2 MANAGEMENT REPORT

MANAGEMENT REPORT

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MANAGEMENT REPORT

Consolidated Management Report for the Company and the Group

The Group management report was included in the PATRIZIA Immobilien AG management report in accordance with Article 315 (3) of the German Commercial Code (HGB) in conjunction with Article 298 (2) of the HGB because the position of PATRIZIA Immobilien AG as a management and financial holding company is mainly shaped by the position of the Group.

The integrated management report contains all details of the net assets, financial and earnings information of the Company and the Group as well as other details required according to German commercial law and the supplementary provisions of DRS 20. All monetary amounts are stated in euros.

1 FUNDAMENTAL PRINCIPLES RELATING TO THE GROUP

1.1 Business model

Present in
15
European markets

PATRIZIA Immobilien AG is one of Europe's leading independent real estate investment companies. Around 700 employees serve our clients in 15 European real estate markets. In addition, PATRIZIA maintains branches in Melbourne and New York. PATRIZIA offers a comprehensive scope of services from asset to portfolio management, the management of acquisitions and disposals for virtually all property classes as well as alternative investments and development. This enables us to fully and precisely meet the desires and requirements of clients. These clients include private and institutional investors focused on the long term such as insurance companies, pension funds, sovereign wealth funds and savings banks from all over Europe and Asia. PATRIZIA offers its client's products tailored to meet individual return, diversification and risk requirements.

PATRIZIA's business model focuses on making investments across Europe for institutional and private investors and on using its own equity to invest in attractive real estate properties and real estate portfolios on a case by case basis. In doing so, PATRIZIA generates fees and investment income which can be classified in three categories:

Business for third parties
Business for third parties involves the placement and management of investment funds by the Group's own investment management companies (MCs) on behalf of private and institutional investors. The funds are structured without an equity contribution by PATRIZIA. PATRIZIA generates stable, recurring income through the fees from the asset management, from the management of properties and from acquisitions and disposals. If PATRIZIA exceeds the individually specified return objectives, the company may also charge a performance fee. Furthermore, the business for third parties includes additional mandates where PATRIZIA offers separate individual services from its service portfolio.

Co-investments

Through co-investments, PATRIZIA also uses its own equity to participate in transactions together with its clients. In addition to the commitment to the client and to the transaction, these investments also generate management fees and income from participations for PATRIZIA. In this way, our shareholders are able to participate in the performance of an attractive and diversified pan-European real estate portfolio.

Principal investments

In general, PATRIZIA is active as an investment manager for institutional investors and private clients and therefore seeks to avoid any conflicts of interest with its own investments. Principal investments, i.e. transactions on PATRIZIA's own account, are therefore either made in the form of interim financing for closed-end mutual funds or as an early-stage investment with the purpose of including it in an institutional fund at a later point in time. In addition, there is a remaining portion of single unit sale assets.

As at 31 December 2016, PATRIZIA managed real estate assets of around EUR 18.6bn (31 December 2015: EUR 16.6bn). The volume of assets managed exclusively on behalf of third parties totalled EUR 11.6bn (31 December 2015: EUR 8.8bn); the portfolio of co-investments in which PATRIZIA participates with up to 10% of its own equity increased to EUR 6.9bn (31 December 2015: EUR 6.7bn). In the past year, principal investments significantly decreased by around EUR 0.1bn (31 December 2015: EUR 1.1bn).

EUR bn
2.0
assets under management growth

In accordance with its business model, PATRIZIA Immobilien AG generates two primary streams of income that form the basis of its operating income:

	Revenues from management services	Revenues from management services	Earnings on capital employed	Performance fees
Fees from third parties	✓	✓	x	✓
Revenues from own Investments	x	x	✓	x

1.2 Group strategy

PATRIZIA's aim is to become a leader in all asset classes, not just in Germany but across Europe. As an independent real estate investor, PATRIZIA acts on behalf of both large institutional investors from all over the world as well as German retail investors and offers added value across all segments of the property. A key element of PATRIZIA's strategy involves further expansion of its position. The goal is to continually increase assets under management and recurring income each year and thereby achieve sustainable growth in operating income.

Expansion of the European platform

In previous years, PATRIZIA has already opened offices in all strong and relevant European countries, and developed teams to ensure a presence in these markets. A key element of PATRIZIA's strategy involves further expansion of existing country activities and the entry into new European markets. As a general principle, PATRIZIA only expands into new markets or market segments where established companies can be seamlessly integrated into the PATRIZIA Group and / or where it is possible to recruit highly qualified experts with a suitable track record. We continue to monitor the market to identify such additions in a timely manner.

Extension of the product portfolio

The product portfolio is being expanded in a targeted manner and now incorporates almost all asset classes: from residential, office and retail to logistics, hotels and home care properties. PATRIZIA's Europe-wide platform provides optimal conditions for offering investments which match the legal and supervisory framework required by individual investors based on national regulations. PATRIZIA's skill set in this field and broad presence in Europe have enabled it to establish itself as an internationally successful brand among investors.

Broadening of the domestic and international investor base

EUR m
254
Volume of funds for retail investors, launched in 2016

The international investor base has undergone and continues to undergo further expansion. This included the establishment of offices in Australia and the U.S. and expanding the European Client Relationship Team specifically for Southern Europe and Scandinavia. In Germany, the strong domestic investor base is also undergoing a continued expansion. The target is to establish relations as stable as those to our existing, predominately German, clients. This includes particularly private clients for which we were able to issue funds worth EUR 254m in the period under review.

The goal is thereby to establish stable long-term customer relationships as with PATRIZIA's existing, predominantly German clients. As well as being interested in new products, these investors often require specialist consultancy services in terms of reinvesting proceeds from the disposal of existing investments.

1.3 Competitive strengths

Direct access to a broad investor base

Since
2016
PATRIZIA offers retail funds

Direct access to a broad investor base is one of PATRIZIA's strengths. This is founded on the trust of clients, which include more than 200 domestic and international institutional investors, who wish to consolidate and expand the business relationship developed over 30 years. These clients regularly and repeatedly invest in PATRIZIA. As of 2016, PATRIZIA has also been offering closed-end funds to retail investors. The demand displayed by this new investor group significantly exceeded our expectations. In this segment, we were able to invest EUR 254m for five different funds in the first year. In total, investors entrusted PATRIZIA with EUR 2.2bn of new equity in the year just ended.

Pan-European network

Based on deep trust and a professional, easily scalable platform, PATRIZIA's scope of activities and our network now encompasses 15 European markets. PATRIZIA is represented in these markets with long-standing, local expertise. Thanks to our regional and sub-regional network, we are able to identify and structure attractive investment opportunities in virtually all asset classes and across varying risk profiles. This network also gives PATRIZIA direct access to the latest market developments and is able to follow almost every noteworthy transaction. The Harald acquisition is one example – an exchange-listed portfolio primarily comprising German residential assets which PATRIZIA acquired in 2015, which was sold for a significant profit in the reporting period.

Offering the entire value chain

It is not just international investors who are impressed by PATRIZIA's wide range of products and services, but German investors too: investors are offered a "comprehensive, care-free package" containing all services and the entire value chain of their investment. It goes without saying that individual components can also be selected from this package.

Successful "track record" attracts further transactions

Successful transactions are commonplace at PATRIZIA. Last year alone we managed acquisitions and disposals totalling EUR 5.1bn, EUR 1.5bn of which was outside of Germany. In addition, we were able to contractually agree on transactions with a value of more than EUR 2.1bn, the majority of which will be realised in 2017. Successful wealth creation within a portfolio is one of PATRIZIA's core competences and that is reflected in the returns achieved for our clients. However, the prudent recognition of opportunities in all asset classes throughout Europe and the prompt and discreet execution of deals are also what clients and business partners value in PATRIZIA.

PATRIZIA has the DNA of an investor

PATRIZIA has the DNA of an investor and we regularly invest alongside institutional clients. PATRIZIA has from the outset made investing our own equity a key element of our business model. The company invests equity on a collaborative basis with clients in co-investments. Our long-standing experience and extensive expertise as an investor are demanded and appreciated by clients.

Reputation creates trust

Among investors and business partners in Europe, the name PATRIZIA stands for a trusting and reliable partnership and successful business. This reputation has developed through sustainable and prudent business acumen. The brand and the trust associated with it are indispensable for securing new clients and expanding existing business relationships. This is why we attach such great importance to managing the PATRIZIA brand and re-earning the trust of our investors with each new transaction.

1.4 Group control and performance indicators

1.4.1 Corporate management based on segments

PATRIZIA's corporate management is performed in the segments Management Services and Investments. The Management **Services segment** includes service commission (fee) income from asset management. The **Investments segment** primarily includes the income earned on capital funds (equity). Further details on segment reporting are available under item 7 of the Notes to the Consolidated Financial Statements.

1.4.2 Corporate management based on financial performance indicators

The following financial performance indicators are used for corporate management at PATRIZIA:

Financial performance indicators	Description
Assets under management (real estate assets)	The growth of the Group is measured by the assets under management.
Operating income	The operating income before tax is the Group's most important key performance indicator. It is calculated from EBT in accordance with IFRS, adjusted by non-cash effects from the valuation of investment properties, unrealised currency effects, the amortisation of fund management contracts and reorganisation expenses. It includes realised valuation gains from the sale of real estate assets held as investment property as well as realised currency effects.

Furthermore, the following framework parameters support Group control:

Additional framework parameters	Description
Management service fee	PATRIZIA receives recurring service fees for managing real estate assets.
Transaction fees	PATRIZIA receives a fee for acquisitions or disposals based on the transaction volumes.
Performance-based fees	PATRIZIA receives performance-based fees when defined target returns for individual investments are exceeded.
Transaction volume	The transaction volume is the total of all acquisitions and disposals for which PATRIZIA receives a fee which is in line with the market.
Investment income	Return on invested own equity
Raised equity	The equity for various investments is raised globally from institutional and retail investors.

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The development of these indicators is explained in detail in item 2.2.

1.4.3 Corporate management based on financial performance indicators

PATRIZIA does not directly apply any non-financial performance indicators for its direct corporate management.

1.5 Employees

Employee structure

38
trainees were employed in 2016

As at 31 December 2016, the European real estate investment company employed a total of 794 full-time employees (2015: 823 employees, –3.5%). This includes 38 trainees and students of the Cooperative State University Stuttgart (Duale Hochschule) studying real estate economics, plus 63 part-time employees.

On 3 January 2017, a purchase agreement for the property management was concluded with Deutsche Immobilien Management (DIM). As a result of the transaction, 115 employees were transferred to DIM and PATRIZIA's number of employees decreased accordingly.

A total of 125 employees work in international subsidiaries across Europe (2015: 99 employees) in Denmark, Finland, France, the United Kingdom, Ireland, Luxembourg, the Netherlands and Spain. The increase in the number of employees is mainly a result of the expansion of our international presence. In terms of full-time equivalents, the European headcount at the end of the year was 770 employees (2015: 800 employees, –3.8%).

PERSONALSTAND EUROPAWEIT

794
employees across Europe

Corporate culture

PATRIZIA'S corporate culture is based on our management principles and rules for collaboration, which are closely interconnected. They are divided into five dimensions: performance, trust, respect, responsibility and support. All dimensions are considered to have equal value and employees are encouraged to share in them and set an example of them in their own conduct. The essential nature of PATRIZIA's corporate culture makes it possible to better achieve these goals.

Diversity in the company

As a company with business activities throughout Europe, there is a constantly increasing level of cultural diversity in the Group. PATRIZIA now has local management teams in nine countries and is active as an investor and service provider on the real estate market in 15 countries. At year-end, PATRIZIA employed people from 29 nations.

The proportion of male to female full-time employees is 53% to 47%, while the proportion of male to female part-time employees is 2% to 98% (2015: 8% to 92%). With an overall proportion of 51%, the majority of employees (excluding trainees) of the PATRIZIA Group are female. In the year under review, female employees made up 5% of the senior management team (Managing Board and first-tier managers) across Europe (2015: 5%), while 25% of all managers in the Group were female (2015: 23%).

Percent
51
proportion of female employees

3
internal trainer

Continuing education

Continuing education for PATRIZIA employees has always been, and remains, a central objective. During the year the PATRIZIA Academy offered 24 seminars including real estate skills, leadership skills, personal and social skills to international skills. Of a total of 12 instructors, eleven seminar leaders were drawn from within the company. Over the course of year under review, PATRIZIA invested around EUR 271,000 in advanced training and continuous education for its employees. This equates to EUR 365 per employee, based on the average number of employees during the year. Each month, a one-hour session on a selected specialist topic is held under the title "PATRIZIA Knowledge". These sessions focus on establishing a dialogue between colleagues and aim to promote understanding among each other and across departments.

Employer attractiveness

In order to ensure that we can enjoy long-term success across Europe as a real estate investment company, we need to make sure that we remain an attractive, exemplary employer in the competition for the best talent. PATRIZIA focuses on a mix of competitive remuneration, voluntary social benefits offered by the company, a friendly and constructive corporate culture and individually tailored development opportunities.

