IKB Deutsche Industriebank AG Restated Financial Statements and Management Report 2006/2007

This report substitutes the Financial Statements and Management Report of IKB Deutsche Industriebank AG 2006/07, disclosed for the first time at 28 June 2007

IKB

Deutsche Industriebank

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Président du Directoire
Euler Hermes

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(Chairman of the Board of Managing Directors
from 29 July 2007)

Frank Braunsfeld (until 15 October 2007)

Dr. Volker Doberanzke (until 7 August 2007)

Dr. Dieter Glüder (from 29 July 2007)

Dr. Reinhard Grzesik (from 15 October 2007)

Dr. Markus Guthoff (until 15 October 2007)

Claus Momburg

Joachim Neupel (until 31 December 2006)

Stefan Ortseifen (until 29 July 2007)

Frank Schönherr (until 30 November 2006)

Restated Management Report of IKB Deutsche Industriebank AG

1. Report on Material Events after the Reporting Date

On 27 July 2007 IKB found itself exposed to a crisis that threatened its very existence, sparked off by the developments on the US sub-prime mortgage market. It took a comprehensive rescue package put together by the KfW Banking Group and three German banking associations (BdB, BVR, DSGV) to secure the Bank's continued existence.

We have listed key events since the outbreak of the crisis in the following table:

Overview of the crisis and key events

27 July 2007	Because of the threat that IKB's liquidity facilities for the Rhineland Finding conduit would be drawn upon, other banks duly froze their credit facilities made available to IKB
28/29 July 2007	IKB together with KfW, three associations of the German banking industry and BaFin put together a comprehensive risk shield
29 July 2007	Supervisory Board meeting: risk shield discussed, Stefan Ortseifen was unanimously removed from office and Dr. Bräunig and Dr. Glüder were appointed to the Board of Managing Directors
1 August 2007	PricewaterhouseCoopers Aktiengesellschaft Wirtschaftsprüfungsgesellschaft (PwC) was commissioned to carry out a comprehensive agreed upon procedures
2 August 2007	The Annual General Meeting for the 2006/07 financial year originally scheduled for 30 August 2007 was postponed
7 August 2007	Supervisory Board meeting: resignation of Dr Doberanzke from office; proposal that no dividend be paid for the 2006/07 financial year
3 September 2007	Forecast for the full year amended with significant losses expected for the 2007/08 financial year
15 October 2007	PwC submits report of the agreed upon procedures Supervisory Board meeting: unanimous approval of the resignation of Dr Guthoff, removal of Frank Braunsfeld from and appointment of Dr. Grzesik to the Board of Managing Directors Resolution by the Board of Managing Directors to amend and restate IKB's 2006/07 consolidated financial statements
29 November 2007	Postponement of the publication of the interim report for the first half of the 2007/08 financial year, which was originally scheduled for 30 November 2007
30 November 2007	Extension of the risk shield announced
7 January 2008	Resolution of the Board of Managing Directors, with approval by the Supervisory Board, to issue a mandatory convertible bond to be subscribed to (and subsequently converted) by KfW; Resolution of the Board of Managing Directors to amend the single-entity financial statements of IKB for the 2006/07 financial year
9 January 2008	Further risks from the Rhineland Funding conduit assumed by KfW and additional banks with legal effect (as announced on 30 November)
13 February 2008	Further package of measures required as a result of the revaluation of on-balance sheet portfolio investments
16 February 2008	Supervisory Board meeting: restated financial statements of 31 March 2007 reviewed and confirmed

Given the impact this crisis has had on the Bank's existence, we will outline below the business activities that triggered the crisis together with the rescue operation provided by the banking pool and further developments, bringing us up to the present situation. This will be followed directly by a preview of the Bank's future developments.

Portfolio investments as an element of the business strategy

In 2001, IKB started to invest increasingly in securities that were collateralised by specific credit portfolios of different asset classes (mainly asset-backed securities – ABS and collateralised debt obligations – CDOs). This type of security can also be linked to a portfolio of credit derivatives or be backed by a portfolio of ABS tranches (CDOs of ABS). Credit derivatives also exposed IKB to comparable risks. These financial instruments are compiled under the term portfolio investments. The aim behind these investments was to improve the Bank's risk/reward structure. Portfolio investments generated a clear increase in income in the past.

The investments were focused in particular on highly diversified loan-based portfolios, such as company loans, credit card receivables, a wide variety of mortgage loan receivables, and also car loans. The regional focus was on the USA. IKB took these investments on its own balance sheet.

The volume of on-balance sheet portfolio investments made directly by the Bank amounted to € 6.8 billion as at 31 March 2007. At this time, 73% of the portfolio comprised triple-A and double-A rated investments. The investment grade share was 98%. US investments accounted for roughly two thirds of the portfolio's underlying, with Europe making up the other third. A detailed illustration of the on-balance sheet portfolio investments can be found in the Risk Report.

Advising and financing the Rhineland Funding and Rhinebridge special purpose vehicles

IKB also initiated the launch in 2002 of the Rhineland Funding conduit (Rhineland Funding), comprising Rhineland Funding Capital Corporation LLC, Delaware, ("RFCC") plus various purchasing entities with registered offices in Jersey and Delaware that have been established since then. IKB acted as advisor for RFCC and the purchasing entities. The legally independent special purpose vehicles invested in similar financial instruments, in terms of both the underlying credit portfolios and the ratings. They were financed on a continuous basis by the issue of commercial paper. IKB and other banks also extended considerable liquidity facilities. In December 2006, IKB AG transferred the advisory services to the newly-established group subsidiary IKB Credit Asset Management GmbH (IKB CAM).

As at 31 March 2007, the investment portfolio of all Rhineland Funding purchasing entities amounted to € 12.7 billion, of which € 11.4 billion was consolidated in the restated consolidated financial statements as at 31 March 2007. The share of investment grade investments was 99.8%. A detailed illustration of Rhineland Funding can be found in the Risk Report.

The securities in the Rhineland Funding purchasing entities had and still have medium to long-term maturities. Refinancing was carried out centrally via RFCC by taking up short-term funding in the form of so-called asset-backed commercial paper (ABCP) with the best short-term rating. The ABCP had short maturities of just a few months in each case and could therefore be regularly replaced with new issues. To this extent, there was a form of maturity arbitrage within the conduit between medium to long-term assets and short-term refinancing with the corresponding margin benefits regarding the funding costs. Interest rate risks were generally neutralised through interest rate hedges.

To cover the risk of follow-on financing for the ABCP investor in particular, banks had provided Rhineland Funding with liquidity facilities, to cover any market disruptions. The ABCP market was seldom subject to disruptions in the past, and when these occurred, they were only short-term in nature. The last significant market disruption, which dates back to 11 September 2001, lasted only a few days.

IKB itself had provided Rhineland Funding with liquidity facilities in the amount of € 8.1 billion as at 31 July 2007. Negotiations on the placement of parts of IKB's liquidity facilities were about to be concluded in July 2007.

