Deutsche Postbank AG

Disclosure Report
in accordance with the Solvency Regulation
(Pillar III Report pursuant to Basel II)

as of December 31, 2007

Table of Contents

1 Scope of application

In its Basel II Framework, the Basel Committee on Banking Supervision has defined standards of international application for capital adequacy requirements of banks commensurate with their underlying risks. In terms of the Solvency Regulation (SolvV) of December 14, 2006, the European minimum capital standards listed in the Banking Directive (2006/48/EC) and the Capital Adequacy Directive (2006/49/EC) as well as the respective equivalent parameters of the Basel capital adequacy recommendation ("Basel II") was implemented into national law effective as of January 1, 2007. The Solvency Regulation replaces the past Principle I and provides a concrete framework for the capital adequacy for banks required by section 10 of the German Banking Act – (KWG).

By means of the present report, Deutsche Postbank AG (herein after referred to as "Postbank"), the parent institution of the Postbank group for regulatory purposes in accordance with section 10a (1) sentence 1 of the KWG implemented the disclosure requirements pursuant to sections 319 to 337 of the SolvV, read in conjunction with section 26a of the KWG effective as of December 31, 2007 for the first time.

The quantitative information published in this report, in accordance with section 339 (20) of the SolvV, refers to those portfolios for which Postbank already calculated the capital adequacy on the basis of the Solvency Regulation as early as 2007 (see Section 2). This report does not contain all the portfolios for which Postbank determined the counterparty default risk in 2007 on the basis of the transitional rules in accordance with section 339 (10) of the SolvV pursuant to the rules of the existing Principle I. In particular, these are the portfolios of subsidiaries, the predominant share of OTC derivatives and current account credits and the lending business in the Retail banking segment. Postbank plans to make a full disclosure as of June 30, 2008, which will comprise all portfolios throughout the Postbank Group.

The Management Board of the Postbank Group has decided to apply the waiver rule pursuant to section 2a of the KWG for the individual institution Deutsche Postbank AG with regard to the requirements of section 10 of the KWG. According to the waiver rule, in meeting organizational and process-related terms and conditions, individual institutions may be exempted from certain rules relating to capital adequacy requirements as well as reporting obligations at the institutional level. Postbank has notified Deutsche Bundesbank and the Federal Financial Supervisory Authority (BaFin) in accordance with section 2a (2) sentence 1 of the KWG of its compliance with the terms and conditions of section 2a (6) Nos. 1 and 2 of the KWG.

All information stated in this report refers in principle to the companies included in the regulatory basis for consolidation. These largely correspond to the companies included under accounting parameters. The following table shows the differences between the individual bases for consolidation, including the names of the companies and their consolidation under regulatory and accounting aspects. In the process, the allocation of companies to the types of enterprises is made in accordance with supervisory group report based on the definitions contained in section 1 of the KWG. All companies designated are fully consolidated. No company is liable to a regulatory capital deduction. Quota-based or at-equity consolidations are not relevant for Postbank at the reference date.

Postbank companies included in consolidation			
Type of enterprise	Company	Regulatory consolidation	Accounting consolidation
Banks	Deutsche Postbank AG, Bonn	X	X
	BHW Bausparkasse AG, Hameln	X	X
	BHW Bank AG, Hameln	X	X
	BHW Home Finance Ltd., New Dehli, Indien	X	X
	Deutsche Postbank International S. A., Munsbach, Luxembourg	X	X
	PB Capital Corporation, Wilmington, Delaware, USA	X	X
	PB Realty Corporation, New York, USA	X	X
	VÖB-ZVD Bank für Zahlungsverkehrsdienstl. GmbH, Bonn	X	X
Financial service providers	Deutsche Postbank Financial Services GmbH, Frankfurt/Main	X	X
Financial holding companies	BHW Holding AG, Hameln	X	X
	PB Holdings Incorporation, Wilmington, Delaware,USA	X	X
Finance companies	Betriebs-Center für Banken AG, Frankfurt/Main	X	X
	BHW Eurofinance B. V., Arnheim, Niederlande	X	
	BHW Gesellschaft für Vorsorge mbH, Hameln	X	X
	BHW Gesellschaft für Wohnungswirtschaft mbH, Hameln	X	X
	Deutsche Postbank Funding LLC I, Wilmington, Delaware, USA	X	X
	Deutsche Postbank Funding LLC II, Wilmington, Delaware, USA	X	X
	Deutsche Postbank Funding LLC III, Wilmington, Delaware,USA	X	X
	Deutsche Postbank Funding LLC IV, Wilmington, Delaware, USA	X	X
	Deutsche Postbank Funding Trust I, Wilmington, Delaware, USA	X	X
	Deutsche Postbank Funding Trust II, Wilmington, Delaware, USA	X	X
	Deutsche Postbank Funding Trust III, Wilmington, Delaware, USA	X	X
	Deutsche Postbank Funding Trust IV, Wilmington, Delaware, USA	X	X
	DSL Holding AG i. A., Bonn	X	X
	PB Factoring GmbH, Bonn	X	X
	Postbank Beteiligungen GmbH, Bonn	X	X
	Postbank Leasing GmbH, Bonn	X	X
Capital investment companies	BHW Invest S. A. R. L., Luxembourg	X	
	Deutsche Postbank Privat Investment Kapitalanlagegesellsch. mbH, Bonn	X	X
	Deutsche Postbank Vermögens-Management S. A., Munsbach, Luxembourg	X	X
Ancillary service providers	Betriebs-Center für Banken Payments & Services GmbH, Munic	X	X
	Betriebs-Center für Banken Processing GmbH, Frankfurt/Main	X	
	BHW Gesellschaft für Wohnungswirtschaft mbH & Co Immobilienverwaltung KG, Hameln	X	X
	Deutsche Postbank Finance Center Objekt GmbH, Munsbach, Luxembourg	X	X
	DPBI Immobilien KGaA, Munsbach, Luxembourg	X	X
	einsnull IT-Support GmbH, Cologne	X	X
	PB Finance (Delaware) Incorporation, Wilmington, Delaware, USA	X	X
	PB Firmenkunden AG, Bonn	X	X
	Postbank Filialvertrieb AG, Bonn	X	X
	Postbank Immobilien und Baumanagement GmbH, Bonn	X	X
	Postbank Immobilien und Baumanagement GmbH & Co. Objekt Leipzig KG, Bonn	X	X
	Postbank P. O. S. Transact GmbH, Eschborn	X	
	Postbank Systems AG, Bonn	X	X
Other enterprises	Betriebs-Center für Banken Verwaltungs GmbH, Frankfurt/Main		X
	BHW Immobilien GmbH, Hameln		X
	PBC Carnegie LLC, Wilmington, Delaware, USA		X
	Postbank Finanzberatung AG, Hameln		X
	Postbank Versicherungsvermittlung GmbH, Bonn		X

Table 1

Due to their enterprise type, the companies reported in Table 1 under "other companies" are not included in the regulatory basis for consolidation. These companies are subjected to regulatory risk weightings.

Compared with the consolidation under accounting law, four companies have been included in the regulatory basis for consolidation; due to their subordinate economic importance, they are not included in the accounting basis for consolidation. The companies in question are BHW Eurofinance B. V., BHW Invest S. A. R. L, Betriebs-Center für Banken Processing GmbH and Postbank P. O. S. Transact GmbH.

In a letter dated September 30, 2007, Postbank informed BaFin of the exemption from inclusion in the consolidated report in accordance with section 31 (3) of the KWG for the following subordinated companies:

- BHW Direktservice GmbH, Hameln
- BHW Financial Srl, Verona
- CREDA Objektanlage- und -verwaltungsgesellschaft mbH, Bonn
- easyhyp GmbH, Hameln
- easytrade services GmbH, Leipzig
- RALOS Verwaltung GmbH & Co. Vermietungs KG, Munich

2 Methods for calculating minimum capital requirements

The Solvency Regulation provides various methods for calculating the regulatory minimum capital requirements for counterparty default risks:

- Standardized approach to credit risk
- Approaches based on internal ratings (IRBA):
  - on the basis of internal estimates of probabilities of default (IRB basis approach)
  - on the basis of internal estimates of probabilities of default, conversion factors and loss quotas (advanced IRB approach)
  - for the retail business

On December 21, 2006 Postbank received approval from the *Bundesanstalt für Finanzdienstleistungsaufsicht* (German Federal Financial Supervisory Authority) to adopt the IRB basis approach as well as the IRB approach for the retail business to calculate the minimum capital requirements. Therefore, in relation to the classes of receivables under the SolvV, since January 1, 2007 Postbank has used the IRB basis approach and the IRB approach for the retail business to calculate its regulatory capital requirements for the following portfolios:

Postbank portfolios subject to the IRB approach in 2007
Central governments: states
Institutions: banks
Corporates: domestic corporates, specialized finance
Retail business: construction finance, installment loans, giro credits for self-employed and corporate customers, retail receivables purchased
Equities unless excluded in accordance with section 338 (4) of SolvV
Securitizations
Other credit-independent assets

Table 2

For 2007, the coverage ratio calculated pursuant to section 67 of the SolvV for the portfolio calculated on the basis of internal ratings amounted to 60.4 % of the exposure values and 51.1 % of the risk-weighted exposure values (calculated on June 30, 2007). The coverage ratio represents the ratio of the total IRBA exposure values or IRBA riskweighted exposure values to all exposure values or risk-weighted exposure values to be taken into account under section 67 (4) of the SolvV. For the year 2007, the BHW portfolios were treated as counterparty risk positions eligible for exceptions in accordance with section 67 (4) No. 7 of the SolvV and therefore were not included in calculating the coverage ratio.

With respect to the other portfolios of Postbank as well as the risk positions of the other companies included in the regulatory basis for consolidation, in 2007 the Deutsche Postbank Group applied the transition regulation set out in section 339 (10) of the SolvV and calculated the risk of counterparty default on the basis of the existing Principle I.

Starting on January 1, 2008, Postbank additionally began reporting capital adequacy on the basis of internal ratings for OTC derivative instruments as well as for the predominant proportion of the portfolios of PB Factoring GmbH; BHW-Bausparkasse AG, Hameln; Deutsche Postbank International S.A., Luxembourg; the London branch and PB capital, Wilmington/USA; and PB Realty, New York, New York, USA. Thus for 2008, the expected coverage ratio (including BHW portfolios) for the portfolios calculated on the basis of internal ratings is 92.3% of the exposure values and 89.9% of the riskweighted exposure values (calculated as at June 30, 2007). For the remainder of the portfolios not calculated in accordance with the IRB approach, the standardized approach to credit risk will be used starting in 2008.

Pursuant to section 70 of the SolvV, in addition to operations being discontinued, Postbank excludes, in particular, counterparty default risks arising from the asset class of central governments, performance of which is owed inter alia by the Federal Republic of Germany or domestic regional, local and municipal governments, from the application of the IRB approach, with no time limit being imposed. In addition, it applies the permanent exemption from the IRB approach as regards receivables with a negligible share of the total portfolio.

For calculating the minimum capital requirements for market price risks, Postbank uses the standardized methods available under the regulatory framework. Postbank plans to introduce an internal market risk model in the medium term also for measuring and controlling market price risks, and also to use this model for calculating the minimum capital requirements under regulatory laws.

For the calculation of minimum capital requirements for operational risks, banks have the basic indicator approach, the standardized approach and the advanced measurement approach available to them. Postbank uses the standardized approach for calculating its minimum capital requirements. This is the basis for a planned, medium-term implementation of the advanced measurement approach. To this end, Postbank develops models of its own and is in the process of establishing an extensive data history.