1.6 Sustainability

PATRIZIA Immobilien AG supports various organisations in the real estate industry that are committed to promoting sustainability and environmentally responsible behaviour. Through our membership of associations related to international real estate companies, we contribute to discussions on sustainability in the real estate sector such as the definition of reporting standards for residential properties.

Sustainability strategy

PATRIZIA's sustainability strategy significantly influences the approach with respect to the sustainable development of the company. Based on international reporting standards, the sustainability strategy comprises 11 core topics based on five strategic fields of action taking into account the importance of various stakeholders. The strategic fields of action focus on employee development, social commitment, PATRIZIA's products, increasing the value of the company and raising transparency. The sustainability strategy aims to integrate social and environmental issues along the real estate value chain into the stakeholder dialogue in order to be prepared for future challenges. An essential part of our expansion in Europe will encompass meeting international requirements and being prepared for future challenges.

www.kinderhausstiftung.de
www.facebook.com/patriziakinderhausstiftung

PATRIZIA KinderHaus Foundation

PATRIZIA also exercises sustainability through its support of the PATRIZIA KinderHaus Foundation, which was established by CEO Wolfgang Egger in 1999, the aim of which is to create living spaces for children and young people in need all over the world by building PATRIZIA children's homes ("KinderHaus"). The main focus is always on constructing new buildings, extending buildings or converting buildings which are precisely tailored to the respective requirements. Various children's homes have been set up in Europe, Africa, Asia and Latin America in the more than 15 years of the foundation's existence. All costs incurred are covered by PATRIZIA and additional sponsors, meaning that 100% of every euro donated is directly spent on the projects.

Percent
100
of every Euro donated is directly spend on projects

2 ECONOMIC REPORT

2.1 Economic environment

Markets in general: Economic recovery continued in Europe in 2016, but is only proceeding very slowly. Growth in 2016 was primarily the result of increasing employment and the ECB's low interest rate policy. The steady economic recovery and a relatively weak euro led to a positive development in consumer spending and exports. The renewed rise in oil prices will likely contribute to an increase in inflation to above 1% in 2017.

Source: Reuters, EZB

Real estate markets: Real estate continues to create great demand from both institutional and retail investors. Investment activities were driven by low returns on alternative investments and the availability and low cost of financing. The interest for properties in primary locations as well as secondary locations remains high. However, focus increasingly shifts to secondary locations due to the lack of availability in primary locations. Favourable economic development resulted in a continued positive momentum for office rental markets and also for retail markets. European residential real estate markets continue to flourish in line with general economic recovery. The largest price increases can be observed in economically successful urban centres and also increasingly in their wider catchment areas. Generally, it can be assumed that the risk of a respective bubble forming currently appears limited since the upturn in regional residential property markets has not yet resulted in a rapid expansion of lending.

Source: RCA, Reuters, brokers

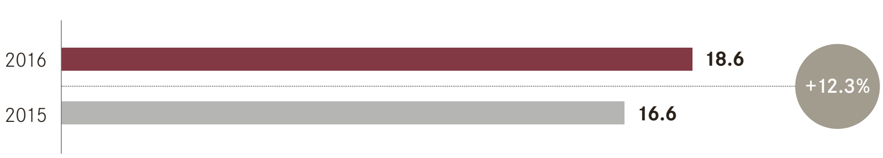
2.2 Operational performance

Key performance indicators

As at 31 December 2016, PATRIZIA was managing real estate assets worth EUR 18.6bn compared with EUR 16.6bn at the previous year's balance sheet date. Of this, EUR 12.5bn was accounted for by Germany and EUR 6.2bn by other countries. Overall, assets under management grew by EUR 2.0bn, or 12.3% during the reporting period. The target growth of around EUR 2.0bn per year was subsequently achieved. PATRIZIA also expects net annual growth of around EUR 2.0bn in assets under management in 2017.

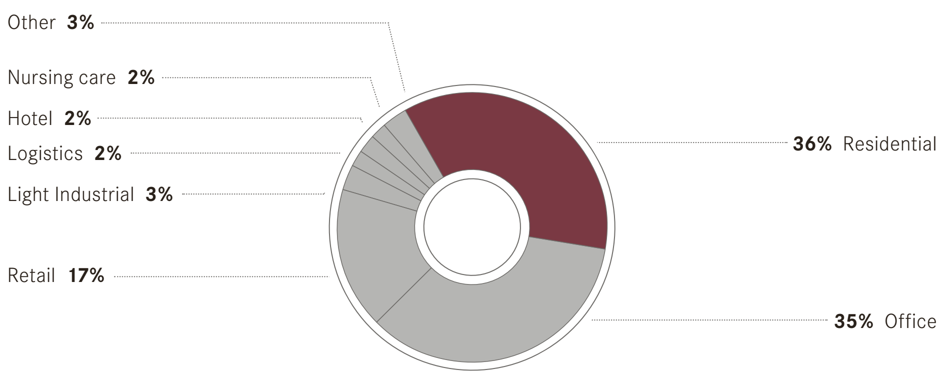
EUR bn
18.6
assets under management as of end 2016

ASSETS UNDER MANAGEMENT (IN EUR BN)

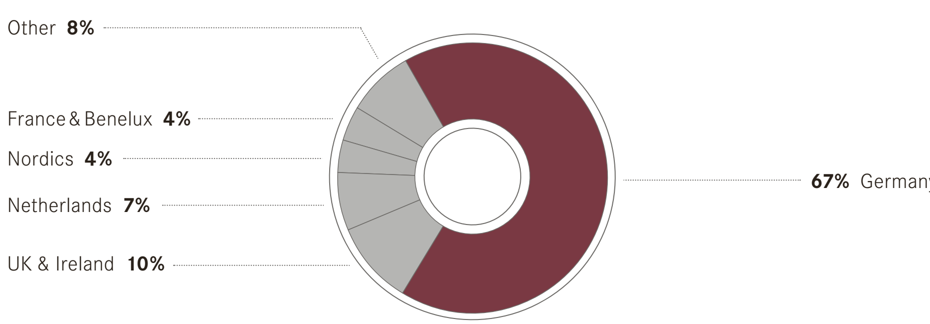


Consolidated Financial Statements

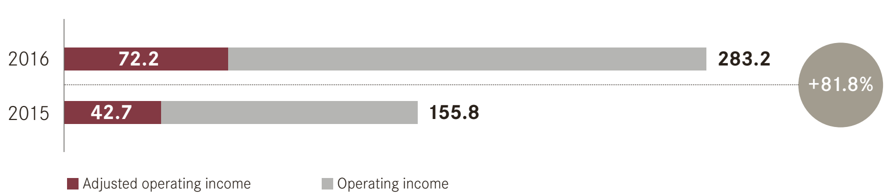
MANAGING ALL MAJOR SEGMENTS (IN %)



GEOGRAPHICAL BREAKDOWN OF ASSETS (IN %)



OPERATING INCOME (IN EUR M)



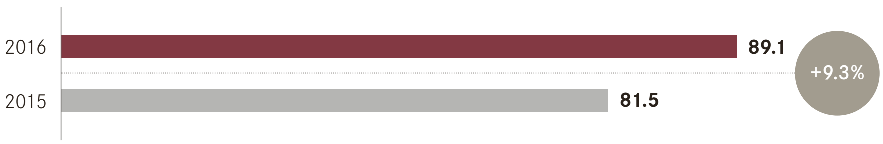
EUR m
283.2
increased guidance was significantly exceeded

For the 2016 fiscal year, operating income significantly increased to EUR 283.2m (2015: EUR 155.8m, +81.8%). This meant the increased forecast of at least EUR 265m which had been increased in November 2015 was significantly exceeded once more. Operating income adjusted for the contribution from the Harald transaction and the performance-related fees from the sale of SÜDEWO was EUR 72.2m in 2016; this is an increase of 69.3% compared to the previous year's result of EUR 42.7m.

Operating income before tax is the Group's most important key performance indicator. It is calculated from EBT in accordance with IFRS, adjusted by non-cash effects from the valuation of investment properties, unrealised currency exposure, the amortisation of fund management contracts and re-organisation expenses. It includes realised valuation gains from the sale of real estate assets held as investment property as well as realised currency effects.

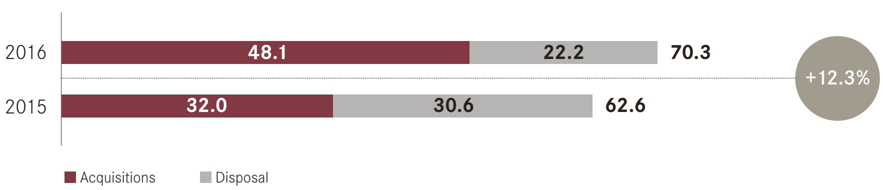
Development of the framework parameters which support corporate management:

MANAGEMENT SERVICE FEES (IN EUR M)



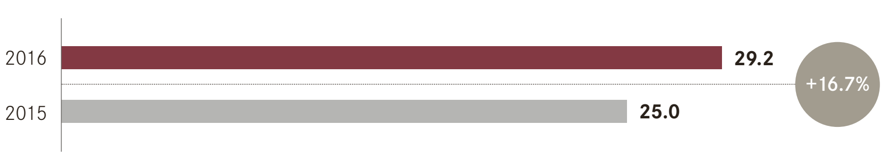
All services provided by PATRIZIA are compensated through management service fees. Management service fees include the compensation for real estate services such as asset and portfolio management and are highly recurring. In 2016, EUR 89.1m of management service fees were generated. Compared to the previous year, this represents an increase of 9.3% (2015: EUR 81.5m).

TRANSACTION FEES (IN EUR M)



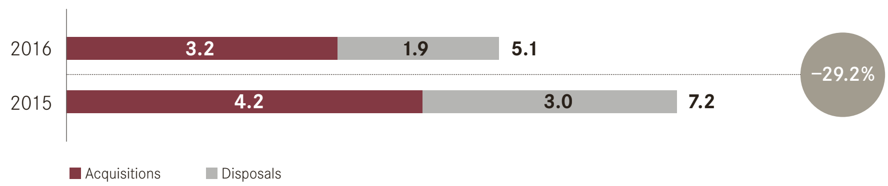
For the acquisition and disposal of assets, PATRIZIA charges a fee that is in line with market conditions. For the year ended, PATRIZIA generated EUR 70.3m in transaction fees, an increase of 19.8% compared to EUR 58.7m in 2015. This increased despite lower transaction volumes and is due to two non-fee-bearing transactions for our own account amounting to EUR 2.5bn in 2015 (sale of SÜDEWO and the acquisition of the Harald portfolio).

PERFORMANCE FEES (IN EUR M)



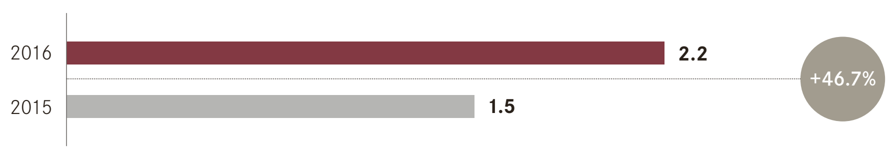
If defined target returns for investments are achieved or exceeded, PATRIZIA receives a corresponding performance fee. For the year ended, PATRIZIA generated EUR 29.2m in performance fees, an increase of 16.7% compared to EUR 25.0m in 2015. For 2015, the performance fee was adjusted by the effect of the SÜDEWO sale.

TRANSACTION VOLUME (IN EUR BN)



The transaction volume comprises realised real estate acquisitions and disposals. In 2016, acquisitions totalled EUR 3.2bn and disposals EUR 1.9bn. Taking into account the EUR 2.5bn non fee-bearing transactions on our own account (disposal of SÜDEWO and the acquisition of the Harald portfolio) in the fiscal year 2015, the transaction volume remained stable.

RAISED EQUITY (IN EUR BN)



EUR bn
2.2
equity raised with domestic and international investors

In 2016, equity of EUR 2.2bn was raised for PATRIZIA's numerous national and international investments. This represents a 46.7% increase on the previous year's figure of EUR 1.5bn.

2.2.1 Third parties

Business for third parties involves the placement and management of special funds by four different regulated Group investment management companies on behalf of private and institutional investors. PATRIZIA generates stable, recurring income from the management of the assets. Our so-called third-party business does not involve any equity investment by PATRIZIA. Third-party business contributed EUR 11.6bn to the assets under management as at 31 December 2016.

PATRIZIA's investment management companies

The funds fulfil the role of holding assets, and the initial holding period planned for these assets is between seven and ten years. Various PATRIZIA business units act as service provider for the funds of the three German investment management companies and the Luxembourg-regulated platform (AIFM), thereby generating fee revenues.

PATRIZIA WohnInvest KVG mbH primarily invests in residential properties and **PATRIZIA GewerbeInvest KVG mbH** in commercial real estate. Both companies operate with a focus on Europe and launch specialised real estate funds for institutional investors.

In contrast, **PATRIZIA GrundInvest KVG mbH** is the designated entity focusing on the private client business. In 2016, it launched five closed-end mutual funds in several countries with a total investment volume of around EUR 250m. The newly launched fund series "Europa Wohnen" invested in the cities Copenhagen (Denmark) and Den Haag (the Netherlands). Furthermore, it invested in a mixed use asset in Stuttgart as well as on the campus of RWTH Aachen University. In its first full year after approval, the investment management company generated contributions to PATRIZIA's revenue and income in Germany, and the retail business will on this basis continue to accompany and support the Group's growth going forward.

