the audit evidence obtained up to the date of our auditor's report. However, future events or conditions may cause the Company to cease to continue as a going concern.

- evaluate the overall presentation, structure and content of the financial statements, including the disclosures, and whether the financial statements represent the underlying transactions and events in a manner that achieves fair presentation.

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

We also provide the audit committee with a statement that we have complied with all relevant ethical requirements regarding independence, and to communicate with them all relationships and other matters that may reasonably be thought to bear on our independence, and where applicable, related safeguards.

From the matters communicated with the audit committee, we determine those matters that were of most significance in the audit of the financial statements of the current period and are therefore the key audit matters. We describe these matters in our auditor’s report unless law or regulation precludes public disclosure about the matter or when, in extremely rare circumstances, we determine that a matter should not be communicated in our report because the adverse consequences of doing so would reasonably be expected to outweigh the public interest benefits of such communication.

Report on Other Legal and Regulatory Requirements

Comments on the Management Report for the Company

Pursuant to the Austrian Commercial Code, the management report is to be audited as to whether it is consistent with the financial statements and as to whether the management report was prepared in accordance with the applicable legal requirements.

Management is responsible for the preparation of the management report in accordance with the Austrian Commercial Code and the Austrian banking regulations.

We conducted our audit in accordance with Austrian Standards on Auditing for the audit of the management report.

Opinion
In our opinion, the management report for the Company was prepared in accordance with the applicable legal requirements and is consistent with the financial statements.

Statement
Based on the findings during the audit of the financial statements and due to the obtained understanding concerning the Company and its circumstances no material misstatements in the management report came to our attention.

Other information

Management is responsible for the other information. The other information comprises the information included in the annual report, but does not include the financial statements, the management report and the auditor’s report.

Our opinion on the financial statements does not cover the other information and we do not express any form of assurance conclusion thereon.

In connection with our audit of the financial statements, our responsibility is to read the other information and, in doing so, consider whether the other information is materially inconsistent with the financial statements or our knowledge obtained in the audit or otherwise appears to be materially misstated. If, based on the work we have performed, we conclude that there is a material misstatement of this other information, we are required to report that fact. We have nothing to report in this regard.

Additional Information in Accordance with Article 10 of the EU Regulation

We were appointed as statutory auditor at the ordinary general meeting dated April 7, 2016. We were engaged by the supervisory board on April 7, 2016. We have audited the Company for an uninterrupted period since its foundation in 2015 (three years). In that year, the operating business of Kommunalkredit Austria AG, Vienna, Austrian Companies Register no. 439528s, was spun off to Kommunalkredit Austria AG, Vienna, Austrian Companies Register no. 45776v ("KA old"). We had audited KA old since 2010.

We confirm that the audit opinion in the "Report on the Financial Statements" section is consistent with the additional report to the audit committee referred to in Article 11 of the EU Regulation.

We declare that we did not provide any prohibited non-audit services (Article 5 (1) of the EU Regulation) and that we remained independent of the audited company in conducting the audit.

Responsible Engagement Partner

Responsible for the proper performance of the engagement is Ms. Dorortea-E. Rebmann, Austrian Certified Public Accountant.

Vienna, March 6, 2018

PwC Wirtschaftsprüfung GmbH

signed:

Dorotea-E. Rebmann
Austrian Certified Public Accountant

This report is a translation of the original report in German, which is solely valid. Publication and sharing with third parties of the financial statements together with our auditor's opinion is only allowed if the financial statements and the management report are identical with the German audited version. This audit opinion is only applicable to the German and complete financial statements with the management report. For deviating versions, the provisions of Section 281 (2) UGB apply.

STATEMENT BY THE LEGAL REPRESENTATIVES

Kommunalkredit Austria AG

Annual Financial Statements 2017

We herewith confirm to the best of our knowledge that the **Financial Statements** of the parent, prepared in accordance with the relevant accounting standards, present a true and fair view of the assets, the financial position and the income of the company, that the Management Report presents the development of business, the results and the position of the company in such a way that it conveys a true and fair view of the assets, the financial position and the income of the company, and that the Management Report describes the essential risks and uncertainties to which the Company is exposed.

Vienna, 5 March 2018

The Executive Board of
Kommunalkredit Austria AG

Alois Steinbichler	**Jörn Engelmann**	**Karl-Bernd Fislage**	**Wolfgang Meister**
Chief Executive Officer	Member of the Executive Board	Member of the Executive Board	Member of the Executive Board

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