3 Structure and volume of own funds

3.1 Elements of own funds

Postbank's own funds are calculated in accordance with the IFRS accounting standards. The amounts shown in the following overview correspond to the values reported in the Postbank Group's consolidated annual financial statements as at December 31, 2007:

Summary of regulatory minimum capital requirements	
	€m
Capital paid up	3,198
Other eligible reserves	3,542
Special items for general banking risks pursuant to section 340g of HGB	–
Other Tier 1 capital instruments	19
Deduction items from core capital pursuant to section 10 (2a) sentence 2 of KWG	– 1,105
Total amount of Tier 1 capital pursuant to section 10 (2a) of KWG	5,654
Total amount of Tier 2 capital pursuant to section 10 (2b) of KWG and eligible Tier 3 capital pursuant to section 10 (2c) of KWG	3,511
Total amount of capital deduction items pursuant to section 10 (6) and (6a) of KWG, 50 % of which are deducted from Tier 1 and Tier 2 capital	– 398
thereof: shortfalls in valuation adjustments and expected losses in the case of IRBA exposures pursuant to section 10 (6a) Nos. 1 and 2 of KWG	– 274
Total amount of modified own funds available pursuant to section 10 (1d) of KWG and eligible Tier 3 capital pursuant to section 10 (2c) of KWG	8,767
thereof: Tier 1 capital	5,455
thereof: Tier 2 capital	3,312
thereof: Tier 3 capital	0

Table 3

The core capital consists of subscribed capital amounting to €410 million, divided up into 164 million registered no-par-value shares. The Management Board is authorized with the approval of the Supervisory Board to increase the capital stock of Postbank by €41 million against a non-cash contribution (limited until March 24, 2009) and by €137 million against a cash deposit (limited until May 10, 2011).

Moreover, the Tier 1 capital includes capital paid up in the form of capital reserves from issues, amounting to €1,161 million (after taking account of the effects of the regulatory consolidation pursuant to section 10a (6) of the KWG, this is equivalent to an amount of €1,137 million).

Tier 1 capital also includes assets contributed by silent partners amounting to €1,651 million, comprising a nominal €51 million in silent participations and hybrid capital. By way of hybrid capital instruments, Postbank used its subsidiaries Deutsche Postbank Funding Trust LLC I to IV established for this purpose – to launch a total of four issues in the form of preferred securities, amounting to €1,600 million in nominal terms (as at 12/2007). These papers were issued in the years from 2004 to 2007 and are subject to interest in conformity with rates prevailing on the market.
Moreover, Tier 1 capital also takes account of other eligible reserves, amounting to €3,542 million. These comprise the reserves set up in the course of annual partial appropriations of net profits.

The other qualified Tier 1 capital instruments, amounting to €19 million, are essentially the capitalized differences of the subsidiaries consolidated under the German Commercial Code (HGB) in accordance with section 10a (6) of the KWG.

Tier 2 capital of Postbank comprises eligible profit participation certificates amounting to €1,213 million and eligible longer-term subordinated liabilities (above all, promissory note loans and bearer debentures) amounting to €2,308 million, meeting the requirements of section 10 (5) and (5a) of the KWG, reduced by €10 million in deductions.

Holders of participation certificates receive an annual non-profit-dependent dividend prior to the portion paid out to shareholders; the entitlement to such a dividend will be reduced in the event that a distributable profit is not available. The participation certificates cannot be terminated by the investors. Postbank has a right of termination as regards certain contractually agreed tax events. The participation certificates have a term to maturity of more than 10 years, and promissory note loans also have residual terms to maturity below 10 years. As a rule, the minimum denomination is €5 million.

The difference between the sum total of expected losses for all IRBA positions of the asset classes of central governments, institutions, enterprises and the retail business as well as valuation adjustments and provisions set up for these positions is to be deducted together with expected losses for IRBA participations totaling €274 million from Tier 1 and Tier 2 capital at 50 percent each.

As at the December 31, 2007 reference date, the Postbank Group had no Tier 3 capital in its portfolio.

In 2007 Postbank increased its level of own funds by €583 million, in particular by raising its Tier 1 capital by means of additional hybrid capital (Funding Trust LLC IV).

With regard to the equity interests that are part of the regulatory basis for consolidation, Deutsche Postbank AG is the indirect or direct principal shareholder. Most of the companies are headquartered in Germany or the EU. In the U.S. Postbank is represented by a total of eleven companies. Postbank notified BaFin in accordance with section 2a (2) of the KWG that restrictions in transfer of financial assets or own funds within the Postbank Group by third parties, companies under private or public law, supranational organizations or states are currently neither known nor discernible.

None of the companies forming part of the Postbank Group reflects a capital deficit as at the December 31, 2007 reference date.

3.2 Regulatory own funds

3.2.1 Regulatory capital requirements

Below, the regulatory capital requirements determined according to the HGB are shown separately for counterparty default risks, market price risks as well as operational risks, with the capital requirements representing each of the risk positions to be taken into account, multiplied by 8 %. The sum total of capital requirements as at December 31, 2007 amounted to €7,646 million. This sum includes the additional capital requirements of €360 million resulting from the transitional rule in accordance with section 339 (3 – 5) of the SolvV (floor provision).

The relief effect of the IRB approach cannot be realized to the full extent since the level of own funds of institutions that use the IRB approach to calculate the total capital charge for counterparty risks is not allowed to fall below 95 % in 2007 of the amount required to be kept in accordance with the provisions of Principle I. In 2008, this base amount will be reduced to 90 % of the Principle I capital requirements in accordance with section 339 (4) of the SolvV.

Capital requirements for counterparty default risks

The capital requirements for counterparty default risks in relation to the banking book and the counterparty risks of the trading book with regard to the portfolios specified in chapter 2 are calculated according to the IRB basis approach and the IRB approach for the retail business.

All other receivables have been backed to an extent of €3,347 million using the methodology of the existing Principle I. This includes the participations amounting to €129 million excluded in accordance with section 338 (4) of the SolvV from the IRBA for a limited period.

Capital requirements for counterparty risks	
	€m
Central governments	106
Institutions	401
Enterprises	408
Retail business	861
thereof: retail IRBA exposures secured by mortgage liens	679
thereof: qualified revolving IRBA exposures in retail business	1
thereof: other IRBA exposures in retail business	181
Participations controlled by probabilities of default	–
Model-controlled participations	–
Participations valued with a simple risk weighting	208
thereof: traded on securities markets	168
thereof: not trade but part of the diversified portfolio of holdings	–
thereof: other participations	40
Participations permanently excluded from IRBA pursuant to section 70 sentence 1 No. 6	–
Investment participations pursuant to section 83 (5) read in conjunction with (3) and pursuant to section 83 (4) sentence 2 No. 2	306
Securitizations	88
Other credit-independent assets	338
Counterparty risk pursuant to Principle I	3,347
Total	6,063

Table 4

Capital requirements for market price risk positions

The following table shows the capital requirements for market price risk positions. Postbank uses the standardized methods to calculate the capital requirements.

Capital requirements for market price risks	
	€m
Currency risks (total)	75
Commodity risks (total)	–
Interest risks (trading book)	896
Stock risks (trading book)	7
Other market price risks (total)	–
Total	978

Table 5

As at the December 31, 2007 reference date, no risks arising from commodity positions and no risks relating to market price risk positions are of relevance to Postbank.

Capital requirements for operational risks

The capital requirements for backing operational risks amount to a capital charge of €245 million calculated using the standardized approach on December 31, 2007. This refers to the installment-based share in accordance with section 339 (10) No. 3 of the SolvV, i.e. after a percentage-based reduction of the capital charge by the ratio between the assessment bases of the counterparty default risk positions for which the risk-weighted exposure values are calculated according to Principle I and the aggregate of the assessment bases of all counterparty risk positions.

3.2.2 Total and Tier 1 capital ratio

The following table shows the capital quotas for the Postbank Group, BHW Bausparkasse AG, Hameln, and Deutsche Postbank International S. A., Luxembourg. In the process, for the Deutsche Postbank Group the minimum capital requirements prior to the application of the transitional rule amounting to 95 % of the regulatory weighting factors in accordance with Principle I are shown pursuant to section 339 (3) of the SolvV as well as the effects thereof.

Total and Tier 1 capital ratios

	Total ratio in %	Tier 1 capital ratio in %	Basis for calculation in 2007
Deutsche Postbank Group, Bonn			
- prior to applying the transitional prov.	9.6	6.9	Solvency Regulation
- effect of the transitional provision	– 0.4	– 0.4	
BHW Bausparkassen AG, Hameln	9.7	6.4	Principle I
Deutsche Postbank International S. A., Luxembourg	10.2	–	Luxembourg regulatory law

Table 6

The total and Tier 1 capital ratios of the Postbank Group as at December 31, 2007 were, without exception, above the minimum regulatory ratios of 4 % for Tier 1 capital and 8 % for total capital. The institutions of the Postbank Group met the regulatory capital adequacy at all times throughout the period under review.

3.3 Internal management of capital

The risk-bearing capacity of Postbank is assessed with regard to investor protection and serves as the basis for deriving the system for limiting material risks. The sum total of the resources available to Postbank to hedge its risks is referred to as the risk cover amount. The Postbank Group considers its risk-bearing capacity as fulfilled if it can service its prior-ranking liabilities with a probability that corresponds to its target rating. In this respect, the Postbank Group bases its risk-bearing capacity on an appropriate confidence level amounting to 99.93 %.

To ensure that its risk-bearing capacity is guaranteed on a sustained basis, possible fluctuations in economic capital and stress scenarios are taken into account in the risk capital allocation. Accordingly, the Management Board of Postbank only makes part of the risk cover amount available for risk purposes. This amount is designated as risk capital and represents a limit for the entire risk of the Postbank Group. The risk capital is defined by the Group Management Board at least on a quarterly basis and allocated to the following risk categories of relevance to Postbank:

- Market price risks
- Credit risks
- Operational risks
- Real estate and equity risks
- Collective risks arising from the home savings business
- Business risks

Operational limits are established for the market price and credit risks directly manageable in the day-to-day business and backed by risk capital. Market price risk for both the core business and for own-account transactions is managed by allocating limits for the relevant portfolios. Control of credit risks in respect of receivables from central governments, institutions and corporates is essentially effected by imposing limits at the portfolio level as well as by investing in an optimized target portfolio in terms of risk and return aspects. Risks are only assumed within the limits derived from risk-bearing capacity considerations in order to achieve yields based on risk/return aspects. This aims to ensure that risks that could jeopardize the Bank's existence are avoided. As of December 31, 2007, risk capital utilization was 43.5 % for market price risk and 61 % for credit risk.

The other risk categories are not managed by operational limits but, in terms of their risk capital, represent values to be deducted from the risk cover amount. Again, Postbank constantly reviews the adequacy of the values deducted. Liquidity risks in the sense of insolvency risks are limited in the Postbank Group above all by constantly making highly liquid ECB-eligible securities available. The liquidity maturity transformation (LMT) risk at present is implicitly limited by the risk capital made available for business risks. Independent limiting of LMT risk is planned to be introduced in the medium term.

The risk-bearing capacity will be guaranteed as long as the limits allocated to the individual risk categories at the Group level are complied with and the aggregated limits and values to be deducted are lower than the risk cover amount. In managing the economic risk capital, the regulatory requirements relating to the minimum capital requirements (regulatory capital adequacy in accordance with the KWG, the Solvency Regulation and the German Large Exposures Regulation) are additional conditions that must be strictly observed.

To guarantee the constant risk-bearing capacity, Risk Controlling calculates the utilization of the limit for market price risk positions on a daily basis. The utilization of the global limit for the counterparty default risk is determined on a quarterly basis along with the capital charges for items to be deducted. Further particulars on internal management of own funds are listed in the Risk Report within the 2007 Annual Report at pp. 75 ff.