Prior to this, comparable liquidity facilities were made available by additional banks in the course of the sharp growth of Rhineland Funding; these comprised in particular USD 4 billion in August 2006, with a further USD 2.5 billion to follow in June 2007. The special purpose vehicles Havenrock I and II were set up in connection with the provision of these liquidity facilities. These companies secured 25% on the liquidity risks for these liquidity providers together with their entire credit risk arising in the event that the liquidity facilities are drawn upon. IKB in turn, provided the Havenrock companies with a liquidity facility to cover their entire liquidity risk (25% of USD 6.5 billion). On the other hand, IKB assumed the credit risk of the Havenrock companies in a range between 0.06% and 25.00% (25% of USD 6.5 billion).

In late June 2007, a further special purpose vehicle, Rhinebridge, took over a portfolio from the IKB balance sheet that had been built up to the required size and refinanced it on the capital market by issuing capital notes and commercial paper. The London branch of IKB CAM acted as portfolio manager for Rhinebridge. As at the end of June 2007, Rhinebridge had an asset volume of USD 2.4 billion.

Unlike Rhineland Funding, this special purpose vehicle, rather than relying solely on commercial paper, was also capitalised/refinanced over the longer term using capital notes in the amount of USD 280 million. IKB's own share in these notes was € 149 million. In addition, commercial paper was issued in the amount of USD 2.2 billion. With effect from 21 July 2007, Rhinebridge also had access to liquidity facilities worth USD 0.2 billion from two banks. As at 30 June 2007, 82 % of the assets were rated AAA, 14% AA and 4% A.

Factors that triggered the crisis

The crisis was triggered by stagnating and falling real estate prices in the USA, especially due to the rise in interest rates. Doubts were also growing about credit issuing practices on the US mortgage market for sub-prime borrowers, with a dramatic rise expected in payment problems and far higher final losses than previously expected.

By the middle of July 2007 the credit rating agencies had begun to place the ratings of credit portfolios that contained sub-prime risks on credit watch. Within a short space of time, a huge crisis of confidence hit the capital market among investors in the asset backed commercial paper market. Owing to the high sub-prime share in its portfolios, there was an increasing risk that Rhineland Funding would no longer be able to guarantee its refinancing in the long term. The capital and banking market therefore predicted that IKB's liquidity facilities would be drawing upon substantially, thus exposing it to considerable sub-prime credit risks. Consequently, the other banks questioned the creditworthiness of IKB and terminated their credit facilities.

Stabilisation of Rhineland Funding and the special purpose vehicle Rhinebridge

Following this crisis weekend, IKB together with KfW drew up a blueprint to stabilise Rhineland Funding's weakened refinancing base to such an extent and until such time as the special purpose vehicle would not become insolvent owing to, amongst other things, the default of commercial paper (CP). This would have had immeasurable consequences within the short timeframe involved – going as far as forced liquidation. Initially, IKB and KfW stabilised Rhineland Funding through the purchase of CPs, thus preparing and successfully implementing the orderly process of refinancing through available liquidity facilities. The latter scenario was aimed for, as soon as it was evident to all parties involved from the joint assessment that the CP market was expected to dry up for quite some time.

For the same reasons, IKB adopted a similar approach to Rhinebridge, which had been launched on the capital market only shortly before the crisis erupted. IKB in its own interests was able to stabilise this special purpose vehicle through the purchase of capital notes and CPs to such an extent that it could independently reduce its portfolio in an orderly and careful manner, thus avoiding the forced sale of the portfolio with the attendant high losses.

Risk shield and additional package of measures

To avoid a moratorium of IKB, a rescue package (risk shield) was put together during the weekend of 27 to 29 July 2007 by KfW Banking Group (KfW) together with the BaFin, the Bundesbank, the Federal Finance Ministry and three associations of the German banking industry (BdB, BVR and DSGV).

In this context, KfW assumed IKB's financial obligations under the liquidity facilities of € 8.1 billion granted to Rhineland Funding with effect from 30 July 2007.

Additionally, with effect from 30 July 2007 and again on 9 January 2008, IKB's risk exposure to Havenrock I and II was largely covered. The shield also includes the issue of a € 54.3 million convertible bond on 7 January 2008 which, subject to the exclusion of the subscription right, was subscribed in full by KfW Banking Group. This amount secured the residual credit risk exposure of IKB from Havenrock I and II.

Out of this overall on-balance sheet portfolio, a nominal amount of € 3.3 billion was held in securities with sub-prime risks (including Rhinebridge capital notes), in securities subject to expected strong market price fluctuation, and in securities that were extremely vulnerable to default (so-called first loss pieces in particular). The banking pool has committed to assume the first loss pieces for this portfolio, up to an amount of € 1 billion.

In February 2008 – following a significant deterioration in market conditions – this cover turned out to be insufficient. Using newly-developed valuation models for IKB's on-balance sheet portfolio investments, the Board of Managing Directors envisages additional mark-to-market losses, in excess of the existing risk shield, of approx. € 950 million.

Of these valuation losses, expected to amount to approx. € 950 million, the lion's share of approx. € 630 million is attributable to the € 3.1 billion sub-portfolio (size as at February 2008) comprising assets exposed to particularly high default risk – in particular, securities exposed to strong market fluctuations and sub-prime components, and so-called first-loss pieces.

This partial amount of € 630 million exceeds the € 1.0 billion risk shield provided by KfW and the pool of banks for first losses on the sub-portfolio referred to above. Given the prevailing market situation, a portfolio sale would likely involve more sizeable discounts.

IKB expects a valuation loss of approx. € 320 million for approx. € 2.8 billion of portfolio investments outside this risk shield, which are generally exposed to lower risk.

The portfolio investments were revalued through a mark-to-model approach, using customised models designed particularly for IKB in order to map its structured portfolio investments, most of which are very complex. The methods used are based on the principles set out in the position paper published by the Institute of Public Auditors in Germany (IDW) on accounting issues related to the sub-prime crisis.

As a consequence, a further package was agreed upon, which consists of the following elements in particular:

Firstly, a proposal will be submitted to the ordinary shareholders' meeting of IKB AG on 27 March 2008 to pass a resolution to increase the company's capital by up to € 1,486,765,992.96, against cash contributions and with a 6-for-1 subscription right for existing shareholders. KfW has committed to BaFin to ensure that a sufficient quantity of new IKB shares will be subscribed to or purchased under the capital increase that IKB will obtain fresh funds in a minimum amount of € 1.250 billion (excluding costs).

Furthermore, KfW has undertaken, vis-à-vis BaFin, to boost IKB's regulatory tier 1 capital by € 600 million until 19 February 2008, by way of an "additional capital contribution" pursuant to section 272 (2) no. 4 of the HGB, to be recognised in the capital reserve. The contractual details governing this contribution will be determined at short notice; they may include a debtor warrant (Besserungsabrede) which may burden the annual results of future periods.