EUR m
254
Volume of funds for retail investors, launched in 2016

PATRIZIA Real Estate Investment Management S.à r.l. (REIM) is our European platform for German and international institutional clients.

Single asset mandates for third parties

PATRIZIA Immobilien AG also manages single asset mandates with real estate assets totalling around EUR 860m. During the reporting period, PATRIZIA acquired the Astro Tower in Brussels for a Taiwanese investor syndicate and signed the acquisition of the Commerzbank Tower in Frankfurt.

PATRIZIA INVESTMENTS FOR THIRD PARTIES AS AT 31 DECEMBER 2016

in EUR m	Assets under management	Equity commitments	of which already invested equity	of which outstanding	Number of established funds
PATRIZIA WohnInvest KVG mbH	*1,497*	*1,523*	*946*	*577* [1]	*9*
Pool funds	1,032	1,063	680	383 [1]	5
Individual funds	465	460	266	194 [1]	4
PATRIZIA GewerbeInvest KVG mbH	*8,496*	*5,844*	*5,071*	*773*	*24*
Pool funds	4,811	3,083	2,766	317	12
Individual funds	1,320	1,447	993	455	10
Label funds	2,365	1,314	1,312	1	2
PATRIZIA Real Estate Investment Management S.à r.l. (REIM) [2]	*468*	*226*	*226*	*0*	*2*
Single asset mandates	*863*	*455*	*455*	*0*	*10*
PATRIZIA GrundInvest KVG mbH	*254*	*0*	*0*	*0*	*5*
Third Parties	**11,578**	**8,048**	**6,698**	**1,350**	**50**

1) Excludes real estate developments secured under purchase contracts

2) PATRIZIA Nordic Cities SCS SICAV-FIS

2.2.2 Co-investments

Through co-investments, PATRIZIA invests in real estate properties in collaboration with clients. In addition to the commitment to the client and to the transaction, these investments also generate management fees in a similar way that it does with our third-party business, and income from participations for PATRIZIA. Shareholders profit from the performance of an attractive and diversified pan-European real estate portfolio. Co-investments contributed EUR 6.9bn to the assets under management as at 31 December 2016. PATRIZIA has invested EUR 0.2bn of our own equity in co-investments.

EUR bn
6.9
Co-Investment assets under management end of 2016

PATRIZIA's co-investments are described below.

Name	Description	AuM in EUR m	PATRIZIA share
GBW	GBW – a former housing company of BayernLB – was acquired in 2013 for a syndicate of German long-term investors. Its aim is long-term, value-adding management of the portfolio, which extends throughout Bavaria. In the fiscal year 2016, there were no material changes to this co-investment.	3,550	5.1%
WohnModul I SICAV-FIS	This co-investment's investment assets include residential and commercial properties across Europe. In the fiscal year 2016, this co-investment made the following acquisitions: – **Berlin:** In Berlin, a residential property was bought in the city centre containing 131 high quality apartments. – **Munich:** In Oberschleißheim, a complex was acquired consisting of three residential buildings with 457 apartments and 14 commercial units. – **Real estate developments in Germany:** In four German cities, there are currently six real estate projects at different stages of development.	1,825	10.1%
PATRoffice Real Estate GmbH & Co. KG	This is an actively managed co-investment with two pension funds from the Netherlands and from Denmark. The exit phase and the sale of the assets commenced in 2013. In 2016, real assets with a value of EUR 36.0m were sold. For the remaining, as yet unsold assets, the transactions will be swiftly concluded and the equity repaid.	209	6.25%
Co-investments in the United Kingdom	PATRIZIA has four different co-investments in industrial parks in the London metropolitan area together with Oaktree Capital Management.	1,050	5–10%
Seneca	The DEIKON portfolio with 86 specialist stores and supermarkets	181	5.1%

2.2.3 Principal investments

In general, PATRIZIA is active as an investment manager for institutional investors and private clients and therefore seeks to avoid any conflicts of interest with its own investments. Principal investments, i.e. transactions on PATRIZIA's own account, are therefore either made in the form of interim financing for closed-end mutual funds or as an early-stage investment with the purpose of including it in an institutional fund at a later point in time. In addition, there is a remaining portion of single residential unit sale assets.

In 2016, the existing principal investments have developed as follows:

Manchester First Street

During the period under review, an undeveloped portion of the asset in Manchester, plot 5, was concluded with the Greater Manchester Pension Fund through a joint venture. The aim is to develop an office complex on the site for which the first leases have already been agreed. In addition to the purchase price, PATRIZIA received a minority stake in the joint venture and will provide project manage the development going forward.

In addition, the largest single principal investment in Manchester, office building No. 1 First Street, was sold to an institutional UK investor. The closing took place in early October 2016.

As at the balance sheet date, PATRIZIA continues to hold two undeveloped areas as well as the food and beverage mall.

Harald

As part of a voluntary public offer, PATRIZIA acquired more than 14,000 apartments in Germany and Sweden during the 2015 fiscal year. The purchase price of the portfolio amounted to approximately EUR 900m. PATRIZIA has since successfully sold all of the units. The units in Sweden were sold for a profit of around EUR 5.3m in 2015, while the sale of the apartments in Germany for around EUR 1.1bn was concluded in 2016.

Other principal investments

For Wildrosenweg in Munich, the closing took place in Q1 2016, after the purchase price had already been paid at the end of 2015 and the single unit sale has started successfully.

In May 2016, a development project was acquired in the attractive Barking district of London. The plan is to develop approximately 200 residential units in a 28-storey building.

Please see item 2.3.2 regarding the contribution to results by these principal investments.

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2.3 Economic environment

2.3.1 General statement by the Managing Board

The fiscal year 2016 was once again an outstanding one for PATRIZIA. All relevant key performance indicators were met successfully. The forecast for the operating income was initially increased from EUR 250m to at least EUR 265m and was ultimately significantly exceeded with an operating income of EUR 283.2m.

EUR m
283.2
operating income 2016

The **operating income** recorded a new record high with EUR 283.2m and increased significantly compared to 2015 (EUR 155.8m, +81.8%). The sharp rise in this key indicator was driven by the proceeds from the sale of the Harald portfolio which contributed EUR 211m to the result and is supported by the generally very positive development of PATRIZIA. Operating income, adjusted for the contribution from the Harald transaction and the performance-related fees from the sale of SÜDEWO, was EUR 72.2m in 2015; this is an increase of 69.3% compared with the previous year's result of EUR 42.7m.

Operating income includes all of PATRIZIA's operating income flows and therefore gives an accurate reflection of actual operating performance. The composition and development of the operating income is explained in detail below.

In the period under review, **fee revenues** increased 14.1% from EUR 165.2m in 2015 to EUR 188.6m. This key performance indicator is relevant because, as part of the transformation of the business from a real estate trader to an investment manager, the increased fee revenues replace the volatile and decreasing disposal and rental revenues as part of the transformation of the business model.

EUR bn
5.1
transaction volume

The **total transaction volume** in fiscal year 2016 remained stable at EUR 7.2bn compared to the previous year. Completed acquisitions totalled EUR 3.2bn and disposals EUR 1.9bn. Moreover, we were able to contractually agree on transactions with a value of more than EUR 2.1bn, the majority of which will be realized in 2017. Of these, EUR 1.7bn represent additional acquisitions while EUR 0.4bn represent already agreed upon disposals.

Assets under management rose as scheduled by EUR 2.0bn to EUR 18.6bn.

Cash and cash equivalents of EUR 440.2m on the balance sheet date will allow PATRIZIA to continue to focus on further attractive investment opportunities in the future. Including attractive co-investments together with our clients, this encompasses the extension of our European activities as well as executing inorganic growth through takeovers of complementary investment managers, if applicable.

The sale of the **Harald portfolio** was concluded as scheduled in 2016. The operating income from this transaction is EUR 211.0m after deduction of transaction-related taxes of EUR 43.2m and minority stakes of EUR 18.3m. In addition, we retained a minority stake in the structure. PATRIZIA continues to hold this minority stake as a Principal Investment and receives a guaranteed dividend amounting to EUR 0.9m p.a.

HARALD

in EUR k	2016
Operating income	272,439
Income taxes	–43,192
Minority stake	–18,290
Share in the operating income of PATRIZIA	**210,957**

The sale was carried out in part as an asset deal and in part as a share deal. The asset deals are recognised as revenue as well as a change in inventories on the income statement. The share deals, on the other hand, are recognised under income from the initial consolidation of subsidiaries. For reasons of comparability, we adjusted for the effects from the sale of the Harald portfolio.

In total, the earnings, net assets and financial position continues to grow well and forms a good basis for the continued implementation of PATRIZIA's strategic goals.

2.3.2 Earnings situation of the Group

Operating Income

Operating income is the Group's most important key performance indicator as it includes the sum of all operating items in the income statement, adjusted by the items listed below. In the 2016 fiscal year, operating income increased by 81.7% to EUR 283.2m (2015: EUR 155.8m). Stripping out the contribution from the sale of the Harald portfolio in 2016, and the performance fee earned for the disposal of SÜDEWO in 2015, the adjusted operating income increased by almost 70% to EUR 72.2m, after recording EUR 42.7m for 2015. The development of the operating income and a prior year comparison is shown below:

Percent

69.3

increase in adjusted operating income

RECONCILIATION OF OPERATING INCOME

in EUR k	2016 (adjusted) [1]	2015 (adjusted) [1]	Change	2016	2015	Change
EBITDA	*56,236*	*47,688*	*17.9*	*328,114*	*175,077*	*87.4%*
Amortisation of fund management contracts [2], depreciation of software and fixed assets	−6,134	−7,059	−13.1	−6,134	−7,059	−13.1%
EBIT	*50,102*	*40,629*	*23.3*	*321,980*	*168,018*	*91.6%*
Financial result (interest result)	−2,523	−6,251	−59.6	−4,304	−16,505	−73.9%
Gains / losses from currency translation	−5,644	1,143		−4,029	−618	
EBT	*41,935*	*35,521*	*18.1*	*313,647*	*150,895*	*107.9%*
Change in value of derivatives	0	0		0	−2,888	
+ Amortisation of fund management contracts [2]	1,968	1,968	0.0	1,968	1,968	0.0%
– Value change in investment property	−431	−462	−6.7	−431	−462	−6.7%
Harald – transaction-related taxes and minorities	0	0		−61,482	0	
Net realised valuation gains from the sale of investment property	1,529	5,758	−73.4	1,529	5,758	−73.4%
Reorganisation expenses	20,406	0		20,406	0	
Expenses / (income) from unrealised currency translation	6,812	−133		7,539	545	
Operating income	**72,219**	**42,652**	**69.3**	**283,176**	**155,816**	**81.7%**

1) adjusted = without SÜDEWO, Harald

2) Fund management contracts that have been transferred in the course of the acquisition of PATRIZIA GewerbeInvest KVG mbH

In line with the transformation of the business model towards an investment management company with a European focus, fee streams have become the main source of operating income. Meanwhile, sales proceeds from single unit sales as well as rental income are increasingly diminishing.

Other items in the reconciliation of the operating income are shown below based on their position in the consolidated income statement.

Consolidated Income Statement

PATRIZIA EARNINGS AT A GLANCE

in EUR k	2016	2015	Change
Revenues	817,879	384,858	112.5%
Total operating performance	526,385	249,419	111.0%
EBITDA	328,114	175,077	87.4%
EBIT	321,980	168,018	91.6%
EBT	313,647	150,895	107.9%
Operating income [1]	283,176	155,816	81.7%
Consolidated annual profit	256,264	134,462	90.6%

1) Adjusted for amortisation on fund management contracts, unrealised changes in the value of investment property and non-cash effects from interest and currency hedging transactions. Non-realised currency changes and reorganisation expenses are eliminated. Realised changes in the value of investment property as well as realised currency changes have been added.

Revenues

Consolidated revenues remained broadly stable at EUR 325.4m in 2016, compared with EUR 338.7m in the prior year period. While sales proceeds from principal investments decreased, all other items grew positively and largely compensated the decline in sales proceeds.

REVENUES

in EUR k	2016 (adjusted) [1]	2015 (adjusted) [1]	Change	2016	2015	Change
Sales proceeds from principal investments	143,705	188,979	–24.0%	629,799	188,979	233.3%
Rental revenues	11,992	8,797	36.3%	18,509	42,761	–56.7%
Revenues from management services	161,261	134,259	20.1%	161,261	134,259	20.1%
Revenues from ancillary costs	4,171	2,464	69.3%	4,021	14,678	–72.6%
Miscellaneous	4,288	4,182	2.5%	4,289	4,181	2.6%
Consolidated Revenues	**325,417**	**338,681**	**–3.9%**	**817,879**	**384,858**	**112.5%**

1) adjusted = without SÜDEWO, Harald

Consolidated revenues are of limited informative value, as items shown beneath the revenue line must also be taken into consideration to obtain a complete picture of the operational performance.