4 Risk management

Managing risks typical for banks calls for a high-quality, sophisticated risk management system in which all developments are reviewed on a timely and regular basis with regard to their impacts on risk. Postbank identifies, analyzes and manages these risks systematically and includes its findings within the scope of a risk-oriented management system for the Bank as a whole. In addition, Postbank has a comprehensive documentation system in place for dealing with bank-specific risks as well as a mature reporting system.

Postbank defines the risks addressed within the scope of this Report as follows:

- Market price risk: Potential losses from financial transactions that may be triggered by changes in interest rates, spreads, volatility, foreign exchange rates, and equity prices, of which
  - interest rate risks in the banking book: changes in the value of financial instruments in the banking book due to the change in market interest rates.

- Credit risk (counterparty default risks): Potential losses that may be caused by changes in the creditworthiness or insolvency of a counterparty.

- Liquidity risk:
  - Insolvency risk: the risk of being unable to meet current or future payment obligations in the full amount due, or as they fall due.
  - Liquidity maturity transformation risk: potential losses due to a change in our own refinancing curve.

- Operational risks: The risk of losses resulting from inadequate or failed internal processes and systems, people, or external events. The definition also extends to include legal risk.

Other risks of relevance to Postbank (real estate, equity interest, collective and business risks) are presented within the scope of the Risk Report within the 2007 Annual Report and are not the subject of disclosure in accordance with the Solvency Regulation.

4.1 Strategies, processes, structure and organization

In accordance with the parameters of MaRisk, the risk strategy is consistent with the business strategy and takes all key fields of activity and risk categories into account. In addition to an overarching, Group-wide risk strategy, Postbank's Management Board adopted resolutions on specific partial risk strategies for credit risks, market price risks, liquidity risks and operational risks. The nature and extent of the risks taken, as well as the strategy for managing such risks, depends on the individual business divisions, whose actions are prescribed within the scope of business strategy. Interest rate risks are managed by Postbank as a component of market price risks. An overview of the content of specific partial strategies for the individual risk categories is shown in the relevant sections of this disclosure report.

The Group Management Board is responsible for risk strategy, the risk-bearing capacity concept, due organization of risk management, monitoring the risk content of all transactions, and risk control. In conjunction with the Risk Committees, the Group Management Board has defined the fundamental strategies for activities on the financial markets as well as the other business sectors of the Group. The following chart illustrates the composition of the Committees and their areas of responsibility:

Composition and tasks of the Risk Committees			
	Credit Risk Committee	Market Risk Committee	Operational Risk Committee
Management Board members, General Managers	Credit Financial Markets Product Marketing Services	Financial Markets Credit Product Marketing Finance	IT/Operations Resources Services Branches
Tasks	Allocate credit risk limits Define limit system Resolve amendments to risk classification procedures Define standard risk costs	Allocate market and liquidity risk limits Manage strategic focus of the banking book Monitor earnings Manage MRC portfolio	Define operational risk strategy Define minimum requirements for Group units Define operational risk parameters

Table 7

Operational responsibility for risk control is spread across several units in the Group. These primarily include the Financial Markets division, Domestic/Foreign Credit Management, the credit functions of Private Banking and, on a decentralized basis, the subsidiaries BHW Bausparkasse AG, BHW Bank AG, Deutsche Postbank International S.A., PB Capital Corp. and PB Factoring GmbH as well as the London branch.

Risk Controlling, part of the Finance division, is the independent, Group-wide risk monitoring unit. Risk Controlling is responsible for determining the methods and models to be applied in risk identification, measurement and limitation. In cooperation with the Risk Controlling units of Postbank Group subsidiaries BHW Bausparkasse AG, BHW Bank AG, Deutsche Postbank International S.A., and PB Capital Corp. and the London branch, the department is responsible for operational risk control and reporting at Group level.

The Internal Audit unit is a further element of the Postbank Group's business and process-independent monitoring system. In terms of the Bank's organizational structure, it is subordinate to the Chairman of the Management Board and reports independently to the Group Management Board.

As part of the entrepreneurial monitoring system, in accordance with MaRisk, the Internal Audit unit audits all Postbank's subdivisions at intervals no longer than three years. Divisions subject to special risk are audited annually. The Internal Audit unit supports the introduction and implementation of key projects and performs special audits on certain occasions. Internal Audit's responsibilities also extend, in scaled-down form, to the subsidiaries of the Postbank Group.

The hedging and mitigation of risks as well as ongoing monitoring of the measures taken to minimize risks are controlled in dedicated form for the specific risk categories and described in the following chapters.

4.2 Group-wide risk reporting

Postbank's Management Board and Supervisory Board are informed by comprehensive reporting on the risk-bearing capacity, risks and limit utilization on a regular basis.

A report on the risk-bearing capacity is published on a quarterly basis. The risks and utilization of the respective limits in the specific risk types are presented in a large number of regular and specialized reports. The reporting comprises all subsidiaries of Deutsche Postbank AG that are relevant in terms of risk. Depending on the significance of the risks, differentiated reports are published on a daily, weekly, monthly or quarterly basis. Group-wide reports are usually addressed to the Group Management Board, the responsible members of the Risk Committees, and the operating units. In addition, the Supervisory Board receives excerpts of these reports. Recipients are thus kept informed of changes in relevant parameters in a timely and comprehensive manner. The Risk Controlling department is responsible for the methodology and content of Group-level risk reports.

In addition to regular management reports, rules have been established for an ad-hoc early warning reporting system that differentiates between different types of risk.

5 Management of counterparty risks

5.1 Strategies, processes, structure and organization

The credit risk strategy is derived from the business strategy and is integrated as part of the risk management system into overall bank management.

The credit risk strategy as a partial strategy is part of the comprehensive risk strategy of the Postbank Group (see chapter 4.1). The credit risk strategy deals with the guidelines and instruments of credit risk control as well as the planned development of lending operations across a defined planning period, taking account of the macroeconomic environment as well as the starting point of business strategy and the risk-bearing capacity of Postbank.

The credit risk strategy and organization directives for lending operations reflect the risk profile Postbank is willing to accept in relation to its customers and the credit product, how control is effected and what measures are taken to reduce risks. The general directive for lending operations contains statements on the organization and risk reporting to the responsible management bodies of the Bank. Management of the credit portfolio at the level of the Bank as a whole is subject to the risk/return calculation comprising both the aspect of adequate diversification of the portfolio and the deliberate definition of a collateralization level of the portfolios.

Management of the loan portfolios for corporates, institutions as well as central and regional governments and local authorities is geared to a target portfolio. This target portfolio was set up by specially taking a balanced ratio of returns to risks into account. The current portfolio of receivables is reconciled with the target portfolio on a quarterly basis. The departures identified are continually included in the control of the loan portfolios. For corporate financing transactions, in addition a profitability study is made in relation to specific transactions by means of the return on equity, the ratio of the risk-adjusted net margin and own funds tied town. Due to the pronounced risk diversification, the retail business is not part of the target portfolio but is managed via the net margin expectations after deduction of the expected risk.

Credit risk management was delegated by the Management Board to the Credit Risk Committee, with control by the Supervisory Board being performed in the Credit Committee. The Credit Risk Committee distributes the risk capital available for counterparty risks in accordance with the credit risk strategy to the market divisions, including the Financial Markets division, takes decisions on the introduction and material changes in risk classification procedures and defines the credit control parameters (e.g. standardized risk costs and cut-off limits).

The Risk Controlling department is responsible for regular review both of the appropriateness of the methods and processes deployed for the purpose of managing counterparty risks and compliance with statutory and regulatory requirements. It is responsible for developing and implementing new models and making adjustments to existing systems. In parallel, the Risk Controlling department continually monitors the development of risk provisioning and, on a quarterly basis, compliance with the credit value-at-risk limits.

In data processing, all relevant input factors and the results of ratings performed are kept in storage, enabling a continuous rating history to be kept for each customer and each transaction.

Operational control of counterparty risks is performed both at the individual transaction level and at the portfolio level in the Market and Back Office divisions. Details are described in chapter 5.3 "Rating-based credit risk management".

5.2 Rating systems

5.2.1 Overview

Rating systems serve to assess the creditworthiness of borrowers and guarantors and, as contemplated by section 60 (1) of the SolvV, comprise all methods, processes, control and monitoring procedures as well as data recording and processing systems used to support the evaluation of counterparty risks, the allocation of IRBA positions to rating classes or risk pools (ratings) and the quantification of expected defaults and losses for the IRBA positions. Internal rating systems are suitable if they correspond to the minimum requirements relating to the use of IRBA (section 56 of the SolvV). In addition to methodical and process-related organizational requirements, the rating systems need to have been proven suitable for classification of portfolio and new business.

The Risk Controlling Credit Risks department is responsible for the process of designing, implementing and monitoring the performance of the internal rating systems. Part of the process of monitoring the rating systems is the need to assess the predictive quality and the correct application of the rating systems, the calibration and validation of the rating systems and the incorporation of the results of monitoring activities into the internal reporting system.

All rating systems must be authorized by Postbank's Management Board. The Management Board receives regular management reports on the effectiveness of the rating systems as well as their results (see chapter 5.4).

As of the reporting reference date, with regard to the corresponding IRBA asset classes, rating systems approved by the regulatory authority are used for the purpose of calculating the capital requirements in accordance with IRBA for the following portfolios:

Overview of rating systems in IRBA asset classes

Rating system for:	SolvV asset class allocated
Central governments: states	Central governments
Institutions: banks	Institutions
Domestic corporates	Corporates
Commercial financing	Corporates: specialized financing
Private customers: construction financing	Retail business: IRBA exposures secured by mortgage liens
Giro credits for self-employed and corporate customers	Retail business: qualified, revolving IRBA exposures, other IRBA exposures in retail business
Private customers: installment loans	Retail business: other IRBA exposures
Retail receivables purchased	Retail business: receivables purchased

Table 8

All rating systems are clearly assigned to an asset class as contemplated by the SolvV. The respective rating models are deployed within the scope of the loan application and approval process for initial classification and in the case of regular and ad-hoc assessments of the creditworthiness of the borrower and/or guarantor. For borrowers and guarantors from the area of corporates, institutions, central governments as well as commercial financing transactions, Postbank uses rating models consisting of a statistical core (statistical balance sheet rating or Monte Carlo simulation of expected cash flows) and supplemented by a heuristic model to incorporate qualitative or other information in the risk classification. Collateral items of relevance are taken into account within the scope of credit risk mitigation methods.

Postbank deploys statistical scoring methods in its retail business. The scoring methods are based on information available internally and externally on the borrower and use statistical processes to evaluate the individual probability of default of the borrower and/or the facility in question. Within the scope of calculating the LGD (loss given default = loss ratio), the realization rates are taken into account in relation to the eligible collateral and, in the case of unsecured loans, the recovery rates.

All internal ratings and scorings are presented using a uniform master scale, which assigns to each rating or scoring result a rating class on the master scale, as well as the default probability determined for that class. Postbank uses the terminology of the Standard & Poor's rating agency here. The rating and scoring methods are validated as part of Postbank's annual model validation process and during ongoing monitoring. The model validation is based on the standardized core analyses that comprise such aspects as the stability of the model formula/the estimated parameters and the distributions, as well as of the accuracy of the rating model, and the confirmation of the predictive power of the models. Within the scope of the validation, possible changes in the loss history are also taken into account by adjusting the parameters accordingly.

In addition, the allocation of the rating classes in Postbank's master scale to default probabilities and the results of the parameter assessment are reviewed by the Risk Controlling Credit Risk department on an annual basis. The incorporation of model validation into Postbank's processes facilitates direct derivation of business policy and model-specific measures from the results of the core analyses. In data processing, all relevant input factors and the results of ratings performed are kept in storage, enabling a continuous rating history to be kept for each customer and each transaction.