The disposal of major parts of IKB's portfolio investments is planned as a further component of the restructuring package.

Findings of the agreed upon procedures carried out by PwC

On 1 August 2007, PricewaterhouseCoopers Aktiengesellschaft Wirtschaftsprüfungsgesellschaft (PwC) was commissioned with the task of carrying out a comprehensive agreed upon procedures. The findings of the agreed upon procedures were submitted on 15 October 2007. The newly appointed members of the Board of Managing Directors were in regular dialogue with PwC on the issues being reviewed even while the agreed upon procedures was being prepared.

Main topics of the agreed upon procedures

Within the scope of the agreed upon procedures, PwC determined the risk situation of the IKB Group. The auditors also analysed how the Bank's risk-bearing capacity could be compromised by Rhineland Funding to such an extent that it threatened the Bank's existence. It also assessed IKB's accounting policies, and evaluated the appropriateness of risk management and control processes, taking into account the Bank's wholly-owned subsidiary IKB Credit Asset Management GmbH (IKB CAM). Furthermore, PwC were asked to investigate whether the Supervisory Board was informed sufficiently and accurately by the Board of Managing Directors of the Bank's risk exposure.

Results and consequences of the agreed upon procedures for the Bank's risk management

A central issue identified by PwC's audit report concerns deficiencies in the risk analysis, risk management and reporting for on-balance sheet investments and the portfolio investments for Rhineland Funding. The advisory service to the special purpose vehicles and the management of IKB's on-balance sheet portfolio investments were for the most part transferred to IKB CAM. According to PwC, the role and importance assigned to IKB CAM in an advisory capacity was too extensive overall. This applied to the preparation of investment decisions as well as in terms of portfolio monitoring – even though the final investment decision regarding on-balance sheet portfolio investments was always made by IKB. Decisions regarding portfolio investments by Rhineland Funding were ultimately made by an Investment Committee comprising two representatives of Dresdner Kleinwort, two independent directors of the purchasing entities, and one director of IKB. The capacity for trading held by IKB CAM within the scope of the applicable control structure was not appropriate in relation to the resulting influence it had on the Bank's risk position.

The auditors also found weaknesses in the analysis of acquired securities. Given the scale of the investment volume and the significance of the risks involved, a continuous separate analysis of each individual issue after the purchase should have been carried out, as well as a systematic and methodically sound management of overall portfolio risk – both for on-balance sheet and off-balance sheet instruments. Instead, the Bank relied predominately on the good ratings, an appropriate distribution of the rating quality in the portfolio and strengthening the credit portfolio in the form of subordinated tranches of each issue. Although the proportion of sub-prime investment has risen significantly, in the last two years in particular, the CP issues retained their very good short-term rating because of the high rating quality of the portfolio. Overall, the diminutions in value from the sub-prime risk in Rhineland Funding that are quite clear now by far exceeded the Bank's risk-bearing capacity.

In light of the auditors' findings, the Board of Managing Directors adopted a programme of immediate action, most of which has already been implemented. The key points of this action plan were as follows:

- No further new business to be concluded in portfolio investments
- Implementation of a comprehensive portfolio analysis and implementation of a much improved portfolio management system (including adjustment of valuation models)
- Re-integration of IKB CAM, transferring functions and personnel resources to IKB AG
- Strengthening the function of Chief Risk Officer (CRO) in particular through merging of responsibility for risk controlling and back office (second vote on credit decisions)
- Establishing a risk committee, to be chaired by the Chief Risk Officer, to ensure a comprehensive assessment and management of all of the risk exposures
- Improvement in reporting to the Supervisory Board, particularly with respect to residual portfolio investments
- Revising the concept to determine the Bank's risk-bearing capacity

Results and consequences of the audit report with regard to accounting

Based on the results of the audit report, the Board of Managing Directors decided, with the consent of the Supervisory Board, to modify the consolidated financial statements as at 31 March 2007, in particular due to the fact that certain accounting questions would be dealt with differently with knowledge of the developments that subsequently occurred on the sub-prime and commercial paper markets. The changes that were applied retrospectively in accordance with IAS 8 impacted in particular on the consolidation of Rhineland Funding and on parts of a issuing entity whose securities serve as an investment vehicle for IKB's economic capital. These are fixed-income securities that were reported up to now under investment securities, each of which securitises a portfolio of mortgage bonds and derivatives. The consolidation now means that the Pfandbriefe and derivatives are accounted for separately so that these items are measured at fair value instead of at amortised cost. The market value of these derivatives fluctuates considerably in line with changes in general market interest rates, so that the consolidation resulted in significant volatility in the income statement. This better reflects theses instruments' risk/return profile in substance.

The retrospective changes in the accounting as at 31 March 2007 yielded an operating result of € 115 million for the financial year 2006/07, which is € 148 million lower than the figure of € 263 million reported originally. This was primarily due to the valuation of derivatives, which were initially included within the scope of consolidating the issuing entity described in the preceding paragraph, and of Rhineland Funding (and Havenrock in particular). Total assets increased by € 11.5 billion – in particular due to the consolidation of Rhineland Funding – to € 63.5 billion as at 31 March 2007. A detailed reconciliation of the balance sheet and income statement can be found in the Notes, in the chapter "Adjustments pursuant to IAS 8".

The previous figures for the 2005/06 financial year have also been adjusted accordingly. Consequently, the operating result has fallen from € 233 million to € 171 million, and total assets as at 31 March 2006 rose by € 9.1 billion to € 53.3 billion.

The Board of Managing Directors also decided to implement adjustments in the segment reporting as of the financial year 2007/08. In future, transactions securitised by the Bank itself will be shown in the segment "Head Office" and the current "Securitisation" segment will be renamed "Portfolio Investments".

Based on the results of the special audit, the Board of Managing Directors, with approval of the Supervisory Board, also decided to issue a restated Annual Report as of 31 March 2007 as well. The restatements that were carried out in the current calculations for the financial year 2006/07 relate in particular to the returns on structured bonds, accounting for the discounting effects in determining the valuation gains for collateral within the scope of deriving risk provisions, as well as the treatment of credit linked notes for accounting proposes. Following the aforementioned restatements and taking into consideration a further allocation to the fund for general banking risks amounting to € 34.6 million, we derive net income for the financial year 2006/07 of € 0.0.

Owing to the events mentioned above and the changes that have been agreed upon, the publication of the audited interim financial report originally scheduled for 15 November 2007 was postponed until March 2008. The publication of the 9-month report scheduled in the financial calendar for 14 February 2008 has also been postponed until March 2008.

Further significant events that occurred after 31 March 2007 can be found in Note 68.

The restructured financial statements and consolidated financial statements as at 31 March 2007 are being reviewed by the German Financial Reporting Enforcement Panel, in accordance with Section 342b, paragraph 2, sentence 3 no. 3 of HGB (sample checks). The Panel will inform IKB of the results upon completion of the review. IKB is obliged to disclose any error determined upon completion of the review by decision of BaFin in accordance with section 37q (2) of the German Securities Trading Act (Wertpapierhandelsgesetz – WpHG).