Sales proceeds from principal investments include purchase price revenues from PATRIZIA's own portfolio, which are now diminishing. The sales proceeds of EUR 143.7m mainly include EUR 46.9m from single unit sales as well as EUR 86.5m of proceeds from the disposal of two assets in Manchester.

The increase in **rental revenues** from EUR 8.8m in 2015 to EUR 12.0m in 2016 was largely due to the addition of single unit sales properties in Munich at the beginning of 2016 and the rental income from the office building in Manchester, which was sold in October 2016.

Revenues from management services are fees that PATRIZIA charge as an investment manager. As PATRIZIA evolves towards a more fee-related business, this accelerated fee streams during 2016 which increased to a total amount of EUR 161.3m, up 14.1% from EUR 134.3m in 2015.

Percent
14.1
increase of fee income

Including GBW, fee income increased 14.1% to EUR 188.6m from EUR 165.2m in 2015.

The table below demonstrates the development of the various fee components, including the contributions from the co-investment in GBW, which are classified as income from participations.

FEE INCOME

in EUR k	2016 (adjusted) [1]	2015 (adjusted) [1]	Change	2016	2015	Change
Management fees	89,062	77,653	14.7%	89,062	77,653	14.7%
Transaction fees	70,329	62,575	12.4%	70,329	62,575	12.4%
Performance fees	29,167	24,988	16.7%	29,167	128,529	–80.6%
Total	**188,558**	**165,219**	**14.1%**	**188,558**	**268,757**	**–29.8%**

1) adjusted = without SÜDEWO, Harald

The **revenues from ancillary costs** amounted to EUR 4.2m (2015: EUR 2.5m, +69.3%) and include the allocation of recoverable ancillary rental costs, which increased in line with rental growth. **Miscellaneous** items include transaction costs and expenses which are charged to the corresponding investment vehicles. Due to steady transaction volumes, this item remains stable at EUR 4.3m.

Total Operating Performance

Total operating performance reflects PATRIZIA's performance more comprehensively than consolidated revenues. Although revenues slightly decreased in 2016, total operating performance increased by 17.7% to EUR 226.9m, from EUR 192.8m in 2015.

Percent
17.7
increase in operating performance

TOTAL OPERATING PERFORMANCE

in EUR k	2016 (adjusted) [1]	2015 (adjusted) [1]	Change	2016	2015	Change
Revenues	325,417	338,681	−3.9%	817,879	384,858	112.5%
Income from the sale of investment property	1,542	10,075	−84.7%	1,542	10,075	−84.7%
Changes in inventories	−115,133	−166,951	−31.0%	−502,018	−166,980	200.6%
Other operating income	9,903	11,010	−10.1%	14,252	16,189	−12.0%
Income from the deconsolidation of subsidiaries	5,187	0		194,730	5,277	
Total operating performance	**226,916**	**192,815**	**17.7%**	**526,385**	**249,419**	**111.0%**

1) adjusted = without SÜDEWO, Harald

Revenues remained broadly stable at EUR 325.4m (2015: EUR 338.7m, −3.9%), as increased fee income from the investment management business compensated diminishing sales proceeds.

Income from the sale of investment property
Income from the sale of investment property, including properties that had been held by PATRIZIA for a long period of time, contributed a net income of EUR 1.6m in 2016 compared to EUR 10.1m in 2015. The total sales proceeds amounted to EUR 10.9m (2015: EUR 69.8m) and the corresponding book values were EUR 9.3m (2015: EUR 59.7m). The strong decline of 84.7% is due to diminishing stock and therefore lower sales volume.

Changes in inventories
During 2016 changes in inventories amounted to EUR -115.1m (2015: EUR −167.0m, −31.0%). Corresponding declines in the carrying value of real estate sold from inventory reduced the stock by EUR 125.3m (2015: EUR 182.3m, −31.3%). The most significant changes to the inventory were the disposal of two assets in Manchester (EUR −72.4m) as well the single unit sales business (EUR −40.9m).

Other operating income
Other operating income decreased by 10.1% to EUR 9.9m (2015: EUR 11.0m). Of this, EUR 4.7m was due to expired obligations (2015: EUR 5.2m) and a further EUR 1.3m (2015: EUR 1.7m) from the reimbursement of transaction costs and fees.

Income from the deconsolidation of subsidiaries
Income from the deconsolidation of subsidiaries amounts to EUR 5.2m (2015: 0m) and relates to assets held temporarily on PATRIZIA's balance sheet for subsequent placement with retail funds of PATRIZIA GrundInvest KVG. PATRIZIA did not charge a gain on the purchase price.

RECONCILIATION OF EBITDA

in EUR k	2016 (bereinigt)[1]	2015 (bereinigt)[1]	Change	2016	2015	Change
Total operating performance	226,916	192,815	17.7%	526,385	249,419	111.0%
Cost of materials	−27,708	−29,746	−6.9%	−33,712	−52,438	−35.7%
Cost for purchased services	−14,832	−14,787	0.3%	−14,832	−14,787	0.3%
Staff costs	−87,292	−93,519	−6.7%	−101,313	−93,519	8.3%
Change in value of investment property	431	462	−6.7%	431	462	−6.7%
Other operating expenses	−61,191	−59,984	2.0%	−68,757	−69,973	−1.7%
Income from participations	32,667	48,215	−32.2%	32,667	151,681	−78.5%
Earnings from companies accounted for using the equity method	7,651	4,232	80.8%	7,651	4,232	80.8%
EBITDAR	76,642	47,688	60.7%	348,520	175,077	99.1%
Reorganisation expenses	−20,406	0		−20,406	0	
EBITDA	**56,236**	**47,688**	**17.9%**	**328,114**	**175,077**	**87.4%**

1) adjusted = without SÜDEWO, Harald

Cost of materials

Cost of materials include construction and maintenance measures for PATRIZIA's own assets, which are usually capitalised. Year-on-year, the cost of materials decreased slightly by 6.9%, from EUR 29.7m in 2015 to EUR 27.7m in 2016, in line with the reduced level of own stock and development activities. It comprises the following items:

- Refurbishment and development costs of EUR 20.6m (2015: EUR 23.6m, −13.0%)
- Maintenance costs of EUR 0.8m (2015: EUR 0.7m, +4.0%)
- Allocable rental ancillary costs of EUR 6.4m (2015: EUR 5.4m, +18.7%)

Cost of purchased services

Cost of purchased services largely include expenditures for the white labelled funds of PATRIZIA GewerbeInvest, for which PATRIZIA acts as service provider only. The cost for these purchased services decreased by 4.8% to EUR 12.8m in 2016, compared to EUR 13.5m in the previous year. Management income from white labelled funds decreased by 2.9% to EUR 15.5m, compared with EUR 16.0m in 2015.

Staff costs

Mainly due to reduced sales commissions and a positive effect from long-term variable compensation, the total staff costs decreased during the year:

STAFF COSTS

in EUR k	2016 (adjusted)[1]	2015 (adjusted)[1]	Change	2016	2015	Change
Fixed salaries	50,483	48,413	4.3%	50,492	48,413	4.3%
Variable salaries	22,544	20,526	9.8%	36,544	20,526	78.0%
Sales commissions	4,212	6,989	−39.7%	4,212	6,989	−39.7%
Social security contributions	10,607	9,609	10.4%	10,618	9,609	10.5%
Effect of long-term variable compensation[2]	−2,824	4,464		−2,824	4,464	
Miscellaneous	2,270	3,518	−35.5%	2,271	3,518	−35.4%
Total	**87,292**	**93,519**	**−6.7%**	**101,313**	**93,519**	**8.3%**

1) adjusted = without SÜDEWO, Harald

2) Valuation changes of the long-term variable remuneration due to change in the share price. For further details please refer to the compensation report under 3.2.

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Staff costs decreased by 6.7% to EUR 87.3m from EUR 93.5m in 2015. The fixed salaries of staff grew by 4.3% to EUR 50.5m from EUR 48.4m in the prior year mainly due to salary increases in line with usual adjustments. Variable salaries rose by 9.8% to EUR 22.5m from EUR 20.5m in the prior year period, reflecting the good operational performance of PATRIZIA. Sales and distribution commissions decreased by 39.7% to EUR 4.2m from EUR 7.0m in the prior year in line with the reduced volume of single units sold. The negative share price performance resulted in a positive effect of EUR 2.8m of the long-term variable compensation, compared with costs of EUR 4.5m in 2015. Miscellaneous items, which mainly refer to payment in kind, decreased by 35.5% to EUR 2.3m versus EUR 3.5m in 2015.

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Change in the value of investment property

This item includes the result of the annual valuation of investment property. For 2016, the change in value amounted to EUR 0.4m, after EUR 0.5m in the previous year.

Other operating expenses

Other operating expenses increased slightly by 2.0% to EUR 61.2m from 60.0m in 2015.

OTHER OPERATING EXPENSES

in EUR k	2016 (adjusted) [1]	2015 (adjusted) [1]	Change	2016	2015	Change
Advisory and audit fees	14,654	16,027	−8.6%	14,953	19,507	−23.3%
Cost of management services	440	222	98.2%	6,300	5,115	23.2%
Vehicle and travel costs	5,399	5,179	4.2%	5,399	5,179	4.2%
IT costs, communication costs and office supplies	7,425	7,863	−5.6%	7,425	7,863	−5.6%
Advertising costs	4,435	4,431	0.1%	4,488	4,785	−6.2%
Recruitment costs, training costs and costs for tempo-rary work	2,577	2,023	27.4%	2,577	2,023	27.4%
Rent, cleaning and ancillary costs	7,003	6,827	2.6%	7,288	7,182	1.5%
Contributions, charges and insurance costs	2,347	1,779	31.9%	2,475	1,790	38.3%
Commissions and other sales costs	2,583	4,429	−41.7%	2,590	4,441	−41.7%
Other taxes	1,218	200		1,218	200	
Indemnity / reimbursement	6,568	1,300		6,568	1,300	
Miscellaneous	6,542	9,704	−32.6%	7,476	10,588	−29.4%
Total	**61,191**	**59,984**	**2.0%**	**68,757**	**69,973**	**−1.7%**

1) adjusted = without SÜDEWO, Harald

Commissions and other sales costs decreased by 41.7% to EUR 2.6m from EUR 4.4m in the previous year, in line with diminishing sales activities. Other taxes increased to EUR 1.2m from EUR 0.2m in 2015 due to asset taxes for a Luxembourg-based subsidiary. Indemnity / reimbursement costs rose to EUR 6.6m from EUR 1.3m in the prior year and mainly relate to extraordinary costs for prior years transactions.

Income from participations

Income from participations and earnings from companies accounted for using the equity method display investment income from co-investments, which are earned in addition to management fees. In the reporting period, income from participations decreased by 23.1% to EUR 40.3m from EUR 52.4m in 2015. The decrease reflects the loss of income from SÜDEWO following its disposal in 2015.

The co-investment **GBW** generated EUR 9.5m from services provided as shareholder contribution and an amount of EUR 17.8m in performance-related shareholder compensation as well as a distribution on invested equity of EUR 3.2m – all unchanged from 2015.

The **Seneca** supermarket portfolio contributed a slightly lower dividend of EUR 0.4m (2015: EUR 0.5m). The **co-investments in the UK** contributed a pay-out of EUR 0.9m compared with EUR 0.1m in 2015. The remaining minority stake in Harald, which is now considered as a co-investment, contributed EUR 0.9m. The co-investment WohnModul I generated an income of EUR 7.7m compared to EUR 4.2m in the previous year, which is reported as earnings from companies accounted for using the equity method.

INCOME FROM PARTICIPATIONS

in EUR k	2016 (adjusted) [1]	2015 (adjusted) [1]	Change	2016	2015	Change
SÜDEWO	*0*	*17,042*		*0*	*120,508*	
Services provided as a shareholder contribution	0	3,625		0	3,625	
Performance-related shareholder compensation	0	0		0	103,466	
Earnings on capital employed	0	13,417		0	13,417	
GBW	*30,520*	*30,555*	*−0.1%*	*30,520*	*30,555*	*−0.1%*
Services provided as a shareholder contribution	9,490	9,490	0.0%	9,490	9,490	0.0%
Performance-related shareholder compensation	17,807	17,842	−0.2%	17,807	17,842	−0.2%
Earnings on capital employed	3,223	3,223	0.0%	3,223	3,223	0.0%
SENECA	*434*	*510*	*−14.9%*	*434*	*510*	*−14.9%*
UK	*853*	*108*	*689.8%*	*853*	*108*	*689.8%*
Harald	*860*	*0*		*860*	*0*	
WohnModul I	*7,651*	*4,232*	*80.8%*	*7,651*	*4,232*	*80.8%*
Total	**40,318**	**52,447**	**−23.1%**	**40,318**	**155,913**	**−74.1%**

1) adjusted for the performance fee for SÜDEWO

Reorganisation expenses

In 2016, PATRIZIA made a strategic decision to focus on its core investment management activities and services which create a higher value for PATRIZIA's clients and their investments. Following this decision, PATRIZIA selected an external service provider for property management services, and subsequently disposed its existing division to a strategic buyer.