Postbank's Internal Audit unit, being a process-independent entity, subjects the appropriateness of the internal rating systems, including compliance with the minimum requirements of the deployment of rating systems, to an annual review.

Below is a more detailed description of the rating systems used for calculating the minimum capital requirements in 2007. As of January 1, 2008 Postbank has included the following additional rating systems in the IRB approach:

- Asset class corporates:
  – European corporates excluding Great Britain
  – Corporates Great Britain
  – Corporates USA

- Asset class corporates: Special financing transactions:
  – Commercial financing transactions, Great Britain
  – Commercial financing transactions, USA

- Retail business: IRBA positions secured by charges on real estate:
  – Private customers: construction financing transactions of BHW

- Asset classes corporates, other IRBA positions in the retail business:
  – Corporate receivables purchased

5.2.2 Asset class central governments

The rating system for central governments is used for the classification of receivables from borrowers allocated to the IRBA asset category of "central governments" in accordance with section 74 of the SolvV. An expert model is deployed which was developed on the basis of internationally comparable key economic and political figures and ratios. The data pool of the Economic Intelligence Unit (EIU) serves as the basis for key quantitative figures. At present, 150 states are regularly classified on a quarterly basis, irrespective of the number of borrowers. In the event of material information being received having an impact on creditworthiness, an earlier re-rating is performed.

5.2.3 Asset class institutions

The rating system for institutions is used to classify all debtors allocated to the asset class of "Institutions" in accordance with section 75 of the SolvV. The rating system rates institutions on the basis of a balance sheet rating, taking external long-term ratings of the three major rating agencies (Standard & Poor's, Moody's and FitchRatings) into account. For foreign banks, the rating for central governments is also incorporated in the rating as such. After the initial rating, the banks are subject to a subsequent rating to monitor creditworthiness at least once per annum. In the event of material information being received having an impact on creditworthiness, a re-rating is performed in the course of the relevant year.

5.2.4 Asset class corporates

Rating system for domestic corporates

The rating system for domestic corporates classifies domestic debtors allocated to the IRBA asset class "corporates" by section 80 of the SolvV. The rating system rates individual enterprises with regard to their risk of default, using statistically calibrated balance sheet ratings and industry information. Moreover, additional qualitative factors are taken into account to assess the future development of the company in the rating system. After the initial rating, the customer category mentioned is subject to a subsequent rating to monitor creditworthiness at least once per annum. In the event of material information being received having an impact on creditworthiness, a re-rating is performed in the course of the relevant year.

Rating system for commercial financing transactions

The rating system for commercial financing transactions is used to classify facilities in commercial housing construction, loans to property developers, operator models, business in the field of real estate and movables leasing as well as real estate located abroad which are allocated to the IRBA asset class "Special financing transactions" in accordance with section 81 of the SolvV. In line with the nature of these financing transactions, the solvency of a customer and the bearer of the economic risk are taken into account along with property-related risk drivers. The latter are varied by means of Monte Carlo simulations and taken into account in the form of models based on future cash flows in estimating the risk of default. After the initial rating, all transactions are subject to a subsequent rating to monitor creditworthiness at least once per annum. In the event of material information being received having an impact on creditworthiness, a re-rating is performed in the course of the relevant year. A simple risk weighting for special financing transactions in accordance with section 97 of the SolvV is allocated to the individual rating classes of the rating system for commercial financing transactions.

5.2.5 Asset class retail business

Private customers construction finance

Using the rating system "Private customers, construction finance" standardized home construction loans are classified irrespective of the allocation of borrowers to natural or legal persons. These are assigned to the IRBA asset class "Retail business, positions secured by charges on real estate" in accordance with section 77 (3) of the SolvV. Since the causes of loan defaults in the categories of own and third-party use differ, two model variants of the rating system are deployed. Construction financing transactions are subject to application scoring; within the scope of the validation, the actual default rates are compared annually for each pool of receivables of the same rating class with the probabilities of default allocated according to the Postbank master scale, and the predictive quality of the scoring process is therefore verified. Separate pool estimates of the probability of default and of loss on default are made for the pools of unscored legacy inventories and dunning stages.

Giro/overdraft facilities for commercial customers

The "Giro/overdraft facilities" rating system is used to classify overdrafts not subject to time limits for self-employed and commercial customers in Germany. These are assigned to the IRBA asset class "Retail business, qualified, revolving loans" in accordance with section 77 (2) of the SolvV. In the process, the scoring system distinguishes between new and portfolio customers with and without limits. The giro/overdraft facilities are subject to application scoring and monthly subsequent scoring in the form of an internal behavior scoring that evaluates the risks of default individually on the basis of account management data and certain external information.

Private customers, installment loans

The rating system "Private customers, installment loans" is used to classify standardized installment loans to private persons. These are assigned to the IRBA asset class "Other retail business" in accordance with section 77 (4) of the SolvV. Decisions on applications for installment loans are tied to the outcome of the scoring model for private customers, installment loans. It is based on the use of many years' internal experience with defaults as well as on the data of external credit inquiry agencies. Installment loans are subject to application scoring; within the scope of the validation, the actual default rates are compared annually for each pool of receivables of the same rating class with the probabilities of default allocated according to the Postbank master scale, and the predictive quality of the scoring process is therefore verified. Separate pool estimates of the probability of default and of loss on default are made for the pools of unscored legacy inventories and dunning stages.

Purchased receivables, retail

The rating system "Purchased receivables, retail" is used to classify construction financing transactions purchased which are assumed within the scope of cooperation agreements with banks, building societies and insurers and which account for the lion's share of the segment of purchased receivables. For purchased receivables, Postbank makes use of the possibilities of risk determination at the pool level according to the top-down approach. To this end, the individual receivables are consolidated to form homogeneous portfolios with the same median probability of default and the same loss in the event of default. The rating system is closely related in methodological terms to the system for the classification of construction finance transactions.

5.3 Rating-based credit risk management

The further material areas of application of risk parameters estimated internally for purposes of calculating the minimum capital requirements are shown below, differentiated by management of credit risks at the individual and portfolio levels.

5.3.1 Management of individual risks

Loan approval process

The credit directives of Postbank contain detailed parameters laid down for all loan operations. Loan approvals are subject to a defined competence ranking. This governs the competencies for loan approvals depending on the loan volume and, for the asset class of central governments, institutions and corporates, also according to the credit rating of a borrower; in the retail business, this is done according to the structure of the facility.

An essential element of the loan approval process is the separation between market (sales/trading) and back office divisions and risk management in business relevant for risk purposes in accordance with the regulatory parameters (MaRisk, SolvV). A permissible exception according to banking regulatory law from the strict separation of functions is the standardized loan approval process in business not relevant for risk purposes, which Postbank defines as private residential construction finance up to €1 million, other retail credit products as well as loans for up to €750,000 in the business division Corporates, to which simplified and standardized processes are applied.

Risk/return key performance indicators

When calculating the loan losses expected in the Postbank Group, the average standard risk costs are factored into the advance calculation on an individual loan basis. This system allows all lending transactions to be evaluated during the advance calculation. The standard risk costs are priced in as a premium for the expected loss and are included in the profitability calculation that is determined in the form of return on equity (RoE) ratios. The profitability calculation aims to ensure an end-to-end assessment of customer relationships and is performed at product or portfolio level for retail customers, and at an individual level for the asset classes of central governments, institutions and corporates.

Credit monitoring and problem loan procedures

For non-standardized loans, credit risks are monitored by regular credit assessments carried out on borrowers and guarantors. The risk level and concentration of risk are capped by limiting a borrower's individual loans or total exposure. State-of-the-art computer systems are used to capture and control the limits. The controls are carried out by the operational lending units in the back office in accordance with banking regulatory requirements and, in the case of trading transactions, by Risk Controlling in addition.

In the area of individual lending to corporate or business customers and mortgage lending in excess of €500,000 per borrower or borrowing entity, the Postbank Group has implemented a credit monitoring process in accordance with banking regulatory requirements. The process enables higher-risk loans to be identified using qualitative and quantitative risk indicators, which are defined for the individual product. The use of risk indicators for early identification of an increasing risk of default enables Postbank to take measures on a timely basis to minimize risks.

In addition, at 14-day intervals Postbank uses research information (e.g. external ratings, spreads of credit default swaps or asset swaps, expected default frequencies from Moody's KMV or analysts' assessments and other corporate news) to perform creditworthiness assessments of loan commitments in the asset class of corporates, institutions, central, regional and municipal governments, as well as securitizations in order to identify negative trends in credit standing at a very early stage and to be able to take alternative action. These assessments are supported by a software program that uses a vast volume of market data for deriving the probabilities of credit default.

Whenever a corporate banking loan is identified as being subject to higher risks, the relevant borrower is placed on a monitoring or watch list. In the event of hard risk indicators, the individual loan is required to be placed on the watch list; where only soft indicators prevail, it is at the credit specialist's discretion to do so. The watch list also serves to capture and analyze any quality changes of such loans. It is constantly updated by the various loan departments and submitted to the member of the Management Board responsible for lending on a quarterly basis. The largest individual exposures, value-adjusted loans as well as loans that were subject to the approval of the Group Management Board are reported to the latter, to the Credit Risk Committee and to the Credit Committee of the Supervisory Board as part of the credit risk report.

5.3.2 Management at portfolio level

In addition to monitoring individual risks, Postbank determines the credit value at risk (CVaR) of the Group's total portfolio of receivables subject to credit risks. The CVaR is the potential negative change in the cash value of the total loan portfolio that is not exceeded within a year with a probability of 99.93 %. Within the scope of the risk-bearing capacity concept across the entire Postbank Group, the CVaR as the benchmark for expected losses from credit risk is to be underpinned by risk capital.

In contrast, the expected loss of a loan portfolio is the portfolio of receivables expected to be in default within an interval of time of one year. This is calculated as the product of the probability of default, the amount of the receivable at the time of default and the loss ratio upon such default. The expected loss does not contribute to the overall risk of Postbank but is taken into account in the margin calculation by way of the standardized risk costs.

CVaR is measured using a credit risk model that allows the consistent capture of all credit risks. CVaR is calculated on the basis of the migration behavior of borrower-specific creditworthiness and correlation effects within the portfolio, so as to quantify risks arising from an adverse concentration of counterparties in terms of their sector, size category, creditworthiness, and country. The probability of a rating change (migration) is continually updated and adjusted to reflect the changes observed in the current economic environment. In calculating CVaR, all receivables are recorded together with their future cash flows and discounted to the observation date, thus allowing the loan loss risk to be measured over a one-year observation period, as well as the effects on the present value of all changes in creditworthiness occurring outside the observation period. In the process, credit risk is measured using current internal and external credit ratings as well as internally and externally calculated assumptions relating to recovery rates.

External input parameters for the calculation of CVaR include constantly updated rating agency data, migration tables derived from the data in question, sector/product default probabilities and correlations, credit spreads (risk premiums for various rating categories/grades), as well as the volatility of these parameters in a Monte Carlo simulation. Homogeneous, granular receivables are aggregated when calculating the CVaR and are not computed at individual transaction level. These relate in particular to retail products. The updated portfolio and market data are used to compute the CVaR of the Group loan portfolio every quarter. For specific products/business divisions, the CVaR is also calculated individually.

The CVaR in the Group loan portfolio is lower than the sum of the individual CVaRs for the business divisions because of diversification effects. The utilization of the CVaR limits made available to individual profit centers by the Credit Risk Committee and that of the aggregate credit risk limit is monitored on an ongoing basis.

In addition to the CVaR calculations, the Group loan portfolio is subject to regular stress testing and sensitivity analyses across all risk classes with the aim of quantifying losses that might arise from extreme events.