Changes to personnel

To support the Bank's continued existence, and on the basis of the findings of the agreed upon procedures carried out by PwC, the Supervisory Board of IKB has implemented extensive personnel changes. The former CEO, Stefan Ortseifen, and the former CFO, Dr. Volker Doberanzke, resigned from the Board of Managing Directors with effect from 29 July and 7 August 2007 respectively. Dr. Markus Guthoff and Frank Braunsfeld resigned as members of the Board of Managing Directors with effect from 15 October 2007.

With effect from 29 July 2007, the Supervisory Board appointed Dr. Günther Bräunig, Member of the Board of Managing Directors of KfW, as CEO, whilst Dr. Dieter Glüder, previously a Director of KfW, was also appointed to the Board of Managing Directors of IKB. During Dr. Bräunig's term of office on the Board of Managing Directors of IKB, his function as member of the Board of Managing Directors of KfW will be suspended. Dr. Reinhard Grzesik was appointed as CFO of IKB with effect from 15 October 2007.

The Board of Managing Directors of IKB terminated the employment of Mr Winfried Reinke, Managing Director of IKB CAM in Dusseldorf, without notice with effect from 1 August 2007; and relieved Mr Claus-Dieter Wagner, Head of Risk Management of his duties, effective 17 October 2007.

Current rating situation

Since the crisis on 27 July 2007, the rating agencies changed their assessment of IKB on several occasions. The long-term rating is decisive for the issue of bonds, which are the main source of refinancing for the Bank's business activities. Until the outbreak of the crisis, IKB had an Aa3 rating from Moody's; it has been downgraded three times since them, most recently on 22 January 2008 to A3. The financial strength rating was also downgraded from B to E+. The rating agency Fitch retained its long-term rating of A+ but downgraded the individual rating from B/C to E.

IKB ratings		Long-term	Short-term	Financial Strength individual rating	Outlook
Moody's		Aa3 (from 15 Sep 2003)	P-1	B (negative)	Stable
	31.07.2007	Aa3	P-1	C (negative)	Negative
	04.09.2007	A2	P-1	D- (negative)	Negative
	22.01.2008	A3	P-2	E+ (developing)	Negative
Fitch		A+ (from 05.10.98)	F1	B/C (from 15.12.05)	Stable
	02.08.2007	A+	F1	C (negative)	Stable
	21.12.2007	A+	F1	E	Stable

Current risks

In order to carry out a full assessment of the current risks, the following arguments should be observed in conjunction with the explanations on risk given in the Outlook.

Operational risks

The impact of the sub-prime crisis had the effect of increasing IKB's operational risks considerably. Internal crisis management requires resources that extend far beyond the Bank's own capacities. This gap will be compensated for as much as possible through the use of external advisors. Additionally, the Bank's own resources are weakened by loss of manpower as a reaction to the crisis. New recruits can only partially compensate for this loss at present.

Legal risks

Over the last few weeks, a series of claims for damages against IKB have been lodged by investors. These claims relate in particular to the press release issued by the Bank on 20 July 2007: it is IKB's view that these claims are unfounded. The investor plaintiffs base their claims for compensation mainly on the charge that IKB's press release as at 20 July 2007 was intentionally erroneous. At that time, IKB did not identify any material risks in relation to the liquidity facility extended to Rhineland Funding, because it did not believe it possible that the entire ABCP market would collapse, thus no longer facilitating refinancing in the long term. In its press release of 20 July 2007, IKB therefore concentrated on the risks at that time in its own balance sheet.

On 10 August 2007, Düsseldorf's Department of Public Prosecution also began investigating managers of the Bank on suspicion of dishonest dealings and violation of the German Joint Stock Corporations Act (Aktiengesetz). The Bank is the potentially aggrieved party. The Board of Managing Directors is supporting the Department of Public Prosecution in its work, and cooperating in all regards, in order to ensure that the matters concerned are resolved in full as soon as possible.

Annual General Meeting and Dividends

The Annual General Meeting that was originally scheduled for 30 August 2007 will now be convened on 27 March 2008. No net profit (Bilanzgewinn) will be shown in IKB's restated financial statements as at 31 March 2007 in accordance with the German Commercial Code (HGB); therefore, no dividends will be distributed. The Bank had originally planned to distribute a dividend of € 0.85 per share.

2. Outlook

Sale process

On 18 January 2008 KfW initiated the process to sell its stake in IKB. This marks the starting point of a structured selling process, during the course of which all potential bidders will have the opportunity of expressing their interest.

Stiftung Industrieforschung – the Industrial Research Foundation – which is IKB's second-largest shareholder, plans to dispose of its stake within the scope of the selling process.

Potential bidders may submit an indicative bid on the basis of an information memorandum. It is intended to grant the remaining bidders the right to review detailed documentation pertaining to IKB (the so-called Due Diligence) and allow them to submit a binding offer on this basis. This Due Diligence is carried out in close cooperation with IKB.

IKB welcomes the start to the selling process. Since the restructuring, IKB's business model has been focused on the Corporate Clients, Structured Finance, and Real Estate Clients business segments. A strong partner will provide extra momentum, enabling IKB to explore new business potential. For this reason, the Board of Managing Directors agreed to support the selling process and to allow selected bidders in-depth due diligence. The Supervisory Board supports the process and established a separate committee for this purpose.

Strategic direction of the Group and future sales markets

In view of the crisis, the Board of Managing Directors conducted a review of IKB's business model and successfully realigned it. IKB's future business model will be focused more strongly on the Bank's three core business units Corporate Clients (encompassing Domestic Corporate Clients, Leasing and Private Equity), Structured Finance and Real Estate Finance. Innovative financing solutions for customers will remain an integral component of the business model, while investments in international structured securities portfolios, funded via short-term Commercial Paper issues, will not.

In terms of the Corporate Clients segment, Germany will remain the core market. However, the aim is to further increase the acquisition potential of this market by offering long-term investment loans to companies with annual sales of € 7.5 million upwards (previous starting point € 10 million) as of the 2007/08 financial year. In particular, the Bank is looking to use its IKB Direct finance platform, which comprises a simplified standardised credit process, to acquire new clients.

We restructured our private equity business at the beginning of the 2007/08 financial year in light of the increasing level of diversification in this market. Our direct investments business will be managed in the newly established subsidiary IKB Equity Finance GmbH, whilst IKB Private Equity GmbH will continue to deal with our mezzanine business and to look after our fund investments in the partner structures of Argantis and MM Mezzanine. A particular focus of IKB Private Equity GmbH during the 2007/08 financial year will lie in offering standardised mezzanine capital within the context of equiNotes III.