The reorganisation process incurred one-off expenses of EUR 20.4m in 2016 (2015: EUR 0m), which PATRIZIA expects to be recouped through savings within the next two to three financial years.

REORGANISATION EXPENSES

in EUR k	2016
Reorganisation expenses for compensation	9,329
Reorganisation expenses for current salaries	4,020
Reorganisation expenses for material costs	2,613
Reorganisation expenses for consulting	4,444
Total	**20,406**

Consolidated Annual Profit

Mainly due to increased income taxes, the adjusted net profit for the period decreased by 15.7% to EUR 27.7m from EUR 32.9m in 2015.

NET PROFIT FOR THE PERIOD

in EUR k	2016 (adjusted) [1]	2015 (adjusted) [1]	Change	2016	2015	Change
EBITDA	*56,236*	*47,688*	*17.9%*	*328,114*	*175,077*	*87.4%*
Amortisation of fund management contracts, depreciation of software and fixed assets	−6,134	−7,059	−13.1%	−6,134	−7,059	−13.1%
EBIT	***50,102***	***40,629***	***23.3%***	*321,980*	***168,018***	***91.6%***
Financial income	2,682	939	185.6%	3,057	6,666	−54.1%
Financial expenses	−5,204	−7,190	−27.6%	−7,361	−23,171	−68.2%
Gains / losses from currency translation	−5,644	1,143		−4,029	−618	
EBT	*41,936*	***35,521***	***18.1%***	*313,647*	***150,895***	***107.9%***
Income taxes	−14,193	−2,623	441.1%	−57,383	−16,433	249.2%
Net profit for the period	**27,743**	**32,898**	**−15.7%**	**256,264**	**134,462**	**90.6%**

1) adjusted = without SÜDEWO, Harald

Amortisation of fund management contracts, software and fixed assets

Amortisation of fund management contracts, the depreciation of software and fixed assets decreased by 13.1% to EUR 6.1m from EUR 7.1m in 2015. The largest single positions are the amortisation of fund management contracts of EUR 2.0m (2015: EUR 2.5m), the depreciation of software of EUR 3.3m (2015: EUR 2.6m, +27.6%) as well as the depreciation of equipment of

Consolidated Financial Statements

EUR 1.2m (unchanged year-on-year). For a summary of the fixed assets please refer to item 4 of the Notes to the Consolidated Financial Statements.

Financial income

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Financial income increased to EUR 2.7m from EUR 0.9m year-on-year and includes interest income on delayed purchase price receipts. Financial expenses decreased to EUR 5.2m (2015: EUR 7.2m; −27.6%). The currency result amounted to EUR −5.6m (2015: EUR 1.1m). This includes realised currency losses of EUR 8.9m (2015: gains of EUR 1.0m), which were compensated by EUR 10.1 (2015: EUR 0m) gains from currency hedging as well as EUR 6.8m non-realised and non-cash effective temporary currency losses (2015: gain of EUR 0.1m). A major driver behind the currency result was the change in Pound Sterling. For further information please refer to item 6.10 of the Notes to the Consolidated Financial Statements.

Income taxes

Income taxes increased to EUR 14.2m compared with EUR 2.6m in 2015. While 2015 was influenced by tax reimbursements for prior years, the rise in 2016 was driven by EUR 7.6m of tax payments on the disposal gains of the assets sold in Manchester.

2.3.3 Net asset and financial situation of the Group

PATRIZIA NET ASSET AND FINANCIAL KEY FIGURES

in EUR k	31.12.2016	31.12.2015	Change
Total assets	993,259	1,631,831	−39.1%
Equity (excluding non-controlling partners)	749,342	521,601	43.7%
Equity ratio	75.4%	32.0%	43,4 PP
Bank loans	53,200	821,828	−93.5%
+ Bonded loans	27,000	67,000	−59.7%
- Cash and cash equivalents	440,219	179,141	145.7%
= Net financial debt	−360,019	709,687	
Real estate assets [1]	**82.1%**	**35.9%**	**46.2 PP**

1) Shareholders equity (excl. minorities) divided by net assets (total assets less total debt covered by incremental cash)

PP = percentage points

Percent

82.1

net equty ratio

Total assets

The Group's total assets decreased to EUR 993.3m compared to EUR 1,631.8m in 2015. The decline was largely due to the disposal of principal investments like the Harald portfolio and the Manchester assets and the redemption of the respective loans in 2016. For PATRIZIA GrundInvest KVG, two assets are held in the balance sheet temporarily.

Investment property and inventories

In the consolidated financial statement, PATRIZIA's real estate assets amounted to EUR 195.2m (31 December 2015: EUR 1,078.7m, –81.9%):

in EUR k	2016	2015	Change
Investment property	12,226	20,802	–41.2%
Inventories	182,931	1,057,942	–82.7%
Principal investments	**195,157**	**1,078,744**	**–81.9%**

Of this, EUR 12.2m were attributable to **investment property**. EUR 182.9m are **inventories** and include principal investments such as the remainder of the Manchester portfolio and the properties in Munich held for residential unit sales as well as assets to be placed in the retail funds of PATRIZIA GrundInvest KVG. The sharp decrease is due to the sale of the Harald portfolio and two assets in Manchester.

The capital allocation table provides an overview of all participations, assets under management and PATRIZIA's invested capital:

PATRIZIA CAPITAL ALLOCATION AS AT 31 DECEMBER 2016

in EUR m	Assets under management	PATRIZIA investment capital	Participation in %
Third parties	11,578	–	–
Co-investments	6,918	182.1	
Residential	5,420	142.6	
GBW GmbH	3,550	55.4	5.1
WohnModul I SICAV-FIS	1,825	86.6	10.1
Other	44	0.7	10.0
Commercial Germany	448	18.4	
PATRoffice	209	5.5	6.3
Seneca	181	4.9	5.1
sono west	58	8.0	30.0
Commercial international	1,050	21.0	
Aviemore Topco (UK)	512	12.9	10.0
Citruz Holdings LP (UK)	93	3.3	10.0
Plymouth Sound Holdings LP (UK)	61	1.8	10.0
Winnersh Holdings LP (UK)	384	3.0	5.0
Principal investments	144	158.6	
Harald	0	22.9	5.3
Other	144	135.6	100.0
Operating companies [1]	–	38.5	100.0
Tied investment capital	18,641	379.1	
Bank balances and cash	-	397.2	–
Total investment capital	18,641	776.3	
of which external capital (bonded loans and bridge financing)	–	27.0	–

1) Tied investment capital relating to the acquisition of companies (mainly the acquisition of PATRIZIA GewerbeInvest KVG) and the capital commitment from the operation of the services business (mainly investments in systems and current receivables).

Capital Structure

In accordance with the decrease of total assets, the liabilities were also significantly reduced at the reporting date.

Bonded loans

In 2013, two bonded loans with a total amount of EUR 77.0m were issued. In 2016, one bonded loan was fully redeemed on time. For the other bonded loan a prepayment of EUR 5.0m was made without pre-payment penalties. A pre-payment of the same amount was also made at the beginning of 2017, hence it was considered as a short-term liability in the balance sheet.

Bank loans and financial liabilities

Two assets to be placed in retail funds of PATRIZIA GundInvest KVG were temporarily added to the balance sheet. The bank loans for these assets amounted to EUR 53.2m as of 31 December 2016. The sharp decrease compared with 2015's short-term bank loans is due to the redemption of loans for the Harald portfolio post sale.

The development of bank loans and financial liabilities is shown in the following table:

in EUR k	31.12.2016	31.12.2015	Change
Long-term bonded loans	22,000	32,000	–31.3%
Short-term bonded loans	5,000	35,000	–85.7%
Short-term bank loans	53,200	821,828	–93.5%
Total	**80,200**	**888,828**	**–91.0%**

A detailed schedule of maturities for the loans by fiscal year is shown in the Notes to the Consolidated Financial Statements under item 5.4.

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Liquidity

Financing of the PATRIZIA Group is centrally managed by PATRIZIA Immobilien AG. As at 31 December 2016, loan agreements existed with three banks. In order to optimise liquidity and interest costs, loans were redeemed over the course of 2016 whenever possible without paying a pre-payment penalty.

Liquidity management ensures that the PATRIZIA Group is able to meet all financial obligations at all times. Most of the Group's affiliated companies and subsidiaries are directly linked to the Group's centralised cash pooling system. On a same-day basis, account surpluses are transferred to the parent company and account deficits are offset. Payment receipts from operating companies and the liquidity surpluses from sales and disposals represent the most important source of liquidity within the Group and ensure that all financing requirements are met. An appropriate liquidity reserves are maintained to ensure the Group's continued solvency. As of 31 December 2016, PATRIZIA holds cash and cash equivalents of EUR 440.2m (2015: EUR 179.1m)

EUR m
440
liquidity at year end 2016

The cash position of the Group is not freely available in its entirety. Through the sale of the Harald portfolio, remaining transaction-based liabilities and payments to non-controlling shareholders of EUR 36.0m have to be made, but were not due at the reporting date. In addition, a cash reserve of EUR 6.9m has to be permanently held available for the regulated investment management companies (KVGs) due to regulatory requirements (2015: EUR 8.4m). Hence, the available free cash balance amounts to EUR 397.2m.

Cash Flow Statement

In the reporting year, cash inflows from current **business activities** amounted to EUR 503.4m (2015: EUR 90.4m). The increase was driven by the sale of the Harald portfolio and the disposal of two assets in Manchester, while only minor assets were acquired. **Investment activities** resulted in a cash inflow of EUR 268.2m (2015: outflow of EUR 181.2m), and were mainly driven by the sale of the Harald portfolio and the disposal of two assets in Manchester as well as inflows from the sale of investment property. Along with that, the significant amount of cash was used to redeem almost all loans, which resulted in a significant outflow from **financing activities** of EUR 508.2m (2015: inflow of EUR 124.1m). The **change in cash** amounted to EUR 263.4m (2015: EUR 33.3m) and increased cash and cash equivalents from EUR 179.1m at the end of 2015 to EUR 440.2m as of 31 December 2016.

SUMMARY OF THE 2015 CONSOLIDATED CASH FLOW STATEMENT

in EUR k	2016	2015	Change
Cash inflow from operating activities	503,382	90,406	
Cash inflow/outflow from investment activities	268,191	−181,210	
Cash inflow/outflow from financing activities	−508,185	124,130	
Changes in cash	263,388	33,326	
Cash and cash equivalents 1 January	179,141	145,361	23.2%
Cash and cash equivalents 31 December	440,219	179,141	145.7%

2.3.4 Notes on the Annual Financial Statements prepared under HGB for PATRIZIA Immobilien AG (Holding Company)

The purpose of PATRIZIA Immobilien AG as parent company is essentially driven by the activities of the operating companies of the Group.

As a financing and management holding company for these companies, PATRIZIA Immobilien AG generated **revenues** of EUR 20.3m (2015: EUR 20.9m, −3.1%), mainly as a result of management cost allocations to the subsidiaries. Commission income for services provided by the subsidiaries is also settled through the parent company and results in corresponding proceeds.

Staff costs decreased by 10.7% to EUR 24.0m (2015: EUR 26.9m) mainly due to the negative valuation impact from long-term variable compensation. The **cost of materials** decreased to EUR 0.1m and **other operating expenses** increased by 33.7% to EUR 42.2m (2015: EUR 31.6m). Other operating expenses increased due to higher rental expenses for office premises resulting from European expansion, higher IT costs, provisions for litigation and other one-time effects from the prior year's transactions. The **Net interest result** decreased to EUR -15.3m from EUR -0.9m due to higher liabilities to the Group's cash pooling. **Net income from profit transfers and loss transfers** decreased significantly to EUR 27.1m from EUR 122.9m, as the 2015 figure was strongly impacted by the effects of the SÜDEWO disposal.

PATRIZIA Immobilien AG's **net result** under German Commercial Code HGB for the 2016 fiscal year turned negative to EUR −20.1m, after a profit of EUR 92.2m in 2015, and led to lower retained earnings of EUR 181.0m (2015: EUR 204.1m)

PATRIZIA Immobilien AG's performance is expected to turn positive again for the 2017 fiscal year, as the Company expects a solid operational performance as well as the pay-out of proceeds from the disposal of the Harald portfolio. For further details, please refer to the Group report on expected developments (item 6).

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SUMMARY OF THE PATRIZIA IMMOBILIEN AG BALANCE SHEET

in EUR k	31.12.2016	31.12.2015
Non-current assets	518,274	475,007
Current assets	421,186	141,900
Prepaid expenses	345	346
Total assets	**939,805**	**617,253**
Equity	456,055	479,120
Provisions	29,405	30,423
Liabilities	454,346	107,710
Total equity and liabilities	**939,805**	**617,253**

SUMMARY OF THE PATRIZIA IMMOBILIEN AG INCOME STATEMENT

in EUR k	2016	2015	Change
Revenues	20,303	20,949	–3.1%
Other capitalised services and other operating income	14,081	18,752	–24.9%
Cost of materials (cost of purchased services)	–13	–63	–79.2%
Staff costs	–24,012	–26,889	–10.7%
Depreciation, amortisation, write-downs and other operating expenses	–42,224	–31,572	33.7%
Profit/loss from participations, profit transfers and loss transfers	27,066	122,890	–78.0%
Net interest result	–15,285	–910	
Result from ordinary activities	***–20,085***	***103,157***	***–119.5%***
Taxes	–2,980	–10,244	–70.9%
Net profit/loss	***–23,065***	***92,913***	
Retained earnings	204,082	111,169	83.6%
Balance sheet profits	**181,017**	**204,082**	**–11.3%**

3 ADDITIONAL INFORMATION

3.1 Information relating to takeovers

All of PATRIZIA's arrangements comply with the standards for German publicly traded companies.