5.4 Reporting

Postbank uses a variety of reporting instruments for presenting the counterparty default risk.

- The credit risk report, which is submitted quarterly to the Group Management Board and the Loan and Equity Investments Committee of the Supervisory Board, provides information on the development of the Group's current loan portfolio and on the default history at business division level. In addition to presenting loan portfolio and credit risk indicators, the report includes details of the largest exposures aggregated by individual borrowers and the largest non-performing loans, as well as the utilization of risk limits.

- The credit monitoring report is prepared quarterly at the same time as the credit risk report and contains additional detailed information at business division and product level regarding the management of credit risk by the operating units. The credit monitoring report is approved by the Credit Risk Committee.

- The credit matrix provides detailed information on credit risk at portfolio level (CVaR, rating distributions, sector distributions, concentration risks, limit utilization, target/actual portfolios), some of which is also included in the credit risk report and the credit monitoring report in aggregated form. The Credit Risk Committee also approves the credit matrix on a quarterly basis.

- To monitor the performance of the risk classification procedures at the level of individual loans (rating and scoring models), model monitoring reports are prepared by business division on a monthly to quarterly basis. Compliance with the model, i.e., its proper application, is also examined.

- At the level of individual loans, the watch lists are another instrument for reporting in respect of larger exposures that have been subjected to valuation adjustments.

6 Quantitative information on the type and extent of counterparty risks

6.1 Information on the structure of the IRBA credit portfolio

All receivables reported in this chapter refer to the credit volume of Postbank for which the latter already calculated its minimum capital requirements on the basis of the internal rating approach in 2007. Accordingly, the portfolios of subsidiaries, the predominant share of OTC derivatives and current account credits and the debt collection business in the Retail banking segment are not included.

Postbank's business strategy provides for a conservative risk policy. In an industry comparison, Postbank has a low overall risk profile in structural terms. The following tables do not show credit independent assets. The equity interests presented in detail in chapter 7.2 of this report and the securitization positions of Postbank shown in chapter 7.3 are not included in the tables of this chapter either.

6.1.1 Structure of IRBA portfolio by sectors, region and residual term to maturity

In accordance with section 327 (2) of the SolvV, assets are shown below by region, industry and residual term to maturity. The tables show the loan volume, broken down into types of receivables on the reference date for disclosure purposes. On- and off-balance sheet transactions are shown at their book values before risk mitigation and before individual valuation adjustments, and derivatives at their positive replacement values.

The following table reflects receivables broken down by industry and debt group. The industry distribution of the portfolio corresponds to the target portfolio defined in Postbank's risk strategy. The portfolio consists primarily of loans to retail customers focusing on private home loan finance as well as loans to banks. The securities portfolios in the banking/insurance industry predominantly contain debtors with first-class credit ratings.

IRBA receivables before credit risk mitigation, broken down by sectors

Types of receivables	Retail customers €m	Banks/ Insurers €m	States €m	Service providers/ Trade €m	Industry €m	Other segments €m	Total €m
Balance sheet transactions	36,734	30,506	9,901	1,231	373	4,420	83,165
Off-balance sheet transactions	3,044	2,228	0	819	616	680	7,387
Derivatives	–	289	–	–	–	–	289
Total	39,778	33,023	9,901	2,050	989	5,100	90,841

Table 9

The following table shows the loan volume differentiated by type of receivable and by key geographic business region for Postbank. The breakdown of geographical regions is effected in accordance with the credit risk strategy of Postbank. Allocation is made according to the country in which the respective borrowers are legally domiciled. The regional breakdown of the portfolio shows a concentration on Postbank's home market, Germany, in accordance with corporate strategy.

IRBA receivables before credit risk mitigation, broken down by geographical region

Types of receivables	Germany €m	Western Europe €m	Other regions €m	Total €m
Balance sheet transactions	57,587	23,426	2,152	83,165
Off-balance sheet transactions	7,314	71	2	7,387
Derivatives	12	260	17	289
Total	64,913	23,757	2.171	90,841

Table 10

The loan volume is broken down by types of receivables and contractual residual lifetime in the following table. Giro accounts, guarantees and transactions being processed are assigned to the residual maturity band "up to and including one year" on principle.

IRBA receivables before credit risk mitigation, broken down by contractual residual maturity

Types of receivables	Up to and including one year €m	More than one year, up to and including five years €m	More than five years, or unlimited €m	Total €m
Balance sheet transactions	9,730	26,318	47,117	83,165
Off-balance sheet transactions	2,002	205	5,180	7,387
Derivatives	263	9	17	289
Total	11,995	26,532	52,314	90,841

Table 11

6.1.2 Exposure for IRBA specialized lending

The table "Exposure for IRBA specialized lending" illustrates the position values of Postbank's commercial financing transactions, amounting to €6,340 million, broken down by risk weighting classes of the simple risk weighting method in accordance with section 97 of the SolvV for specialized lending. These are loans in the commercial residential housing construction, loans to property developers, operator models, transactions in the field of real estate and movables leasing as well as properties abroad. On the whole, the risk profile reflects a strong concentration of 89 % accounted for financing transactions with very good credit ratings.

Exposure for IRBA specialized lending according to the simple risk weighting method

	€m
Risk weighting class 1 (strong)	5,666
Risk weighting class 2 (good)	89
Risk weighting class 3 (satisfactory)	136
Risk weighting class 4 (weak)	163
Risk weighting class 5 (default)	286
Total	6,340

Table 12

6.1.3 IRBA exposure by type of asset class and risk category

Unlike tables 9 to 11, the following two tables reflect no book or market values as measurements of the extent of credit risk, but exposure values. The two factors differ in the sense that the so-called conversion factors are an element of the exposure values in the form of the expected utilization of the loans in the case of a possible event of default. The conversion factor in the asset classes of central governments, institutions and corporates under the IRBA foundation approach amounts to 75 % for irrevocable credit commitments, for instance. Derivatives are shown with their credit equivalent amounts in this table.

In addition to the total amount of exposure values, the table "IRBA exposure values by asset class and risk class" for central governments, institutions and corporates contains the unutilized credit commitments as well as the average risk weighting per risk and asset class weighted with the relevant exposure values for the credit rating categories "Investment Grade" and "Speculative Grade". The breakdown of the sub-portfolio into central governments, institutions and corporates is illustrated by focusing on the "Investment Grade" credit rating category.

Credit-independent assets, participations and securitizations are not shown in the following tables.

IRBA exposure values and average risk weightings by asset type and risk category in asset classes central governments, institutions and corporates

	IRBA-asset class	Investment Grade (AAA – BBB–)	Speculative Grade (BB+ – CCC–)	Total
Average risk weighting	Central governments	13 %	–	13 %
	Institutions	16 %	25 %	16 %
	Corporates	58 %	164 %	63 %
	Thereof: SMEs	43 %	82 %	52 %
	Thereof: specialized lending	64 %	189 %	70 %
	Thereof: receivables purchased	–	–	–
	Total	22 %	143 %	23 %
Total amount of exposure values in €m	Central governments	9,902	–	9,902
	Institutions	31,549	74	31,623
	Corporates	7,641	414	8,055
	Thereof: SMEs	158	48	206
	Thereof: specialized lending	5,755	299	6,054
	Thereof: receivables purchased	–	–	–
	Total	49,092	488	49,580
Thereof: open loan approvals in €m	Central governments	–	–	–
	Institutions	10	–	10
	Corporates	860	43	903
	Thereof: SMEs	83	21	104
	Thereof: specialized lending	349	6	355
	Thereof: receivables purchased	–	–	–
	Total	870	43	913

Table 13

Accordingly, the table "IRBA exposure values of retail business by asset type and risk category" contains the total amount of the exposure values for the individual EL bands.

IRBA exposure values of retail business by asset type and risk category

	IRBA asset class	0.00 – 5.00 %	5.01– 20.00 %	20.01– 50.00 %	50.01– 100 %	Total
Total amount of exposure values in €m	IRBA retail positions secured by mortgage liens	36,026	540	751	26	37,343
	Qualified revolving IRBA exposures in retail business	22	2	0	0	24
	Other IRBA exposures in retail business	3,103	184	41	59	3,387
	Total	39,151	726	792	85	40,754

Table 14

Loans under the sub-portfolio of retail business, amounting to €40,754 million, reflect the orientation of Postbank as the leading German retail bank. Another feature evident is the focus on real estate financing to private customers with a credit volume of €37,343 million. The portfolio structure of the retail business reflects a good to very good credit status in principle.

6.2 Notes on credit risk mitigation methods

6.2.1 Fundamentals of hedging and mitigating risk

The risks assumed in day-to-day business operations by a bank can be reduced by deploying credit risk mitigation methods in the form of items of collateral or by netting procedures. For the IRBA portfolios, regulatory hedging instruments comprise financial collateral, guarantees and credit derivatives as well as other items of collateral, including mortgage liens and physical collateral.

To take account of collateral in calculating the minimum capital requirements, Postbank implemented the regulatory requirements relating to collateral management within the scope of the IRBA introduction. Strict standards in accordance with the Solvency Regulation are applied to the quality (e.g. the legal effectiveness and enforceability) of collateral accepted. As in the case of an underlying transaction with a counterparty, the value of the items of collateral is not only assessed at the time of granting the loan but continually monitored throughout the term to maturity of the loan, on the basis of uniform Group standards.

The back office division is responsible for collateral management and comprises recognition, verification and regular evaluations as well as management of credit risk mitigation methods. Administration of collateral is supported with the aid of IT and handled by the exposure management systems. Value recognition of collateral is performed according to fixed monitoring frequencies, depending on the type of collateral; as a rule, this occurs annually or at shorter intervals in the case of critical exposures.

For collateral in the form of real estate liens in the field of home loan finance for private customers, in the year 2007 Postbank developed a market fluctuation concept for monitoring the value of residential property, a system that is based on statistical analyses of market indices and ad-hoc analyses in the event of exceptional changes in value and serves to verify the value of collateral annually.

Positive correlations between the counterparty risk of the borrower and the risks of value impairment of collateral are taken into account conservatively.

6.2.2 Type and extent of credit risk mitigation methods

In relation to the IRBA portfolios, regulatory hedging instruments comprise financial collateral, guarantees and credit derivatives as well as other items of collateral, including mortgage liens and physical collateral. In addition, credit risks can be mitigated by deploying netting arrangements.

Postbank takes its decisions regarding the recognition and application of a hedging instrument for credit risk mitigation purposes in the overall context of its business and credit risk strategy.

Credit risk mitigation methods that are part of synthetic securitizations are dealt with separately in chapter 7.3.

Financial collateral

Financial collateral in the retail business is directly integrated into the estimate of LGD and is therefore not reported as such. In respect of all other IRBA asset classes, financial collateral held by Postbank is not taken into account for regulatory purposes with a risk-mitigating effect.

Financial collateral that has the effect of mitigating counterparty risks, being part of the Principle I position in 2007, is not subject to disclosure.

Financial collateral representing the securities side in connection with securities repurchase/lending transactions is netted with the monetary side within the scope of this risk report and not reported separately.

Guarantees and credit derivatives

Guarantees and credit derivatives need to be irrevocable and unconditional in order to qualify as credit mitigation instruments in calculating the minimum capital requirements for counterparty risks. Only guarantees by states, other public authorities, institutions, supranational organizations and legal persons with a rating of at least A are recognized. Guarantors and collateral providers in connection with credit derivatives are subject to the same risk classification, mitigation and monitoring procedures as borrowers. In the case of guarantees and credit derivatives, the extent of the backing is calculated in accordance with section 86 (1) of the SolvV.

In the retail business, the collateralization effect of warranties is taken into account directly in estimating the LGD and therefore not reported separately.