As well as improving our market position in equipment leasing in Germany, the Bank is also looking to establish branches in Russia and Romania in addition to our existing bases in Central and Eastern Europe. This is based on our appreciation of the fact that a number of German and Western European companies have established themselves in these countries and are looking to finance their production capacity there through leasing arrangements.

In terms of real estate financing, our goal is to grow the volume of new business organically over the next three years. The European real estate platform established during the 2006/07 financial year, which is mainly geared towards syndicated finance, will contribute to this, as will medium and long-term real estate finance in Germany. This will be supplemented with project development activities, for which IKB can offer the full range of its services, earning attractive commission income in the process.

In the Structured Finance division, IKB will be continuing to pursue its successful internationalisation strategy, with particular focus on the European markets. The Bank will play a greater role in the development of these markets, both in the mid-cap LBO sector and in selected areas of project finance. Based on the current situation, we expect that we will also be able over the next two years to generate around 70% of our income from the Structured Finance division on foreign markets, with the share of project finance rising further.

Investments in international credit portfolios must first be stabilised and significantly reduced. Whether new business is gained on a much lower scale and with a different risk structure after this process will depend on future capital resources and the extent to which the markets return to normal.

Future economic parameters

The Board of Managing Directors expects that the basic economic parameters at national and international level will remain positive for the Bank's business in 2008 and 2009. As far as IKB's core market is concerned, namely Germany, the following developments are expected in the economy as a whole:

- German GDP growth was around 2.5% in 2007. The main growth drivers were the export-oriented German companies that drew particular benefit from the positive development of the global economy thanks to their excellent range of products. Global momentum is now grinding to a halt, so that the leading research economists are predicting that German GDP growth will fall to around 1.5% to 2% in 2008. Even this forecast comes with risks given the ongoing turbulence on the financial markets.

- The economic problems in the USA resulting from the crisis in the real estate market will have an even greater impact worldwide in 2009. Germany's GDP growth is unlikely to be more than roughly 1.5 %.

- Domestic economic growth will be supported by private consumption in the next two years. In light of positive employment effects and improved income prospects, this effect will be more pronounced in particular in 2008.

- Exports are unlikely to be increasing as strongly as in previous years, given that the global economy is cooling down. IKB is forecasting a rise in the region of 5% to 7% for 2008 and 2009, after 8% in 2007. Capacity utilisation and order levels of IKB's clients – mainly strongly export-oriented medium-sized companies – will therefore remain high for some time yet.

- The most important economic factor for the Bank's lending business, namely investment in plant and equipment by the corporate sector, should post growth rates of 4% to 5% in 2008 and 2009, following a rise of at least 8% in 2007. Lending business involving domestic companies is expected to continue at profitable levels as a result.

- The German Council of Economic Experts anticipates that the international markets, which are relevant for IKB, will develop as follows: in Western Europe, gross domestic product growth will gradually weaken from 2.7% in 2007, to 2% in 2008 and around 1.8% in 2009. The economic research institutions are forecasting substantial weakening in the USA to 1.5% in 2008 and 2009 compared with growth of 2.3% the year before. In light of falling house prices and negative income effects, consumer hesitation amongst private households should have a bearing above all in 2009. The outlook for central Europe remains positive, with GDP growth rates of around 5% forecasted for 2008 and 2009.

The future competitive environment

The competitive situation in the German banking sector was tense once again in 2007. The economic problems affecting many banks as a result of the sub-prime crisis make it especially difficult to predict how competition will look in 2008. Already, during the last few months of 2007, a reticent approach to lending was in evidence in Germany, particularly in the case of real estate loans, combined with an improvement in gross margins. Meanwhile, there are some signs that long-term credit for corporate customers is being used by other banks as an entry product so that further services can be placed with that same customer at a later stage. Overall, this means that IKB remains in competition in domestic lending business above all with the major banks, selected Landesbanken and the major savings banks. The entry into the German market of new competitors, particularly from abroad, looking to offer long-term finance to medium-sized companies is something the Bank expects to see only to a limited extent. Healthy market development hinges on all market operators passing on the higher refinancing and placement costs in the credit margins.

With regard to the credit needs of German medium-sized enterprises, the Bank expects to see a reserved development. Companies are, certainly, investing strongly to meet domestic and foreign demand. At the same time, however, many companies have generated high incomes in the good economic environment of the last few years and are therefore in a position to finance large portions of their investments with only small levels of borrowed capital.

In terms of international finance, IKB expects a significant reduction in market volume during this financial year. It is impossible to predict margin levels in the current market situation.

Financial situation

The risk shield, together with the additional package, has stabilised IKB‘s financial situation. According to the related action plan, a proposal will be submitted to the ordinary shareholders‘ meeting of IKB AG on 27 March 2008 to pass a resolution to increase the company‘s capital by up to € 1,486,765,992.96, against cash contributions and with a 6-for-1 subscription right for existing shareholders. KfW has committed to BaFin to ensure that a sufficient quantity of new IKB shares will be subscribed to or purchased under the capital increase that IKB will obtain fresh funds in a minimum amount of € 1.25 billion (excluding costs).

Furthermore, KfW has undertaken, vis-à-vis BaFin, to boost IKB‘s regulatory tier 1 capital by € 600 million until 19 February 2008, by way of an “additional capital contribution” pursuant to section 272 (2) no. 4 of the HGB, to be recognised in the capital reserve. The contractual details governing this contribution will be determined at short notice; they may include a debtor warrant (Besserungsabrede) which may burden the annual results of future periods.

The disposal of major parts of IKB‘s portfolio investments is planned as a further component of the restructuring package.

The refinancing of lending business during the 2007/08 financial year has been made significantly more difficult since the crisis in July 2007 and has been primarily carried out through secured borrowing. Once the planned capital increase has been carried out, the Board of Managing Directors expects to be able to recommence refinancing also by unsecured means, using bonds on the national and international capital markets. This is subject to the international capital markets returning to normal. Additionally, as in the past, IKB will refinance a portion of its lending business by taking up funds from the public development banks.

Complementing its long-term refinancing, the Bank will be issuing money-market instruments primarily with maturities of between 60 and 180 days as a means of diversifying its funding mix in the interbank market.

Furthermore, every opportunity should be used to further relieve pressure on the Bank’s ability to carry and sustain risk on the assets side, with a view to improving the solvency ratios. These measures include a further reduction in market price risk as well as in the risk-weighted assets in the lending business, both by limiting new business and by outsourcing credit risks.

Liquidity strategy

Following the outbreak of the crisis, the Bank undertook to extensively revise and refine its liquidity planning and management. This now allows it to generate a detailed forecast of the daily liquidity situation in each of the following three months as well as a sufficiently reliable forecast for a 12-month horizon.

The Bank's liquidity requirements are covered through borrowing on the money market (cash and term deposits), by secured and unsecured means, participating in ECB repos, selling liquid securities investments as well as accepting customer deposits on the basis of promissory note loans. IKB receives additional funds through the promotional loan programmes offered by KfW and the state development banks, which it uses in financing its medium-sized clients.