Composition of subscribed capital, capitalisation

On 16 June 2016, the Annual General Meeting approved the management's proposal to carry the entire profit to new account and to issue bonus shares in a ratio of 10:1 for the 2015 financial year. Since the corresponding capital increase was registered into the Commercial Register on 12 August 2016, the Company's subscribed share capital (nominal capital) has totalled EUR 83,955,887 and is divided into 83,955,887 shares. These shares are registered no-par value shares. There are no other classes of shares.

Restrictions relating to voting rights or the transfer of shares

Each share confers the right to one vote; there are no restrictions concerning either voting rights or the transfer of shares. The Managing Board is also not aware of corresponding shareholder agreements.

Direct or indirect interest amounting to more than 10% of the capital

As at 31 December 2016, Wolfgang Egger, CEO of PATRIZIA Immobilien AG, held a total stake of 51.62% in the Company via First Capital Partner GmbH, in which he directly and indirectly holds a 100% stake via WE Vermögensverwaltung GmbH & Co. KG.

Shares with special rights conferring powers of control

There are no shares with special rights conferring powers of control.

Control of voting rights where employees hold shares in the Company's capital

There are no controls in respect of voting rights.

Appointment and dismissal of members of the Managing Board, changes to the Articles of Association

The appointment and dismissal of the Managing Board is governed by Article 84 of the German Stock Corporation Act and is supplemented by Article 6 of the Company's Articles of Association. Changes to the Articles of Association take place in accordance with Article 179 et seqq. of the AktG in combination with Articles 16 and 21 of the Articles of Association of PATRIZIA Immobilien AG. These make use of the option, granted by law, of specifying a different capital majority.

Powers of the Managing Board to issue and buy back shares

By resolution of the Annual General Meeting of 25 June 2015, the Managing Board is entitled to acquire shares in the Company with a volume of up to 10% of the share capital until 24 June 2020. The entitlement may be exercised by the Company in full or for partial amounts, on one or more occasions and in pursuit of one or more purposes, but also by its subsidiaries or for its own account or for the account of the latter by third parties. Purchases can be exercised at the discretion of the Managing Board via the stock exchange, by means of a public bid made to the shareholders, through the use of derivative instruments or through an individually negotiated repurchase. The acquired shares may subsequently be used for all legally permissible purposes; in particular they may be cancelled, sold in exchange for a contribution in kind or to shareholders or used to meet subscription or conversion rights.

The Managing Board was further authorised, by resolution of the Annual General Meeting on 16 June 2016, to increase the share capital on one or more occasions with the consent of the Supervisory Board by up to a total of EUR 37,000,000.00 in exchange for cash contributions and / or contributions in kind by issuing new, registered no-par value shares by 15 June 2021 (Authorised Capital 2016 / I). In certain cases, the Managing Board is authorised, with the approval of the Supervisory Board, to exclude the legal subscription rights of the shareholders. The complete authorisation results from Article 4 (3) of the Articles of Association.

Furthermore, the Managing Board is authorised, by resolution of the Annual General Meeting on 16 June 2016, to increase the share capital on one or more occasions with the consent of the Supervisory Board by up to a total of EUR 1,000,000 in exchange for cash contributions and / or contributions in kind by issuing new, registered no-par value shares to be granted to employees of PATRIZIA Immobilien AG or affiliated companies by 15 June 2021 (Authorised Capital 2016/II). The complete authorisation results from Article 4 (3a) of the Articles of Association.

In addition, the Managing Board is authorised on one or more occasions, with the approval of the Supervisory Board to grant until 15 June 2021 convertible bonds, warrant bonds, participatory rights, and / or participating bonds or, respectively, a combination of these instruments in the nominal amount of up to EUR 950,000,000.00 with or without a term limit and to grant the creditors or respectively the bearers of bonds conversion privileges or option rights to shares of the Company with a pro-rata amount of the share capital of up to EUR 38,000,000.00 in accordance with the specific provisions of the respective option and convertible bond conditions or respectively participatory rights and participating bond conditions. The details relating to the contingent capital increase result from Article 4 (4) of the Articles of Association.

Significant agreements by the Company contingent upon a change in control subsequent to a takeover bid

No agreements contingent upon a change in control subsequent to a takeover bid exist.

Compensation agreements by the Company with the members of the Managing Board or employees for the event of a takeover bid

No compensation agreements exist with the members of the Managing Board or employees for the event of a takeover bid.

3.2 Compensation report

The compensation report explains the principle features of the compensation system for the Managing Board and Supervisory Board of PATRIZIA Immobilien AG and discloses the amount of the payments made to the individual members of the Managing Board and Supervisory Board for the 2016 fiscal year. The compensation report considers all statutory requirements and corresponds to the recommendations of the German Corporate Governance Code, with the restriction that the variable portion of remuneration does not set a maximum amount.

Compensation of the Managing Board

The system of management compensation used was approved under a resolution of the Annual General Meeting on 23 June 2010. The amount and structure of the compensation paid to the Managing Board members are determined and regularly reviewed by the Supervisory Board. The compensation paid to Managing Board members is based on their respective remit, the personal performance of the individual Managing Board member and of the Managing Board as a whole, as well as the economic and financial situation and performance of PATRIZIA. The compensation paid to Managing Board members is customary for the sector, appropriate and performance-related. It is made up of non-performance-related components and performance-related components with short- and long-term incentive effects. There are no agreements in place in the case of a change of control.

Non-performance-related compensation

The non-performance-related components comprise fixed basic compensation, which is paid as a monthly salary, pension contributions as well as non-cash and other benefits which primarily consist of values to be applied in accordance with tax guidelines for the use of a company car and insurance premiums.

Performance-related compensation

As a general principle, performance-related, variable compensation components are calculated on the basis of quantitative and qualitative targets set at the start of the fiscal year, which are divided into three categories: company targets, business line targets and individual targets. Consequently, the amount of variable compensation paid out depends on the degree to which the predetermined targets are achieved, missed or exceeded.

The primary criterion for the achievement of company targets is the operating result, the Group's most important performance indicator. Every year, depending on the Company's planning, a target figure that exactly specifies the amount of consolidated profit to be achieved is defined. If the operating result is less than the hurdle of 67% of the defined target figure, the variable compensation of the Managing Board is omitted completely, irrespective of which other targets – company, business line or individual targets – were achieved. Additional criteria for calculating variable compensation are the return on equity in the past fiscal year and the performance of PATRIZIA's shares over two years in relation to the DIMAX real estate reference index. The target figures defined for each target correspond to a degree of achievement of 100%. If the actual value determined corresponds to more than 120% of the defined target value, 150% of the variable compensation is paid. This is also the upper limit that has been defined, at the time of granting, for the maximum amount of variable compensation that can be achieved. If 80% of the target is achieved, 50% of the variable compensation is granted.

Short- and long-term components of variable compensation

For each predefined target, a variable compensation amount is calculated depending on the degree to which the target has been achieved. The total of all the amounts is paid out in two components. Two-thirds of the amount is paid out as a cash payment, which is designated as a short-term component. The remaining third of the variable compensation is granted as performing share units, i.e. it is not paid out directly in cash. This third is intended as a component with a long-term incentive plan. Performing share units are virtual shares which grant the legitimate beneficiary the right to receive a monetary amount after a fixed performance period has passed. The performance share units do not carry any voting or dividend rights. Since the beginning of the 2015 fiscal year, this performance period is three years for all members of the Management Board. The performing share units do not grant any voting or dividend rights. The variable compensation component with a long-term incentive effect is initially converted into performing share units at the average Xetra rate of the PATRIZIA share 30 days prior to and post 31 December of the fiscal year in question. The cash price equivalent of the shares calculated from this is paid out at the average Xetra rate 30 days prior to and after 31 December of the third year following the fiscal year in question, i.e. after the end of the vesting period. The variable compensation component with a long-term incentive effect is thus linked to the Company's share price performance. A maximum amount for the fair value at the time of payment has not been set.

Shares of the individual components in the Managing Board's overall compensation

Assuming that both PATRIZIA and the Managing Board members meet 100% of their targets for the respective fiscal year, the following approximate compensation structure applies for the fair value at the time of granting: around 41% of the total remuneration of Messrs Egger and Schmitt is made up of non-performance-related compensation components; short-term variable compensation, which is payable immediately, accounts for a further 39%; the long-term compensation component from performing share units makes up around 20% of the overall compensation. For Mr Bohn, the ratio is 46% / 36% / 18%.

Total remuneration for the 2016 fiscal year

The remuneration granted to the members of the Managing Board for the 2016 fiscal year totalled EUR 3.7m (2015: EUR 3.5m). Some of this remuneration was not accompanied by actual payments, however. A total of 52,128 performing share units are included for the Managing Board for 2016; the cash equivalent of this sum will be paid out in the 2020 fiscal year (29,575 units for the 2015 fiscal year for payment in 2019). The total remuneration paid out to the Managing Board was EUR 4.0m in the reporting year (2015: EUR 4.0m).

The following table corresponds to the sample tables recommended in the German Corporate Governance Code and differentiates according to payments which the members of the Managing Board have been granted for the fiscal year but which have not yet been paid out in full and payments which have actually been made.

The following payments were granted to the members of the Managing Board for the relevant fiscal year:

	Wolfgang Egger, CEO				
Payments granted in EUR k				**Joined: 21.08.2002 Appointed until: 30.06.2021**	
	2015	**2016**	**2016 (Min)**	**2016 (Max)**	**2015**
Fixed compensation	360	390	390	390	60
Fringe benefits	27 [1]	27 [1]	27 [1]	27 [1]	2 [1]
Total	**387**	**417**	**417**	**417**	**62**
One-year variable compensation	529 [2]	570 [3]	0	570 [4]	47 [2]
Multi-year variable compensation					–
Performing share units tranche 2017–2019	–	285 [3]	0	285 [4]	–
Performing share units tranche 2016–2018	264 [2]	–	–		23 [2]
Total	**1,180**	**1,272**	**417**	**1,272**	**132**
Pension expenses	12	12	12	12	1
Total compensation	1,192	1,284	429	1,284	133

1) The item primarily includes non-cash benefits arising from the provision of company cars and insurance premiums.

2) Granted in the 2016 calendar year for 2015 year once all criteria required for determining the variable compensation were known.

3) Corresponds to the liability posted for 150% target achievement (the exact amount will be defined in the outstanding settlement).

4) Corresponds to the maximum amount of variable compensation that can be achieved of 150%.

	Karim Bohn, CFO			Klaus Schmitt, COO			
	Joined: 01.11.2015 Appointed until: 31.10.2018			Joined: 01.01.2006 Appointed until: 31.12.2020			
	2016	**2016 (Min)**	**2016 (Max)**	**2015**	**2016**	**2016 (Min)**	**2016 (Max)**
	360	360	360	360	420	420	420
	11 [1]	11 [1]	11 [1]	13 [1]	13 [1]	13 [1]	13 [1]
	371	**371**	**371**	**373**	**433**	**433**	**433**
	420 [3]	0	420 [4]	540 [2]	600 [3]	0	600 [4]
	210 [3]	0	210 [4]	–	300 [3]	0	300 [4]
	–	–		270 [2]	–	–	
	1,001	**371**	**1,001**	**1,183**	**1,333**	**433**	**1,333**
	12	12	12	24	24	24	24
	1,013	383	1,013	1,207	1,357	457	1,357

The following payments were made to the members of the Managing Board in the relevant fiscal year:

Amount paid in EUR k	Wolfgang Egger, CEO Joined: 21.08.2002 Appointed until: 30.06.2021		Karim Bohn, CFO Joined: 01.11.2015 Appointed until: 31.10.2018		Klaus Schmitt, COO Joined: 01.01.2006 Appointed until: 31.12.2020	
	2015	2016	2015	2016	2015	2016
Fixed compensation	360	390	60	360	360	420
Fringe benefits	27 [1]	27 [1]	2 [1]	11 [1]	13 [1]	13 [1]
Total	**387**	**417**	**62**	**371**	**373**	**433**
One-year variable compensation	412	529	0	47	354	540
Multi-year variable compensation						
Performing share units tranche 2013–2015	-	-	-	-	-	782 [3]
Performing share units tranche 2012–2014					628 [2]	
Performing share units tranche 2014–2015	-	863 [3]	-	-	-	-
Performing share units tranche 2013–2014	388 [2]	-	-	-	-	-
Total	**1,187**	**1,809**	**62**	**418**	**1,355**	**1,755**
Pension expenses	12	12	1	12	24	24
Total compensation	1,199	1,821	63	430	1,379	1,779

1) The item primarily includes non-cash benefits arising from the provision of company cars and insurance premiums.