Personal items of collateral that mitigate the exposures in the IRBA asset classes of corporates, institutions and central governments were not recognized for regulatory purposes in 2007.

Collateral in the form of real estate liens

Postbank uses collateral in the form of real estate liens as security for private home loan financing operations as a key instrument to mitigate the risks associated with lending. Collateral in the form of real estate liens is subject to a prudent evaluation that also duly takes concentrations of risk into account. The collateral is monitored at different intervals and intensities, depending on the underlying risk involved. In the event that a borrower becomes insolvent on a long-term basis, the collateral is realized.

Collateral in the form of real estate liens is taken into account in the retail business in calculating the LGD and therefore is not reported separately. In this context, the amount taken into account differs according to the type of use as a commercial or residential property and, in the case of residential buildings, on whether they are owner-occupied or used by third parties. In 2007, Postbank developed a market fluctuation concept for monitoring residential properties which is based on statistical analyses of market indices and ad-hoc analyses in the event of exceptional changes in value.

In the IRBA asset class of corporates, the value of real collateral allocated to the assets rated according to the simple risk weighting method for special lending transactions pursuant to section 97 of the SolvV amounts to €5,728 million and is included in calculating the risks weighting class. The internal rating system for special lending transactions conservatively takes account of the high level of correlation between the counterparty risk of the borrower and the value of collateral. The rating for special lending transactions is updated at regular intervals, at least annually.

Other IRBA collateral

Other IRBA items of collateral in accordance with sections 160 and 161 of the SolvV (e.g. assignment of receivables) are not taken into account by Postbank for regulatory purposes in the portfolios calculated according to IRB approaches in the year 2007.

Netting

Banks can also reduce the minimum capital requirements by means of netting arrangements. In the process, the basis for assessment is reduced either by netting individual transactions with an offsetting effect or by deploying netting arrangements. In the year 2007, netting arrangements were not taken into account in calculating the minimum capital requirements of IRBA portfolios.

Outlook

Going forward, Postbank will deploy additional credit risk mitigation methods to lower its minimum capital requirements in 2008. These include, in particular, risks mitigation methods in relation to derivative counterparty risks exposures as well as portfolios subject to the standardized risk approach.

6.3 Notes on risk provisions

6.3.1 Definitions and provisioning

All loan commitments are subject to regular review concerning the extent to which the financial assets may be partially or completely uncollectible. An extraordinary review, also of collateral, is made whenever the bank obtains information from external or internal sources, indicating a negative change of the risk assessment of the exposures or of any items of collateral.

Postbank distinguishes between the following stages of performance impairment:

Definition of delay

Classification in the category of "exposure in arrears" or "loans past due" occurs in the case of delay in payment, i.e. the debtor has exceeded an external limit communicated to him or utilized credit without prior consent. In delineation from non-performing loans, those subject to a delay in payment but not classified as non-performing are categorized as "past due" or "in arrears".

Definition of non-performing

The classification as "non-performing" is geared to risk provisions being set up by Postbank or the establishment of default of the customer or facility. The category of "non-performing" extends to include all receivables with individual valuation adjustments, lump-sum individual valuation adjustments, depreciation and provisions in relation to suretyship agreements, guarantees and irrevocable credit commitments.

Definition of default and risk provisioning

A borrower is in loan default in accordance with section 125 of the SolvV if the debtor is in delay vis-à-vis the bank with a substantial share of its total commitment under the loan granted for a period of more than 90 consecutive calendar days. A borrower may already be in default prior to this period having elapsed, namely if the bank is of the opinion that the debtor is unlikely to meet its payment obligations in total without the bank having to resort to additional measures to secure the loan, such as the realization of collateral.

In the retail business, defaults are detected automatically according to the data fields specified as relevant for each of the individual transactions. In the case of the asset classes central governments, institutions and corporates, manual criteria of default are maintained in a separate default database. The same applies to special financing transactions and receivables purchased under factoring agreements. In the case of capital market securities as well as securities and derivative exposures of investment funds, analysis and recording take place within the scope of the daily mark-to-market evaluation.

On the basis of the transactions recorded in the default database, a monthly monitoring or watch list is generated. The Risk Controlling division has the methodical responsibility for the database along with the continual further development thereof.

Postbank establishes individual valuation adjustments for non-performing or defaulted individual exposures. The extent of the individual valuation adjustment is determined by taking account of the cash value of the future cash flow, the fair value of the collateral or the market value of the loan. All loan commitments for which individual valuation adjustments have already been made as well as all exposures kept on the watch list are subjected to a revaluation on a regular basis.

Lump-sum valuation adjustments are made for homogeneous loan portfolios of installment loans and giro receivables subject to computerized limit monitoring and automated dunning processes if such valuation adjustments are required. In performing measurements, reliance is on lump-sum ratios based, in turn, on historic rates of default.

In accordance with the provisions of IFRS, portfolio valuation adjustments are made for latent risks that could not be identified as yet since a customer is still meeting its payment obligations, for instance. To calculate the portfolio valuation adjustments, internally and externally estimated probabilities of default and loss ratios on default are applied, with the period of time between the event of loss and detection thereof (LIP or loss incurrence period factors) being estimated, depending on customer groups and product types.

Uncollectible claims are written off with a direct impact on profit and loss.

Provisions are set up for suretyship agreements, guarantees and irrevocable loan approvals for which there is a risk of default.

6.3.2 Current risk exposures

All risk provisioning amounts reported in this chapter refer to the portfolios for which Postbank already calculated its minimum capital requirements on the basis of the internal rating approach in 2007. Accordingly, the tables do not reflect the risk provisioning of subsidiaries as well as for current account loans and the collection business in the private customer segment.

The following table shows the book values of all non-performing and past due loans calculated according to internal rating approaches in 2007 as well as the portfolios as at the reporting date of risk provisioning and changes thereof in the current reporting period from January to September 2007 in relation to the industries considered essential for Postbank.

Breakdown of risk provisioning by sectors

	Retail customers €m	Banks/ insurers €m	States €m	Service providers/ trade €m	Industry €m	Other segments €m	Total €m
Book values of non-performing exposures	913	–	–	66	22	379	1,380
Book values past due exposures	103	–	–	4	1	49	157
Portfolio of individual valuation adjustments	204	–	–	29	7	165	405
Portfolio of portfolio valuation adjustments	48	–	–	–	11	–	59
Portfolio of provisions	–	–	–	–	–	–	–
Expenses in period for individual valuation adjustments	66	–	–	5	–	27	98
Expenses in period for portfolio valuation adjustments	4	–	–	–	–	3	7
Expenses in period for direct depreciation	1	–	–	–	–	–	1
Expenses in period for provisions	–	–	–	–	–	–	–
Income received on receivables written off	4	–	–	–	–	–	4

Table 15

Similarly, the following overview shows a classification of risk provisioning for the IRBA portfolios by the regions of importance to Postbank. In this table, in compliance with the SolvV no changes in risk provisioning inventories are reported.

Breakdown of risk provisioning by geographical region	Germany €m	Western Europe €m	Other regions €m	Total €m
Book values of non-performing exposures	1,373	7	0	1,380
Book values of past due exposures	156	1	0	157
Portfolio of individual valuation adjustments	397	8	0	405
Portfolio of portfolio valuation adjustments	55	4	–	59
Portfolio of provisions	–	–	–	–

Table 16

As at the reporting date, no exposures are included in the IRBA portfolio for which provisions are set up.

The following list shows the changes in risk provisioning for the IRBA portfolios since the beginning of the fiscal year until the December 31, 2007 reference date:

Changes in risk provisioning for loan operations	Starting balance €m	Additions €m	Retirements €m	Depreciation charged to risk provisioning €m	Exchange rate related and other changes €m	Closing balance €m
Individual valuation adjustments	307	123	21	4	–	405
Portfolio valuation adjustments	52	8	1	–	–	59
Provisions	–	–	–	–	–	–
Total	359	131	22	4	–	464

Table 17

The "actual losses" reported in the following table are the result of the difference between additions and retirements of individual valuation adjustments as well as the difference between direct depreciation and income received on claims written off. The information refers to an observation period of half a year. The losses are reported separately for the two half-years in 2007.

Actual loan losses operations compared with previous period IRBA asset classes	Actual losses July 1 – Dec. 31, 2007 €m	Actual losses Jan. 1 – June 30, 2007 €m
Central governments	–	–
Institutions	–	–
Corporates	15	18
IRBA retail exposures secured by mortgage liens	33	24
Qualified, revolving IRBA exposures in retail business	–	–
Other IRBA retail exposures	7	1
Participations	–	–
Total	55	43

Table 18

7 Special quantitative information on the counterparty risks

7.1 Information on derivative counterparty risks

Postbank enters into derivative financial transactions within the scope of its trading activities and in controlling its assets and liabilities. Derivative financial instruments in foreign currencies are essentially concluded in the form of forward exchange transactions, currency swaps, cross currency swaps and foreign currency option transactions. Interest derivatives in particular are interest rate swaps, forward rate agreements as well as interest futures and interest option transactions; in isolated cases, forwards and futures are also concluded for fixed-income securities. Equities derivatives are concluded in particular in the form of stock options and stock/index futures. Credit derivatives are concluded on a smaller scale and were backed by own funds in 2007 in accordance with Principle I, which means that they will be subject to disclosure only as of 2008.

A precondition for entering into derivative counterparty default exposures is compliance with loan approval procedures. In the business with derivative counterparty risks, the same risk classification, limiting and monitoring processes apply as in classical loan operations (see section 5.3.1). The amounts taken into account for derivative exposures are considered together with the other credit risk-related products in calculating the exposure, in limiting the extent of risk, in calculating risk provisioning as well as the mechanisms of capital allocation.

Derivative financial instruments of the trading and banking books are taken into account on the date of trading for derivatives with positive market values. Valuation is effected at fair value. Fair values are publicly quoted market prices. In the absence of market prices, the fair value is measured by means of recognized valuation methods. The valuation result and the results realized are reported under Postbank's net trading income. With regard to recognition and valuation of derivatives, reference is made to the 2007 Annual Report, at page 112f.

The counterparty risk consists of the potential replacement or replenishment expense as additional cost or reduced income in the case of new business written on account of the default of the original contracting party and the add-on as a risk premium. In this connection, Postbank decided in favor of the regulatory market valuation method. The potential replacement or replenishment expenses as a positive market value of the derivatives (section 19 of the SolvV) without an add-on either represents market values capable of being observed (marking to market) or theoretically derived (marking to model) values.

Postbank has entered into bilateral collateral agreements with most of its key counterparties in the Financial Markets division. In the process, all positions included are netted on a daily basis and the surplus amount is settled by means of cash collateral. The procedure for the acceptance and management of collateral is performed within the scope of an independent, system-controlled process.

The positive replacement or replenishment values for derivative counterparty risk positions in relation to the IRBA portfolios totaled €289 million as at December 31, 2007.

Netting arrangements and collateral for the mitigation of counterparty risks are not taken into account with a risk-mitigating effect for regulatory purposes in 2007. Since contracts with a central counterparty are not subject to counterparty risk, the information contained in the table is confined to derivatives traded OTC and contracts on exchanges not recognized as a central counterparty for regulatory purposes.

The following table shows the derivative counterparty risks exposures as contemplated by section 19 of the SolvV, broken down into the respective basic value of the contract. In relation to the total counterparty risks of Postbank, this risk is of subordinate importance. Postbank currently has no commodity futures in its portfolio. Credit derivatives were calculated according to Principle I in fiscal 2007 and are therefore not shown in this table.