These instruments also represent the basis for the Bank to generate liquidity until such point as it is broadly eligible for capital market refinancing, especially for long-term borrowing. Successful completion of the planned capital increase will be decisive in this context.

The Bank also intends to deploy at least a part of its portfolio investments of € 5.9 billion (valuation as at February 2008) for the purpose of generating liquidity. Funds will be raised either from such a sale from the shielded part of these portfolio investments, or until then from the loss settlement (up to a maximum of € 1 billion).

The Bank has calculated that it will require funds in the region of approx. € 12 billion spread out over the next 12 months. All told, the Board of Managing Directors anticipates a trend towards a gradual normalisation of money and capital markets in the course of 2008, although short-term distortions cannot be ruled out.

Expected income situation

The necessary restructuring measures, and especially the market development of securitised credit portfolios (as explained above) will also have a major detrimental effect on the result for the current financial year. On the basis of the current market situation, however, this is offset by a positive measurement effect of around € 770 million, of which only a small portion is considered sustainable. The background to this distorted picture is that IKB opted, under IFRS, to measure a substantial portion of its liabilities at fair value. The fact that these liabilities of IKB have lost a great deal of fair value due to the current crisis means that they are reported in the balance sheet on the basis of the lower fair value. This measurement gain is recognised as income in the IFRS consolidated financial statements. Provided that it does not relate to actual defaults of interest or principal on hybrid liabilities, it will be reversed by the time the liabilities are repaid at nominal value, thus creating a corresponding expense. If the fair value of the liabilities rises due to an improvement in IKB's capital market standing, this expense may also occur at a much earlier stage.

Overall, the Board of Managing Directors expects the Group to record a loss for the 2007/08 financial year (according to IFRS) of approx. € 550 million. The previous forecast of a consolidated loss of up to € 700 million for the IKB Group did not include the additional mark-to-market losses of resulting from the revaluation of portfolio investments. It does also not include the above mentioned large positive measurement effect of its liabilities at fair value.

The current estimate of results is still subject to significant uncertainty. This is due to the fact that the audit of the half-yearly report as at 30 September 2007 has not yet been completed. The partial sale of a portfolio investments may also result in higher losses.

The Board of Managing Directors expects the net retained loss in the single-entity financial statements of IKB AG to amount to approx. € 750 million. This figure reflects higher losses from the revaluation of portfolio investments, which were offset to some extent by loss-sharing on profit-participation certificates and silent partnership contributions.

Although the operating results of the Corporate Clients, Real Estate Clients and Structured Finance segments are expected to be lower than the year before, they will still be clearly positive. This is due to the fact that whilst the crisis has placed major restrictions on these segments' new business, they have not been affected by losses made in the portfolio investments.

Once the restructuring process has been completed, the Bank should have an income structure that is quite different, with the level of income expected to be lower overall, as income from portfolio investments will fall substantially. The 2008/09 financial year will still be burdened significantly by the impact of the crisis, in particular by the restrictions to new business origination since August 2007, and the strong rise in refinancing cost. The Board of Managing Directors envisages results for the 2008/09 financial year to be slightly positive. The medium-term objective is to generate an adequate return on invested capital from the Bank's operative business.

As a result of write-backs which hybrid capital investors (and possibly KfW) are entitled to, in combination with additional measures within the package, net profit may remain at a low level over several financial years.

Risks of future development

Liquidity risks

The continued existence of IKB is dependent on its ability to achieve greater access to the capital market again in the next financial year also for unsecured longer-term funding. For this purpose, it is essential that

- the planned capital increase is approved in the required amount, registered in the Commercial Register, and carried out without delay;

- the measures planned to generate liquidity, especially new borrowing that are necessary in the short-term and the extension of secured money market funding, are implemented;

- a significant portion of portfolio investments is disposed of; and

- no legal action is taken against the measures set out above, or against the entire risk shield; this applies in particular to any action taken by the EU.

The Board of Managing Directors assumes that the planned measures outlined above will be implemented as expected in the medium term, thus permitting the Bank to once again achieve extended access to the capital market and also for unsecured longer-term funding.

Market price risks

In conjunction with the measures described above that were taken to shield against risk in the portfolio investments on IKB's balance sheet (and the package implemented to offset the valuation losses determined in February 2008), existing risks associated with a change in the credit spreads for these financial instruments were reduced significantly.

Given the prevailing market situation, however, a portfolio sale would likely involve more sizeable discounts. Moreover, a proportion of these risks – especially for financial instruments outside the risk shield – will remain with IKB even after portfolio investments have been sold.

Further market price risks are associated with the Bank's interest rate exposure. In the meantime, the protective measures introduced in the course of the new financial year had the effect of reducing the risk on this position considerably.

Risk shield and additional package of measures

Implementation of the risk shield and the additional package is subject to the absence of any concerns raised under EU legislation. This has not happened to date, although the related review has not yet been completed.

The agreements regarding the risk shield provide for a special right of termination for KfW in the event of IKB failing to comply with certain reporting duties (or to comply in line with contractual agreements) after two deadlines have been set.

The Board of Managing Directors considers this risk to be minor, as a project to identify, establish, and monitor compliance with contractually-agreed reporting was successfully implemented in close co-operation with KfW, to ensure IKB fulfils its contractual duties vis-à-vis KfW.

Cyclical risks

The business prospects of the Bank's clients in the Corporate Clients, Real Estate Finance and Structured Finance divisions are affected not least by economic development.

A deterioration of the economic environment in the USA can lead to higher provisions for loan losses above all with regard to the funding of American transactions, so as to take adequate account of potentially higher loan defaults. Given that the economic slowdown in the USA should impact significantly on Germany and Europe, higher provisions for loan losses should also be forecasted for European acquisition finance, loans to German SMEs and to a lesser extent for real estate finance.

3. Report for the Financial Year 2006/07

Explanations on the business conditions and basic parameters, the financial situation and the risk report are based predominately on the period from 1 April 2006 to 31 March 2007 – and hence on a period prior to the outbreak of the crisis. Against this background, the explanations in the following three chapters provide a comprehensive insight into the Bank's situation only if it is viewed in conjunction with the Report on Material Events After the Reporting Date and the Outlook.

3.1 Business Conditions and Basic Parameters

Business environment

The 2006/07 financial year was marked by benign macro-economic conditions: this applies both to economic development in IKB's core market, Germany, and to economic development in those countries in which IKB is involved through its structured finance business and equipment leasing activities.

In Germany, GDP rose by 2.9% in 2006. Furthermore, investment in plant and equipment, an even more important indicator for IKB's domestic lending business, rose by 8.3% year-on-year. The main factor driving this increase was exports, which grew by 12.5%.

This strong level of growth can be attributed in particular to the fact that German companies largely export goods based on state-of-the-art technology (i.e. those goods where R&D account for more than 3.5% of sales revenues). The good position enjoyed by German companies on the world markets applies not least to IKB's main target group, medium-sized industrial enterprises.