2) Amount paid out in 2015 after conversion of the performing share units tranche 2013–2014 and 2012–2014 at an average price of EUR 13.12425.

3) Amount paid out in 2016 after conversion of the performing share units tranche 2014–2015 and 2013–2015 at an average price of EUR 25.393.

Mr Arwed Fischer was granted in 2016 a total compensation in the amount of EUR 810,000 and received a total compenseation in the amount of EUR 1,431,000.

Compensation of the Supervisory Board

The compensation of the Supervisory Board is determined by resolution of the Annual General Meeting and in the Articles of Association. The Supervisory Board receives fixed compensation in line with the level customary in the market; this is paid to members in four equal instalments at the end of each quarter. No variable compensation is paid.

In view of the size of the Supervisory Board with three members, no committees were formed. Consequently, the committee remuneration recommended by the German Corporate Governance Code does not apply. If a Supervisory Board member was not a member for the entire fiscal year, he / she only receives the fixed compensation pro rata temporis. The members of the Supervisory Board also receive reimbursement for all their expenses as well as reimbursement for any value-added tax payable on their compensation and expenses.

The following payments were granted to the Supervisory Board in the 2016 fiscal year:

	Fixed compensation	
in EUR	2016	2015
Dr Theodor Seitz, Chairman	40,000	40,000
Alfred Hoschek (since 4 June 2015)	30,000	17,250
Gerhard Steck (since 1 July 2015)	30,000	15,000
Harald Boberg (until 25 June 2015)	0	15,000
Manfred J. Gottschaller (until 4 June 2015)	0	15,000
Total	**100,000**	**102,250**

3.3 Declaration on corporate governance – Disclosures in accordance with Article 289a HGB (German Commercial Code)

The Managing Board of PATRIZIA Immobilien AG issued a declaration on 23 January 2017 concerning corporate governance in accordance with Article 289a HGB and has made this available to the public on the Company's website www.patrizia.ag/investor-relations/corporate-governance/erklaerung-zur-unternehmensfuehrung.

www.patrizia.ag/investor-relations/corporate-governance/erklaerung-zur-unternehmensfuehrung

3.4 Transactions with related companies and individuals

The Managing Board submitted a dependent company report to the Supervisory Board, to which it adds the following final statement: "As the Managing Board of the Company, we hereby declare that to the best of our knowledge at the time when the legal transactions listed in the report on relationships with affiliated companies were carried out, the Company received appropriate consideration for each legal transaction. There were no measures taken during the fiscal year that require reporting."

Detailed information on business relationships with related companies and individuals can be found in the Notes to the Consolidated Financial Statements under item 9.3.

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4 SUPPLEMENTARY REPORT

Appointment of a new Managing Board Member

Effective 17 April 2017, the Managing Board appointed Anne Kavanagh as the Chief Investment Officer (CIO) and fourth member of the Managing Board. Going forward, Anne Kavanagh will, in this role, be responsible in particular for all the investment activities of the Group.

5 DEVELOPMENT OF OPPORTUNITIES AND RISKS

5.1 Management of opportunities and risks

The group-wide risk management system ensures that internal and external opportunities and risks are systematically captured, assessed, controlled, monitored and communicated. Our aim is to obtain information on risks and opportunities and their financial implications at an early stage and to manage them in such a way that the long-term value of the company is sustainably safe and can increase. The Managing Board of PATRIZIA Immobilien AG bears overall responsibility. The responsibility for monitoring and developing the risk management system lies with the risk management working group, which consists of employees drawn from operational areas as well as the Controlling and Investor Relations departments.

Opportunity management is performed independently of risk management. The Transactions and Alternative Investments departments monitor the market for attractive investment opportunities together with the Country Heads. The Product Development and Institutional Clients departments develop new products and structures for our clients. Strategic growth opportunities are identified and consistently pursued by PATRIZIA's Strategy Committee. PATRIZIA's asset management companies each maintain a risk management system focusing on the real estate special funds that they manage and in order to ensure compliance with supervisory requirements. The risks and opportunities that PATRIZIA identifies and communicates at an early stage – defined as negative / positive deviations from planned figures – pass through the further management process. This is ensured through the regular jour fixe session of the Managing Board and of the Cooperation Committee, which is made up of all Country Heads, Group Heads, Operational Group Heads and the COO.

The Group Controlling reports provide a regular and reliable information base for managing opportunities and risks. The value drivers for each area of responsibility are subjected to a monthly target-actual analysis in order to identify undesirable developments at an early stage and to take appropriate measures. Identified opportunities and risks are integrated into the regular planning and forecasting processes. Risks are evaluated on the basis of the probability of their occurrence and the magnitude of potential damage and are summarised at Group level. We use this information to develop the required course of action and to limit their impact through operational measures and, where necessary, through financial precautions such as accruals. The analysis generally covers the period of our corporate planning but can also be extended beyond this in the event of significant strategic risks.

The efficiency and effectiveness of the risk management system are assessed once a year in an internal risk audit. The results are set out in a risk report, which presents all risks, operational measures and responsibilities that were previously examined by the departments in charge. In addition to the Managing Board, the relevant contacts of the business functions are informed of the risk inventory's results. In addition, the early risk detection system is examined by the auditor in accordance with Article 317 (4) of the German Commercial Code (HGB).

5.2 Internal control and risk management system with regard to the reporting process – disclosures in accordance with Article 289 (5) and Article 315 (2) No. 5 of the German Commercial Code (HGB)

The risks relating to accounting and financial reporting are that our annual financial statements and interim financial statements could contain incorrect presentations. In order to avoid sources of error, PATRIZIA Immobilien AG has established an internal control system (ICS) for its accounting process. It ensures sufficient security for the reliability of its financial reporting and preparation of its annual and quarterly reports. Nevertheless, the ICS cannot provide absolute security. The members of PATRIZIA Immobilien AG's Managing Board sign the declaration of legal representatives each quarter. In doing so, they confirm that accounting standards have been complied with and that the figures represent the actual net assets, financial position and result of operations. The starting point for the ICS is the projection based on the targets set by the Managing Board and the planning of the operative business development. This planning provides budgetary values for the coming fiscal year and budget figures for the following fiscal year for each company and each cost centre. Differences between the actual and target figures are determined and analysed on a monthly basis. Revised forecasts for the current fiscal year are prepared on an ongoing basis based on actual values already booked as well as the identified risks and opportunities and open budget values.

The ICS includes all measures and processes to ensure that all business transactions are entered quickly into the bookkeeping and financial statements. It examines the effect of amendments to laws and accounting standards and the preparation of financial statements. Systematic implementation of the four eyes principle ensures compliance with legal regulations in accounting processes. The separation of functions and authorisation regulations, which are reinforced by standardised control and coordination processes, form the basis of the ICS. All authorisations are documented and subject to system-based archiving.

The accounting for all operational and property holding companies in Germany is located centrally within PATRIZIA Immobilien AG. Accounting for companies located abroad is generally performed by the national company. The basis for accounting is provided by group-wide standards within a central IT environment, which is mainly based on SAP. The Group Accounting department performs the consolidation required to produce the consolidated financial statements centrally. Employees involved in the preparation of the annual financial statements are appropriately trained, and the responsibilities and controls for preparing the annual financial statements are clearly defined.

The effectiveness of our accounting-related ICS is evaluated as part of the final reporting procedures and examined by our auditor as part of its auditing remit.

5.3 Important categories of opportunity and risk

5.3.1 Market risks

Opportunities and risks arising from macroeconomic developments: The European real estate investment market is characterised by high demand, which is expected to continue due to a lack of alternative investments and favourable terms of financing. This high demand is accompanied by a lack of available investments, especially in the top European locations, increasingly making B and C locations the investment focus. Comprehensive knowledge of local conditions is essential for an investment in these locations. Due to its presence in the individual European markets and its extensive knowledge of regional markets, PATRIZIA is able to offer such knowledge, meet the high demand with its comprehensive product portfolio and optimise these through acquisitions and divestitures as well as development projects. The consequences of BREXIT and the political uncertainties in the

Netherlands, France, Germany and Italy might curb positive economic development of the Eurozone. This, in turn, could further increase demand for real estate as a safe asset class. Currently, we do not see any substantial weakening risk in PATRIZIA's development in the medium term.

Residential real estate market: Even though the market in urban areas has responded to the existing shortages with increased construction activity, there continues to be excess demand, which is expected to continue in 2017 as well. This should lead to increasing rent, even though some rent increases have been restricted by regulatory measures. The European home price index steadily increased in 2016. For investors seeking to diversify their portofolio, residential real estate continues to be of great interest. Consequently, real estate available for sale, particularly at top locations, should remain scarce. An increased move to B and C locations will probably follow suit. Such locations, however, require outstanding expertise in market-determining factors as well as an active portfolio management.

Commercial real estate market: We expect the positive economic development in the Eurozone and the related decrease of unemployment figures as well as robust private consumption to continue to ensure a stable demand for office, retail and logistics properties in 2017 as well. Additional growth in rents and a positive growth in value may ensue. The extent of investment activities will mainly be determined by product availability, which has decreased significantly over the past few years, particularly at top locations. B and C locations will become increasingly interesting to investors. We will be able to see increases in rent particularly in the top locations, and also in the secondary locations. The yields will remain under pressure, and additional yield compressions are likely.

Competitive environment: There continues to be high demand for indirect real estate investment opportunities. PATRIZIA fully implemented the Alternative Investment Fund Managers Directive (AIFMD) in 2015. The new structure allows cross-border synergies to be leveraged across all classes of product. In addition to expanding the local AIFM platforms for professional investors in Germany, Luxembourg, the United Kingdom and Denmark, PATRIZIA was able to successfully place its products pertaining to the newly established area for the issuance of closed products for private clients at the beginning of last year. Using its established country platforms in Germany, the Nordic region, the United Kingdom and Ireland, France, Spain, and Portugal as well as Luxembourg and the Netherlands, PATRIZIA will expand its product and service range and increasingly acquire international investments. As a consequence, the number of staff working for the Institutional Clients segment has been increased, especially in order to now also look after the markets in Southern Europe, North America and Australia. Due to the successful sale of the Property Management segment, PATRIZIA was able to achieve a stronger focus on its core competencies in the Management Services segment, whose synergies are expected in the coming years. Clients are attaching increasing importance to outstanding management quality at competitive prices. PATRIZIA considers itself well-positioned in this respect.

Long-term investment contracts: Steady income flows result from a large number of long-term investment contracts, concluded for a fixed term. For this reason, the loss of a single mandate – even through the disposal of a portfolio – is not associated with any substantial risk, rather more being a part of our business model.

5.3.2 Business risks

Purchase and sale of real estate: The persistent trend toward strong demand for real estate continued in 2016. In an uninterrupted environment of loose monetary policy, international investors continued to invest in European real estate markets. The transaction volume is once again very high, which is consistent with the volume of previous years. Therefore, it is still a challenge to acquire suitable properties for our clients with risk-adjusted yields in a very competitive market.

Even in this market environment, PATRIZIA was able to use its experience and market know-how to acquire attractive properties and portfolios for its clients, sometimes by approaching sellers directly in order to avoid competitive situations and to thus provide its investors in this market environment with the ability to make profits and optimise their portfolios through target-ed sales.

The continued strategic development of PATRIZIA's European platforms facilitate an additional broadly positioned access to attractive investment opportunities. This makes PATRIZIA a reliable and professional partner throughout Europe in the reliable and fast realisation of major individual investments and portfolios.

In spite of this seller's market, the risk remains that the sale of assets held by PATRIZIA may not be executed at the intended price.

Employees: The skills and motivation of PATRIZIA's employees are essential for success. Through our employees, we gain the trust of our investors, tenants, business partners and shareholders and are thus able to establish long-term business relationships. We endeavour to retain qualified staff over the long term. We use personnel development measures, deputising rules and early succession planning in an attempt to reduce the risk of staff turnover and loss of knowledge and in order to fill management positions internally. Furthermore, the recruitment of new employees, especially during the period of growth, is vital for PATRIZIA's successful future development.

For further information, please refer to the section on Employees under item 1.5.

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IT security: Almost all our essential business processes are supported by IT systems. Any fault in the operation of the IT systems affects our business activities. A substantial loss of data could lead to serious financial losses and also adversely affect public perceptions of the Company. Virtually all systems have been operated redundantly in two physically separate computer centres since 2015 in order to always ensure the availability of business applications. In addition, the ERP (Enterprise Resource Planning) systems are operated in parallel on a mirrored basis. These two measures guarantee a significant reduction in downtimes in the event of an emergen-cy. Additional security measures such as the introduction of a NAC solution (Network Access Control) as well as additional anti-malware mechanisms reduce the risk of damage caused by viruses, Trojan horses and ransomware. Data backups are performed on a regular basis in order to prevent the technical loss of company data and to ensure the reliability of IT operations. A password policy also ensures that access passwords are changed regularly.