Derivate counterparty risk exposures

Types of derivatives	Positive replacement values €m
Interest contracts	129
Foreign currency contracts	141
Stock contracts	18
Credit derivatives	–
Commodity contracts	–
Other contracts	–
Total	289

Table 19

Postbank reports a total of €391 million to be taken into account as the counterparty risks of the derivative counterparty default risks exposures in the form of the credit equivalence amount in relation to IRBA portfolios. Postbank uses the market valuation method.

7.2 Notes on equities in the banking book

In addition to those equities required to be consolidated for regulatory purposes or deducted from own funds (see chapter 1), Postbank holds other participations assigned to the banking book that are subject to the minimum capital requirements within the scope of the IRB approach. The following table shows participations valued according to the simple risk weighting method. Of these, the predominant portion is accounted for by investment funds as an investment medium. All positions are held for investment purposes. Moreover, Postbank has equities in other companies for strategic reasons that are not to be consolidated for regulatory purposes.

The following table "Value approaches for IRBA equities depending on their type and marketability" only refers to equities in the banking book that are non-consolidated or deducted from own funds. In accordance with the IFRS regulations, these equities are valued at cost at the time of acquisition and at fair value within the scope of subsequent valuations; as a rule, the latter corresponds to the publicly available market price. Equities not listed for trading on an active market are valued at amortized cost. In the case of material or long-term impairments, depreciation is effected at fair value.

Of the difference reported between fair value and the book value, €67 million is accounted for by the relevant revaluation reserve set up for this portfolio.

Value approaches for IRBA equities, depending on the nature and marketability

Type of equities	Book value €m	Fair value €m
Equities in banks and other financial institutions	271	382
thereof: traded on securities markets	271	382
thereof: non-traded but belonging to the diversified equities portfolio	–	–
thereof: other equities	–	–
Equities in companies and other holdings	590	856
thereof: traded on securities markets	455	672
thereof: non-traded but belonging to the diversified equities portfolio	–	–
thereof: other equities	134	184
Total	860	1,239
Memo: Equities temporarily excluded from IRBA in accordance with section 338 (4) of SolvV	1,610	1,610

Table 20

The following table shows the profits realized in this fiscal year in relation to the total of equities defined in this chapter as well as unrealized earnings. The profit/loss realized from disposals, amounting to €411 million, includes €391 million in earnings realized on the sale of the insurance subsidiaries of Postbank. No valuation gains or losses were realized in 2007.

Profits and losses from equities

	€m
Profits/losses realized from sales and liquidations in the period under review	411
Unrealized revaluation profit/losses	93
thereof: included in Tier 1 capital	–
thereof: included in Tier 2 capital	–

Table 21

The following table shows the equities items of Postbank in the IRB approach, to which the simple risk weighting method was applied.

Exposure for IRBA equities according to the simple risk weighting method

	€m
Equities traded on securities markets (290 %)	726
Non-traded equities belonging to the diversified equities portfolio (190 %)	–
Other equities (370 %)	134
Total	860

Table 22

7.3 Notes on securitizations

The securitization of financial assets enables the underlying credit risks to be transferred to third parties. As a rule, entire pools of receivables are transferred, consisting of two or more subcategorized risk segments (tranches) with different degrees of risk. Postbank acts as investor or originator on the financial markets. It does not operate as a sponsor.

Postbank predominantly exercises its role as an investor in securitizations within the scope of credit substitute transactions with the intention of generating income and achieving portfolio diversification. In this context, Postbank invested e. g. in structured credit products (SCPs). Specifically, these are the following product types: Asset backed securities (ABSs), collateralized debt obligations (CDOs), collateralized loan obligations (CLOs), residential mortgage backed securities (RMBSs) and commercial mortgage backed securities (CMBSs). The investor positions under banking, depending on the intention and structure of the investment, are allocated to the IFRS categories of loans & receivables or available for sale and valued accordingly. (For details on IFRS accounting and valuation of SCPs, see Note (4) (g) of the 2007 consolidated annual financial statements).

Securitization exposures are rated by at least one recognized rating agency (Standard & Poor's, Moody's or FitchRatings) and generally have a rating of BBB– or better at the time of acquisition. These are predominantly super senior and granular securitization exposures. There is no internal rating model for these exposures. Postbank applies the rating-based approach according to section 257 of the SolvV to the above-mentioned securitization transactions.

Postbank acts as originator under one synthetic securitization transaction (PB Domicile 2006-1). The total volume of the securitization amounts to €2,386 million. This transaction leads to relief in terms of regulatory capital requirements on the one hand, and to a diversification of risk on the other. The rating-based approach according to section 257 of the SolvV is applied to the PB Domicile 2006-1 exposure assumed by Postbank as originator. The originator exposure is reported at the amount to be repaid. The underlying receivables are kept within the IFRS categories to which they have been assigned.

On the one hand, this transaction is secured by market-weighted collateral amounting to €174 million and, on the other, by two swaps with a total volume of €2,203 million against defaults of the reference portfolio. In supplementation of the guarantor's counterparty risk, Postbank thus retains €9 million in own risk for which backing is required (see table 25).

The following table shows the total amount of receivables securitized by the Postbank Group as originator in the form of residential properties ("PB Domicile 2006-1" transaction). No traditional securitizations took place in the Postbank Group in 2007.

Total amount of securitized receivables

Type of securitization	€m
Traditional securitizations	–
Synthetic securitizations	2,386
thereof: residential properties	2,386
thereof: commercial properties	–
thereof: other receivables	–
Total	2,386

Table 23

No new securitization transactions were conducted in the course of fiscal 2007.

The following table shows the non-performing and outstanding and securitized receivables and, in relation to these, the losses incurred under which the Postbank Group acted as originator (PB Domicile 2006-1).

Non-performing and past due securitized receivables as well as losses realized in 2007

Types of securitized receivables	Non-performing/ past due receivables €m	Losses realized €m
Residential properties	27	–
Commercial properties	–	–
Other receivables	–	–
Total	27	–

Table 24

The following table shows the exposure value of retained or acquired securitization exposures of Deutsche Postbank AG in its function as investor and originator, broken down into the type of underlying receivables in each case. In its role as investor, the securitization exposures are predominantly collateralized debt obligations (CDOs).

Total amount of retained or purchased securitization exposures

	Amounts outstanding	
Exposure values	Investor function €m	Originator function €m
Items impacting on balance sheet	4,516	9
Receivables	–	–
Measures to improve credit quality	–	–
Participations in ABS transactions	4,516	9
Other items impacting on balance sheet	–	–
Items with no impact on balance sheet	–	–
Total	4,516	9

Table 25

The following overview shows the total amount of securitized receivables and the minimum capital requirements for the various risk weighting bands. The table illustrates that Postbank invested quite predominantly in tranches with low risk weightings.

Minimum capital requirements for retained or purchased securitization exposures

Risk weighting bands	Amount receivable €m	Capital requirements €m
< 10 %	400	3
≥ 10 % and < 20 %	2,760	32
≥ 20 % and < 50 %	703	15
≥ 50 % and ≤ 100 %	596	38
> 100 % and ≤ 650 %	0	0
1250 % or capital deduction, as applicable	64	64
Total	4,525	152

Table 26

8 Management of market price risk, including interest rate risk in the banking book

8.1 Strategies, processes, structure and organization

Postbank considers market price risks an integral element of the overall risk profile of the Group. Hence the extent of market price risks is derived from a venture capital allocation that restricts the scale of risks assumed as a whole to an acceptable and desirable level for Postbank on the one hand and leads to an optimized risk mix in terms of risk/return aspects on the other.

The market risk strategy as part of the overarching Group-wide risk strategy illustrates what risk profile Postbank is willing to accept in assuming market price risks, how these are measured and controlled and what measures are taken to avoid undesirable risks. In addition, the strategy also contains statements on the fields of activity and portfolios subject to the relevant market price risks as well as on the organization and processes of risk control and risk reporting to the responsible management bodies of Postbank.

The market price risks defined within the market risk strategy comprise interest rate risks, stock price risks, foreign currency risks, spread risks as well as volatility risks. These are assumed by Postbank within the scope of its business activities in the strategic fields of corporate customers and retail banking and transferred for control to the centralized Financial Markets division or to the decentralized control units. Taking internal and external restrictions into account, the risk exposures are organized here within the scope of an overarching asset allocation intended to ensure an optimum positioning in terms of risk/return aspects. Moreover, in the course of trading Postbank assumes market price risks within the scope of the approved limits.

Risk management of market price risks, the most important risk category in the Postbank Group in terms of the allocated risk capital, was delegated by the Management Board to the Market Risk Committee, with verification being made by the Supervisory Board. Operational market price risk control is essentially performed on a centralized basis in the Financial Markets division of Deutsche Postbank AG; BHW Bausparkasse AG including its subsidiaries as well as the foreign subsidiaries in New York and Luxembourg and the London branch manage their risks independently within the framework of separately defined risk limits.

The Risk Controlling division acts as a Group-wide, independent monitoring unit. Apart from being responsible for the applied methods and models for risk identification, measurement and control, Risk Controlling is also the competent unit for the operational limit monitoring and reporting function.

Further information on the management of market price risks is contained in the 2007 Annual Report of the Postbank Group (pp. 78 ff.).

Control and measurement of market price risks

An essential task of market price risk control is the management of assets and liabilities of the balance of market price sensitive exposures assumed from specific fields of activity. In addition to assets/liabilities management in the banking book, risk is also assumed by trading as reported in the trading book. Market price risks are actively assumed to generate profits within limits derived from risk-bearing capacity aspects.

All market price risks are measured on a value-at-risk basis. Risk measurement and monitoring is performed for the bank as a whole on an end-of-day basis. For the trading portfolios, in addition intraday monitoring takes place.

To control market price risks, Postbank uses a system of limits to restrict risks derived in terms of risk-bearing capacity aspects. The total venture capital made available by the Management Board for market price risks is spread by the Market Risk Committee to the banking book portfolios and to the trading accounts.

The allocation of operational limits is made in principle for a period of ten days. The respective limits are the absolute maximum up to which risk exposures may be assumed. The limits are rendered dynamic, depending on profit or loss; losses accrued reduce the limit, with profits generated replenishing it again up to the maximum of the originally defined level.

In view of the significance of market price risks for the Postbank Group and the volatility of market fluctuations, Postbank has defined escalation mechanisms to be applied in the event of extreme market fluctuations of relevance to the Postbank Group, facilitating a timely response.

Backtesting

The methods used to calculate the VaR are reviewed for their reliability on a regular basis. In the process, the predictive accuracy of the calculated VaR is backtested by comparing it with the gains and losses arising from actual market changes, but for the same portfolio (clean backtesting). The evaluation is made according to the "traffic light" color code model published by the Bank for International Settlements (BIS). The Management Board is informed of the backtesting results at regular intervals.

Stresstesting

Stress tests comprising both sensitivity analyses and macro stress tests are performed to analyze loss potentials. These analyses quantify the effects of extraordinary events and extreme market conditions to the asset positions of the Postbank Group. The effects of the scenarios are compared with the allocated limits. The Management Board is kept regularly informed of the results of the scenario analyses. The scenario analyses performed in the year under review show that the risk-bearing capacity of the Postbank Group was secured at all times, even in extreme market situations.

8.2 Reporting

The Postbank Group uses various regular reporting instruments that provide detailed information on the market price risks assumed:

- The daily report informs the Group Management Board and the executives responsible for exposures on a daily basis, before trading begins, of the positions assumed, the utilization of limits and the economic profit/loss of the positions.
- The weekly report summarizes the essential changes on the market and in the positions and is addressed to the executives in charge of exposure management. The daily and weekly reports are regularly coordinated with the executives responsible for exposure management and supply the basis for operational control.
- The monthly report provides a comprehensive overview of the trends relating to market price risks within the period under review and is addressed to the Group Management Board. Apart from current events and key risk ratios, this report also contains the results of the stress test and backtesting analyses performed on a regular basis. In addition, information is provided separately by portfolios and currencies on the interest rate risk in the banking book amid a defined interest shock and additional interest scenarios.
- The monthly MRK reporting provides key risk ratios (VaR, interest sensitivities, stress test results) in aggregated form for the Market Risk Committee as well as cash value and/or periodic results, delineated by management units and impact on profit and loss.
- The Risk Report to the Supervisory Board is a quarterly summary of key risk ratios and, in addition, shows the results of sensitivity and stress test analyses since 2007.