Due to the high volume of incoming orders from abroad, companies were motivated to expand capacity in 2006 in addition to stepping up their investment in capital goods. Since these small- and medium-sized enterprises continue to operate the majority of their production sites in Germany, accordingly they borrowed funds to finance their capital investments and construction projects.

The real estate market also clearly picked up in Germany during the 2006/07 financial year. Following years of stagnation, if not recession, there was a clear upward trend in demand for real estate buoyed by the general upturn in the economy as a whole.

Strategic positioning of IKB

IKB is the leading German specialist bank in long-term finance for medium-sized corporate clients, real estate investors, project partners and institutional investors. In terms of granting long-term corporate loans to the manufacturing industry, the Bank is the market leader with a market share of just under 10%. IKB's main rivals in Germany are the major universal banks, as well as selected larger institutions from the public banking sector.

IKB's strengths are to be found in its specialisation, in its skill and expertise in this area of specialisation, and in the high level of trust placed in the Bank by its clients.

The foundation for the activities is provided by IKB's exceptionally well trained and highly dedicated team of employees. What is important is that the employees can strongly identify with the Bank. Employee surveys regularly show that over 90% of IKB staff agree that this is in fact the case. This is one of the top results in the financial sector. Since the onset of the crisis in July 2007 there has been a rise in staff turnover. However, in view of the situation, the level is still relatively low, demonstrating the strong sense of loyalty felt by employees to IKB.

All of the Bank's business activities focus on its clients. In order to be able to deepen and widen relationships with customers in a targeted way, IKB has divided its market activities into the following segments:

- Corporate Clients
- Real Estate Clients
- Structured Finance; and
- Securitisations

Corporate Clients

The Corporate Clients segment encompasses domestic corporate lending, leasing and private equity.

In terms of issuing long-term investment loans to German medium-sized companies, IKB is Germany's market leader. In addition to the high quality of the advisory services on offer, clients value the Bank's clear commitment to Germany's medium-sized businesses – all the more so during difficult economic periods. In turn, clients place a very high level of trust in IKB.

IKB engages in equipment leasing at a national and international level, -and is one of the market leaders in machinery leasing in Germany. With regard to foreign markets, IKB has a successful presence in selected Central Eastern European countries (Czech Republic, Hungary, Poland and Slovakia), as well as in France and Austria.

IKB Private Equity focuses on providing medium-sized companies with direct shareholdings as well as mezzanine capital, particularly within the context of securitisation transactions backed by profit-participation certificates.

Real Estate Clients

The focus in the Real Estate Clients division lies in the following areas:

- domestic real estate finance;
- international real estate finance;
- equity finance (project development); and
- services.

As well as tailored financing, IKB can also offer its clients the full range of real estate services.

By establishing a European financing platform during the second half of 2006, the Bank is getting involved in attractive real estate investments, primarily in the UK, the Benelux countries, France, Italy and Spain.

Structured Finance

Structured Financing, encompassing national and international acquisition and project financing, has developed into a key income contributor for the Bank over the last few years. IKB acts as the arranger of structured finance in Germany, France and – since the 2005/06 financial year – also in Italy and Spain. The Bank also successfully assumes the role of participant in the UK and USA.

IKB applies the same principles of success to acquisition financing as to domestic corporate clients business, namely highly skilled employees in all activities specific to the transaction and excellent industry know-how. Also of crucial importance is IKB's local presence in all of the key Western European markets, enabling the Bank to take due account of regional characteristics when cooperating with private equity investors on the ground in mid-cap transactions.

As part of the Bank's project finance activities, IKB arranges and structures the financing for national and international projects. These activities – for energy or infrastructure projects for example – now account for more than 40% of new business in the Structured Finance segment. IKB also finances the export of capital goods (ECA-covered export finance) and accompanies medium-sized companies as they build up production capacity abroad as part of an internationalisation strategy.

Securitisations

The Securitisations segment encompassed two areas: the placement of credit risks with third parties and investments in international credit portfolios. The subsequent consolidation of Rhineland Funding is reflected in this segment. As of the 2007/08 financial year, transactions securitised by the Bank itself will be shown in the segment "Head Office" and the current "Securitisation" segment will be renamed "Portfolio Investments".

Since the late 1990s, IKB has been pursuing the concept of the risk-based external placement of balance-sheet assets, and of loans and advances to customers in particular. To date, the Bank has securitised a cumulative volume of almost € 18 billion of such assets, placing them largely synthetically on the national and international capital markets. This has enabled IKB to reduce its credit risk and to free up a high level of equity, with the result that during the period from 1995 to 2007 the Bank was able to raise its on-balance sheet loan volume (excluding the consolidated purchasing entities of RFCC) by 115% without issuing new shares.

IKB has enjoyed attractive issuing conditions thanks to the high granularity of the individual risks and the convincing performance of previous placement transactions. The current distortions on the securitisation market have, however, greatly increased the placement costs. Having said that, IKB expects the markets to normalise again, even if not to the level prevailing before the sub-prime crisis, which will mean that the strategy of placing credit risks can be continued.

The capital released through securitisation activities over recent years has been used to expand national and international lending business and for investments in international credit portfolios. Two thirds of the investments made on the balance sheet of IKB AG and IKB International Luxembourg are focused on US portfolios with at least investment grade ratings (including, for example, credit card claims, mortgage loan claims and corporate loans), with the remaining third being invested in similarly structured European portfolios.

Cooperations

Once again in the 2006/07 financial year IKB enjoyed very successful working relationships with its cooperation partners.

A joint finance volume of € 1.4 billion was recorded with the KfW Banking Group as a result of either side inviting the other to contribute to financing projects, compared with € 0.9 billion during the previous year. Most of these transactions, as in the previous year, related to national and international project finance.

In addition to these joint deals, IKB once again refinanced a portion of its domestic corporate client lending business with KfW. At its clients' request, IKB made particular use of the following standard programmes: KfW Entrepreneur Loan Programme (Unternehmerkredit), KfW Entrepreneur Capital Programme (Unternehmerkapital) and KfW Innovation Programme (Innovationsprogramm).

There was a gratifying development to report with regard to Movesta Lease and Finance GmbH, a joint subsidiary of IKB and KfW IPEX-Bank. Movesta was able to record € 0.6 billion of new business during the period, up by more than 50% on the year before. Movesta's business activities focus on real estate leasing and the leasing of large-scale equipment.

The upturn in the German economy had a positive impact on Movesta's level of new business. However, the debate surrounding the new basic tax conditions in Germany was more of a burden on real estate leasing business over the course of the year. In light of this obstacle, the good result recorded by Movesta in what was only its second year should be rated even more highly.

The working relationship with the Bank's cooperation partner Sal. Oppenheim was successful during the year under review. Once again, both partners were able to achieve an increase in the reciprocal flow of deals. Moreover, Sal. Oppenheim is a Designated Sponsor of the IKB share.