Financing risks: Borrowing is not essential for PATRIZIA's business model as a Group, but it is essential for the operating business. The Company's own managed real estate (principal investments) is no longer financed with external financing. The risk of external financing not being available to PATRIZIA Immobilien AG for potentially new principal investments is currently extremely low. One of the two EUR 35m bonds taken out in 2013 was repaid as scheduled in June 2016. The other bond with a remaining balance of EUR 27m is scheduled for repayment in June 2018. At 2 January 2017, another unscheduled repayment was made in the amount of EUR 5m. Along with significant liquidity, PATRIZIA is in a position to respond to the capital requirements of new investments at any time. At 31 December 2016, EUR 53.2m were included in the item for short-term bank loans. The loans must be attributed to the companies of PATRIZIA GrundInvest KVG and finance assets that are to be placed as public funds in the short- to medium-term. PATRIZIA also procures external capital as part of its service under co-investments and funds.

Credit terms: Due to the sale of the principal investment "Harald" and "First Street" in Manchester and the respective repayment of the loans, there are no more credit terms and thus no more corresponding risks. Some of the loan agreements pertaining to the property and portfolio financing of co-investments and third-party transactions require compliance with indicators, whose compliance is constantly monitored. There are no direct effects for PATRIZIA resulting from this.

Interest risks: There are no interest rate risks for PATRIZIA, since it no longer has any bank loans and since the bond as well as the long-term loans of PATRIZIA GrundInvest carry a fixed interest rate.

Liquidity risk: There is currently no indication of a possible liquidity shortage. At 31 December 2016, bank balances and cashs on hand amounting to EUR 440.2m were available to PATRIZIA in order to cover its operating liquidity and financing requirements. Moreover, we expect further cash surpluses from operating business that will be used for investment planning in matching periods. The equity released through sales is also increasing existing liquidity. PATRIZIA optimises and manages liquidity by means of cash pooling. Early warning indicators and comprehensive continuous liquidity planning also serve to prevent risks and to ensure that an unexpected liquidity requirement can be serviced.

Exchange risk: Most of the Group's subsidiaries and real estate companies are located in countries of the European Monetary Union, where there is no currency risk. The exceptions are the the international offices in Denmark, Sweden and the United Kingdom, which exercise asset management mandates and perform purchases and sales on behalf of funds and invest within the context of co-investments. PATRIZIA had approximately EUR 94m invested in foreign currency at the reporting date. Since the participating interests in these companies and the granting of shareholder loans are effected in the respective national currency, the subsidiaries and real estate holding companies are subject to the risk of changing exchange rates. This position may increase with continuing expansion in Europe outside the Eurozone. In addition, the Group's entire exchange risk is monitored and measured on a regular basis in order to immediately identify actions that may need to be taken and to initiate countermeasures. In the past fiscal year, expected sales proceeds in British Pound were, for example, hedged against exchange risks.

Legal risks: PATRIZIA is present in different legal systems. As a result of their business operations, individual companies may be involved in various litigation and arbitration proceedings. Out-of-court claims are also occasionally asserted against them. We aim to minimise any legal risks by monitoring our contractual obligations and involving internal and external legal experts in contractual matters. We have booked accruals for potential losses from pending cases. In some cases, the claims asserted against us are significantly higher than the amount of the corresponding accruals. Based on an extensive legal assessment, we consider these claims to be unfounded. No contractual risks exist with regard to co-investments, e.g. in respect of the social clauses, since these only affect non-consolidated subsidiaries. The investment contracts do not reveal any substantive contractual risks either.

5.3.3 Partners risks

Third parties: With regard to special real estate funds, opportunities and risks result from income from fees that depend on managed real estate assets, on purchases and sales and on the returns achieved. This income can be negatively affected by a decline in the value of real estate, rent losses and a reduced transaction volume. However, PATRIZIA operates a large number of different funds and is able to access a diverse supply of suitable properties in Germany and other countries. Since the properties held in special funds have to be backed by equity, borrowing in this constellation can be obtained quickly and on favourable terms. Generally, we do not expect a lower level of investment activity in the future. We consider the risk of a decrease in planned dividend payments to investors to be very slight. On the contrary, we see an opportunity for acquiring new clients and expanding our fund business based on the performance of the funds and PATRIZIA's reputation. Additional opportunities arise by introducing closed-end real estate funds to private investors. We will be using these public investment funds to make properties with a market value of between EUR 50–150m accessible that will appeal to private investors particularly because of their size. As an asset manager, PATRIZIA is also responsible for managing and optimising third-party properties. Poor service could lead to dissatisfaction of the respective clients or to financial claims that might extend to the loss of contracts and an impact on the Group's earnings situation. We assume a very low probability of this happening in 2017 with, at most, negligible financial consequences.

Co-investments: PATRIZIA participates in projects through co-investments. Acquiring clients, and with them the necessary equity, does not constitute any real limiting factor. We do not consider securing financing to be a risk, either. As already explained under "Purchases and sales of real estate", the challenge tends to lie in acquiring suitable real estate that meets the criteria defined by PATRIZIA and investors.

Raising equity capital: We do not see any risk of a shortage of business partners / investors or problems in acquiring new business partners / investors owing to the high level of liquidity on the investor side combined with the pressure to invest and the lack of investment alternatives. Extending co-investment and fund business activity increases PATRIZIA's dependence on institutional clients, which could put pressure on our margins. This risk is offset by our sales strategy, which also involves addressing additional, in particular foreign, investors. Over 200 institutional investors – from savings banks and insurance companies to pension funds and sovereign wealth funds – now invest via PATRIZIA. Over 50% of the investors have invested in several PATRIZIA products.

5.4 Overall assessment of opportunities and risks

Risk management at PATRIZIA is a process which records risk positions, identifies changes in risk and defines appropriate actions. In 2016, like in previous years, PATRIZIA examined the evaluation categories for the potential magnitude of damage of all known risks and increased or reduced them as necessary.

The risk management system illustrated here enables PATRIZIA to counteract risks at an early stage and to exploit the opportunities that present themselves. Considering all individual risks and a possible cumulative effect, PATRIZIA's overall risk is limited at present. No significant risks to the future development, or even the continued existence, of the Company and the Group have been identified based on our current knowledge and medium-term planning.

6 REPORT ON EXPECTED DEVELOPMENTS

6.1 Future economic framework

Source: PATRIZIA Research

Macroeconomic development: Due to the solid overall economic situation, we expect the labour markets to improve further in 2017. Due to the European Central Bank's decision to extend the bond purchase programme until the end of 2017, we expect interest rates in Europe to remain at a low level. Increasing oil prices already caused inflation to increase at the end of 2016, and we expect this trend to continue in 2017. Some of the potential economic consequences of the Trump presidency, political uncertainties in the Netherlands, France, Germany and Italy, and the BREXIT negotiations, are issues that could lead to some unrest in 2017 in the financial markets, which should prompt further growth in demand for less risky assets such as real estate among institutional and private investors.

Source: PATRIZIA Research

Develoment on the Euroepan real estate market: The favourable development on residential and commercial real estate markets, especially in European metropolitan regions, should continue in 2017. Taking into consideration the lack of supply in the top locations, investors will increasingly have to divert to B and C locations. Values should develop positively in 2017 as well because financing terms are still favourable and the interest of investors in real estate investements should remain high. Taking into consideration this situation, the limited availability of product in particular will be a challenge.

6.2 Expected development of the earnings situation and assumptions concerning achievement of targets in 2017

6.2.1 The Group in general

EUR bn
2.0
growth in assets under management expected in 2017

The outlook for the 2017 fiscal year is very positive. Due to the foreseeable transfers of portfolios and properties based on contracts already concluded, 2017 is again expected to result in an increase of assets under management and therefore a further increase and stabilisation of fees generated by Investment Management Services in 2017. Another increase of EUR 2bn is anticipated from assets under management.

PATRIZIA therefore expects further sustainable growth in earnings as expressed by the operating result. The operating result for 2017 is expected to range between EUR 60–75m following a comparable adjusted operating result of EUR 72.2m in 2016. Taking into account the earnings from the

Harald portfolio, the operating result for the past year is EUR 283.2m. It should be noted that transaction-related taxes and minority shares were already deducted from the operating result for 2016.

	Last forecast 2016	Actual figures 2016	Adjusted operating result 2016	Forecast 2017
Assets under management	Growth of EUR 2bn	Growth of EUR 2bn	Growth of EUR 2bn	Further growth of EUR 2bn
Operating result	At least EUR 265m [1]	EUR 283.2m [1]	EUR 72.2m	Between EUR 60–75m

1) Please refer to the explanation of the forecast above for details concerning the definition of the operating result

Operating result

The projected operating result for 2017 ranges from EUR 60–75m.

Below, we have explained the assumptions and expectations on which the projected operating result is based.

PATRIZIA intends to further increase the assets under management and, based on an average inventory of the managed real estate assets of between EUR 19.5bn and EUR 20.5bn, expects asset management fee income from between EUR 89.5m and EUR 91.5m. Compared to 2016, the asset management fee income remains stable, even though the sale of the Property Management business resulted in the loss of a fee volume of approximately EUR 10m.

Assuming a continued active transaction market in 2017, the Company is expecting transaction-related fees of between EUR 55–65m based on a transaction volume of between EUR 4.0bn and EUR 5.5bn.

Income from perfromance fees is determined by the generated yields that exceed the agreed-upon target yields. These result in particular from the performance of value-increasing measures as well as sales. For the year 2017, PATRIZIA expects to generate perfromance fees in the amount of EUR 29–38m.

The projected fees from the service business add up to a total income of between EUR 173.5-194.5m. In addition, the Company expects net income from the sale of its own assets and co-investments of approximately EUR 39m.

PATRIZIA projects operating costs, which mostly consist of personnel and material costs, in the amount of between EUR 148–153m. Compared to 2016, operating costs will slightly increase because global fundraising activities are to be expanded and, due to inflation, the cost of personnel is expected to slightly increase.

EUR m
60–75
anticipated operating income for 2017

Over the course of the year, we will update these projections in consideration with the development of operations.

Assets under management

For 2017, another net growth by approximately EUR 2bn to what would then be EUR 20.6bn is expected. In addition to continued strong demand from German private and institutional investors, the Company is expecting additional transactions with international investors. Having contacted new potential investors outside of Germany and Europe in the past few years, this contact will be intensified by a team whose structure and staffing has been increased. To this purpose, offices have already been established in the United States and Australia, and additional offices, for example in Asia, are to follow.

EUR bn
2.1
Transactions have been signed for complettion mainly in 2017

Furthermore, transactions in excess of EUR 2.1bn have already been contractually agreed upon. EUR 1.7bn of these are purchases, and EUR 0.4bn are sales, most of which are to be completed in 2017.

6.3 Expected development of net assets and financial situation

Following the closing of the Harald sale, PATRIZIA basically has only marginal liabilities to banks. It only finances interim financing for closed private investor funds in the short term. The current forecast does not contain on the basis of a reasonable commercial assessment any assumptions relating to noteworthy investments of the existing cash on hand either.

6.4 Dividend policy

10:1
subscription ratio for "bonus shares"

For the past 2016 fiscal year, the Managing Board and the Supervisory Board of PATRIZIA Immobilien AG propose that the retained earnings of EUR 181.0m be fully carried forward to the new account. As in previous years, a capital increase from company funds will be used to issue new shares to shareholders in a ratio of 10:1. On the one hand, the increased number of shares will increase the liquidity of the company's shares, and on the other hand PATRIZIA can, as in the past, use the liquid funds to exploit investment opportunities which arise. The shareholders will not be required to make any contribution. The retained liquid funds are to be used for co-investments and to expand European activities, and, if applicable, to take over another complementary asset manager. The objective is each time to contribute to PATRIZIA's sustainable, long-term growth.

If the Annual General Meeting of PATRIZIA Immobilien AG to be held on 22 June 2017 agrees to the measure, the capital increase will be effected by issuing 8,395,588 new registered no-par value shares. This measure will not affect the amount of total equity since it simply involves a transfer from retained earnings to subscribed capital. The share capital will increase from a current total of EUR 83,955,887 to EUR 92,351,475, divided into the same number of no-par value shares. The new shares will carry dividend rights from the beginning of the 2017 fiscal year.

6.5 General statement of the Company's management of prospects for 2017

PATRIZIA will continue its highly successful development in 2017. Institutional and private investors are increasingly taking advantage the Europe-wide presence of PATRIZIA as an independent real estate investment manager. We continue to intensively expand this position, for example through the addition of another internationally experienced Managing Board member. This will be reflected in assets under management, which are again anticipated to rise by EUR 2.0bn in 2017, thereby increasing income from fees and generating an operating result between EUR 60–75m.

The outlook for 2017 and statements about subsequent years include all the events that were known at the time the consolidated financial statements were prepared and that could influence the business performance of PATRIZIA.

Augsburg, 13 March 2017

WOLFGANG EGGER	KARIM BOHN	KLAUS SCHMITT
CEO	CFO	COO

This report contains specific forward-looking statements that relate in particular to the business development of PATRIZIA and the general economic and regulatory environment and other factors to which PATRIZIA is exposed. These forward-looking statements are based on current estimates and assumptions by the Company made in good faith, and are subject to various risks and uncertainties that could render a forward-looking estimate or statement inaccurate or cause actual results to differ from the results currently expected.