8.3 Fundamentals of hedging and mitigating risk

As explained in chapter 8.1, there are highly developed processes and methods in place in the Postbank Group for controlling market price risks and monitoring compliance with the defined limits. In addition, Risk Management is supported by the stress and backtesting processes to review the risk measurement method deployed.

In addition to these processes to restrict the market price risks assumed, market price risks are also hedged by means of fair value hedges if active risk assumption is not desired. Both individual transactions and homogeneous sub-portfolios are hedged. In the case of interest-bearing positions in securities and long-term receivables, interest swaps are predominantly used as hedging instruments, while cross-currency swaps and structured swaps are also used in respect of issues. Control of stock portfolios is primarily performed by means of derivatives in the nature of options. The effectiveness test for all fair value hedges is performed prospectively by means of a sensitivity analysis of the underlying and hedging transaction, supplemented by a homogeneity test of the sub-portfolios. The actual changes in the market value of underlying and hedging transactions are compared regularly and retrogressively for each hedging relationship and partly supplemented by simulation models.

8.4 Specific information on the interest rate risk in the banking book

In accordance with section 24 (1) No. 14 of the KWG, banks are obliged to notify the supervisory authorities ("breakout bank"), if a sudden, unexpected change in interest rates causes the cash value in the banking book to decline by more than 20 % of regulatory capital requirements. The regulatory interest rate change to be applied amounts to +130 basis points or –190 basis points, respectively:

Interest rate risk in the banking book

	Interest shock (+130 BP/–190 BP)	
Currency	Value change +130 BP €m	Value change –190 BP €m
EUR	–673	1.084
USD	–140	228
JPY	–6	10
GBP	–8	12
CHF	–1	1
Other	–1	1

Table 27

In the Postbank Group, the change in value determined on a daily basis always remained below the reportable threshold of 20 % in fiscal 2007.

In accordance with the regulatory parameters, when calculating the change in cash value in the banking book, all interest-bearing balance sheet items and interest-sensitive off-balance sheet items are taken into account in accordance with internal control methods and models.

What is of special importance for the Postbank Group in this connection are the deposit-taking operations of Deutsche Postbank AG at variable interest rates, to which the model of sliding averages is applied, the items of the cooperative building society of BHW Bausparkasse AG as well as using implicit options to track customer behavior in the case of other customer transactions. Special tracking regulations and deposit base definitions are used as the basis for a modern risk management concept.

Interest rate risks are assumed in all forms described in the "Principles for the Management and Supervision of Interest Rate Risk" according to Basel II. These are the risk of refinancing, the structural, the underlying and the option risk. Refinancing and structural risks are assumed in cash flow mismatches that respond to interest rate level and yield curve changes. Underlying risks are assumed between market segments, e. g. *Pfandbriefe* (mortgage bonds) against the swap market, but also directly between individual customers. Option risks also exist, both in customer business and in financial instruments.

The regulatory defined interest shock on which the results reported in the table are based is to be considered an extreme scenario. The results of regular reviews of interest rate risks are taken into account in fixing the limits. The market price risk determined by means of the VaR for the banking book in relation to a confidence level of 99 % and a 10-day holding period amounted to €209 million as at December 31, 2007.

9 Management of liquidity risks

9.1 Strategies, processes, structure and organization

In managing liquidity risks, the Postbank Group distinguishes between two types of risk, namely the insolvency risk and the liquidity maturity transformation risk (LMT risk). The insolvency risk is the risk of being unable to meet current or future payment obligations in the full amount due or as they fall due. The liquidity maturity transformation risk describes the risk that may arise on account of a change in the Bank's own refinancing curve (spread risk) from a mismatch of the liquidity-related structure of maturities.

The Deutsche Postbank Group considers the liquidity risks an integral element of the risk strategy of the Bank as a whole. In the liquidity risk strategy, the framework for control, i.e. management and monitoring of liquidity risks, is defined on a binding basis. The Group Management Board ensures that the rules formulated are implemented and applied throughout the Group. Implementation of the liquidity risk strategy is effected on the one hand by regular reviews of liquidity and taking measures to preserve it, and on the other by the defined decision-making persons contracting targeted liquidity exposures within the framework of the limits laid down from time to time.

Unlike the other types of risk, the insolvency risk at Postbank is deliberately not underpinned with venture capital since the risk cover amount is not suitable for covering the risk of insolvency. In the event of a shortage of liquidity, the only possibility of obtaining additional liquidity (liquidity reserve in the form of readily marketable securities) is decisive for the ability of a bank to take action.

Management and measurement of liquidity risks

In principle, liquidity control is effected on a centralized basis in the Financial Markets division of Deutsche Postbank AG, with BHW Bank AG, die BHW Bausparkasse AG, the foreign subsidiaries in New York and Luxembourg and the London branch controlling their risks independently within the scope of uniform parameters laid down throughout the Group.

The task of Liquidity Management is to ensure Postbank's ability to pay at all times – not only in normal circumstances but also in stress situations. To this end, the liquidity positions are subjected to regular stress tests. These simulation models take account of external changes in various market factors and structural changes within the refinancing portfolios. An appropriate portion of free securities eligible as collateral with central banks serves as a liquidity reserve as a precaution in the event of such scenarios possibly occurring.

As part of its responsibility as a Group-wide, independent monitoring unit, the Risk Controlling division defines the applied methods and models for risk identification, measurement and control and assumes the operational monitoring and reporting function.

The liquidity status of the Postbank Group is assessed each business day on the basis of funding matrices and cash flow forecasts and risk management is performed on this basis. The control measures are focused above all on optimizing the liquidity costs and further diversifying the sources of funding. To compensate for unexpected liquidity outflows, a portfolio of securities with first-class credit rating and fungibility is maintained, which can be sold at short notice or pledged with central banks in order to obtain short-term liquidity.

In accordance with section 12 of the Liquidity Regulation (transitional provisions), in 2007 Postbank continued to apply the Liquidity Principle (II) pursuant to section 11 of the KWG as a regulatory assessment criterion (ratio of coverage of funds available to collectible payment obligations). The requirements were met at all times.

9.2 Reporting

The Postbank Group uses various regular reporting instances for the purpose of reporting liquidity risks:

- The members of the Market Risk Committee and the units relevant for liquidity management purposes are informed on a daily basis of the liquidity status at Group level.
- The Group Management Board receives monthly overviews of the liquidity status, including the established stress tests at Group level.
- Monthly information on liquidity figures in accordance with the Liquidity Regulation is reported to the Group Management Board within the scope of the Management Board Information System (MIS).

9.3 Fundamentals of hedging and mitigating risk

Maintaining liquidity at all times is the central requirement for conducting banking operations and thus represents an ultimate requirement as regards liquidity risk management and, therefore, a strict ancillary condition in the target system of the Deutsche Postbank Group.

Thanks to its corporate policy orientation as a retail bank, Postbank has a broad refinancing basis in business with customers and therefore is only dependent on the money and capital market to a limited degree. Liquidity risks are only assumed within the framework of approved limits. In the event of an unexpected liquidity outflow, an extensive portfolio of free securities eligible as collateral with the ECB is maintained, which can be used to obtain liquidity at short notice. In order to extend its funding basis, in 2007 a debt issuance program was launched, providing among other things for regular issuing of Pfandbriefe, or mortgage bonds (Jumbo, Private Placements) starting in the 1st quarter of 2008. The program also allows for other forms of issues. All products can be issued in marketable currencies and structuring variants. Moreover, in 2007 Postbank was awarded a Pfandbrief license for public and mortgage bonds.

The Treasury units are responsible for ensuring liquidity at all times. In the event of a liquidity contingency, the Liquidity Emergency Crisis Task Force is clearly responsible and authorized to issue instructions to all portfolio executives of Postbank as well as to the portfolio executives at the subsidiaries and foreign branches.

10 Management of operational risks

10.1 Strategies, processes, structure and organization

Postbank defines operational risk as the danger of losses due to the inappropriateness or failure of internal processes and systems, people or as a result of external events. The definition also extends to include legal risks. Operational risks can occur in current business operations within the scope of all processes.

Strategic parameters for management of operational risks are part of the overall strategy. The objective is to use suitable measures to confine operational risks to a minimum. The partial strategy comprises Group-wide fundamental rules, e. g. for active security such as transparency of processes, unambiguous rules regarding competencies and appropriate security directives, but also for passive security in the form of adequate financial cover.

The uniform standards in the Group can be supplemented at the level of business divisions. In the past, this was implemented for the field of Transaction Banking. For the processes in connection with payments, beyond the usual emergency planning additional principles were defined for the purposes of business continuity management and disaster backups.

The Management Board of Postbank is responsible for managing, monitoring and controlling operational risk. The Committee appointed by the Management Board for management of operational risks (ORK) is responsible for defining overarching principles applicable throughout the Group. To secure uniform procedures in the Group as a whole, activities are coordinated by the central Risk Controlling division of Deutsche Postbank AG. This organizational unit is also responsible for regular reviews of the appropriateness of the methods and procedures in use for the purpose of controlling operational risks.

In supplementation of centralized Controlling and to support the respective executives in risk prevention, a two-tiered organizational structure is in place per division and subsidiary, with decentralized Operational Risk Managers.

The operational risks are integrated into the risk-bearing capacity concept of the Postbank Group. The amount calculated to be taken into account for operational risks is included in the limiting process as a sum to be deducted from the available risk cover amount. A sub-allocation of venture capital to the individual profit centers is not made at present.

Operational Risk Management

Management of operational risk is effected on a decentralized basis in the respective units of the Group. To analyze operational risks, Postbank essentially relies on recording risk indicators, performing structured self-assessments and collecting cases of losses being incurred.

Postbank applies the standardized approach for the purpose of determining the minimum capital requirements for operational risks.

Compliance with the requirements of the Solvency Regulation was confirmed as part of an audit conducted by the Internal Audit division and reported to the banking regulators. By implementing the requirements for the standardized approach, at the same time the foundations were laid for a change at a later date to an advanced measurement approach (AMA). This also includes the use of external data obtained from the DakOR data consortium.

10.2 Reporting

The management levels of the Postbank Group receive reports on operational risks and losses on a regular basis.

- The members of the Operational Risk Committee receive monthly information on cases of loss and selected indicators that have exceeded the defined tolerance threshold.
- The Group Management Board receives a current compilation of loss cases on a monthly basis as part of the Risk Report from the Risk Controlling Market/Operational Risks department.
- In addition, the Operational Risk Committee is informed half-yearly of the results of the self-assessment.
- At a decentralized level, the persons responsible at the various levels receive reports geared to the specific information needs.

In the case of serious cases of loss beyond a defined amount of loss, the members of the Operational Risk Committee are informed without delay within the scope of the ad-hoc reporting.

10.3 Fundamentals of hedging and mitigating risk

With a classified organization structure, clear rules relating to competencies and work instructions for the sub-processes, Postbank has laid the foundations for the reduction of operational risks. Employees receive regular training and are informed about novelties in processes and work instructions on a timely basis.

All transactions with material risk content may only be entered into subject to simultaneous double checks. The functionality and security of IT systems are continually monitored.

Insurance policies taken out against losses arising from operational risk are reviewed at regular intervals by a separate organization unit.

List of tables

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