The Bank also worked intensively with its French cooperation partner Natixis during the financial year under review. Joint activities focused on corporate client business, structured finance, promissory note loans and, in particular, loan syndication. Both Natixis and IKB were able to invite each other to participate in many attractive business transactions. The fact that Natixis – in the wake of the merger between Natexis Banques Populaires and the investment bank IXIS in 2006 – is now one of Europe's leading banks opens up new prospects for bilateral activities.

3.2 Financial Condition and Results of Pperations

The changes to the financial figures as at 31 March 2007 compared with the previous year are outlined below: any significant deviations in the new figures for 2006/07 compared with the original figures, owing to the changes to the financial statements, will also be shown.

Income

Net interest income grew by 25.9 % during the reporting period, to € 381 million (2006/07 prior to restatement: € 509 million). Roughly 80 % of this total relates to the business activities of our market-facing segments, whilst 20% was achieved primarily from the investment of equity capital.

Proprietary investments included structured capital markets products, whereby an initial fixed return was followed by variable-interest periods. As a specific change, implied premiums for issuer conversion options which are embedded in the coupon were identified and deferred over subsequent periods. As a result, net interest income declined by € 77.9 million. In addition, € 49.6 million in premiums on Credit Default Swaps which are subject to mandatory decomposition was reclassified from interest income to fee and commission income.

Accordingly, net fee and commission income rose by € 49.6 million as a result of the restatement, to € 164 million (€ 125 million prior to restatement). Approximately one-third of this income resulted from structuring fees and commission earned in the Corporate Clients, Real Estate Clients and Structured Finance segments, with two-thirds being contributed by the Securitisation segment, from advisory fees relating to the Rhineland Funding conduit.

The net result from financial operations was negative, at –€ 10.1 million (€ 0.5 million).

Against the background of the continuing expansion, general administrative expenses increased by 14.3%, to € 259 million. The main cause of the rise in general administrative expenses was the hiring in the 2006/07 financial year of 61 new employees on balance (average FTE).

Net other operating income and expenses was down by 32.4 %, to € 161 million, in line with expectations. The net figure comprises the intra-group transfer of the shareholding in IKB International to IKB Lux Beteiligung S.à.r.l. This followed the spin-off of shareholdings in subsidiaries into a separate holding company, which we had initiated in the previous financial year, in order to realise tax-exempt income in the interest of our shareholders.

Amortisation and write-downs of receivables and specific securities, as well as additions to loan loss provisions, decreased by 37.2%, to € 304 million. The € 34 million increase compared to the € 270 million figure originally reported was due to the first-time incorporation of the expected realisation period for pledged collateral, by discounting using a market interest rate for an adequate maturity. Net loan loss provisions amounted to € 249 million (€ 541 million); the results from liquidity reserves swung to –€ 55 million (€ 57 million).

The net result before taxes declined by 20.3%, to € 134 million. The Bank appropriated this result to transfer € 110 million to the fund for general banking risks in accordance with section 340 g of the German Commercial Code ("HGB"). Taking into account € 24 million in taxes, the net profit is € 0.0 million. The Board of Managing Directors and Supervisory Board will thus propose to the General Meeting that no dividend be distributed.

Segment performance

Corporate Clients

IKB achieved a 14.1% rise in new business in the Corporate Clients segment, recording a figure of € 4.8 billion. This rise is all the more remarkable in light of the fact that the volume of loans disbursed had already been improved by 22% in the previous financial year. An increase was also recorded with regard to the credit portfolio, up to € 16.8 billion (€ 15.7 billion).

Accounting for € 3.9 billion, long-term domestic corporate finance made up the largest proportion of the loan disbursement volume in the 2006/07 financial year. A year-on-year increase of 15.0% was recorded in this area.

Equipment leasing is becoming ever more important to medium-sized companies. This growing importance enabled the Bank to increase the finance volume of new business by 17.1% compared with the previous year to € 0.8 billion. Three quarters of this amount related to domestic clients whilst one quarter of the demand emanated from business partners abroad.

Private Equity activities focused during the year under review on the equiNotes II profit-participation programme, which were issued again in conjunction with Deutsche Bank after the equiNotes I programme was closed. The mezzanine capital made available to medium-sized companies through this programme, which is not included in the disbursement figures, amounted to € 220 million. The total amount of both profit-participation programmes was close to € 600 million.

The Corporate Clients segment improved its operating result for the 2006/07 financial year to € 135 million (€ 130 million). The competition for the medium-sized companies was as intense as ever, with a related fall in the average margin achieved in new business to 1.12% (1.31%). Against this background, provisions for possible loan losses in the Corporate Clients segment were cut to € 38 million (€ 44 million). The resulting cost/income ratio was 46.7% (44.4%), with a return on equity of 21.0% (21.6%).

Real Estate Clients

IKB recorded a positive development with regard to its European real estate finance activity. New business worth € 0.3 billion was acquired within just a few months of the Bank's foreign activities being launched. This good result was made possible by the fact that IKB launched this business within the framework of its European financing platform with internationally experienced teams. Looking at real estate finance as a whole, this means that the Bank was able to increase the disbursed amount by 29.0% over the period under review to € 1.3 billion.

The Real Estate Clients segment increased its operating result to € 35 million (€ 32 million). At 1.32% (1.33%), the interest margin almost matched the high level of the previous year. Return on equity stood at 18.2% (17.0%), whilst the cost/income ratio was 45.1% (39.6%).

Structured Finance

IKB is also able to report on a successful performance in the area of structured finance. Operations in this area of business are focused on acquisition and project finance both in Germany and Western Europe and in the USA. IKB was able to observe a high level of demand for its finance products in all of the markets due to the good economic development.

The Bank was therefore able to generate a 52.0% rise in new business in this area during the reporting period, to reach a new all-time high of € 5.3 billion. Of this total, around 30% related to domestic acquisition and project finance, whilst IKB was able to realise 70% on the foreign markets, primarily Western Europe and the USA.

The operating result of the Structured Finance segment recorded a significant increase, up by almost 42% to € 111 million. The margin fell to 2.01% (2.55%). This fall was essentially due to the changed product mix of new business, which focused more strongly during the reporting year on project finance, a more stable source of business with lower margins. In terms of new business, 43% related to project finance, whilst acquisition finance accounted for 57%.

Return on equity lay at 33.9 % (35.2%), whilst the cost/income ratio improved to 31.0% (35.5%).

Securitisations

At € 34 million, the Securitisation segment reported a significantly lower result compared to the previous financial year (€ 145 million). This decline was mainly attributable to the net expenditure from financial instruments at fair value of € 49 million (2006/07: income of € 42 million), and higher provisions for possible loan losses of € 19 million. The cost/income ratio rose to 36.4% (21.0%).

As in previous years, activities were focused on investments in international credit portfolios. New business in this segment totalled € 1.2 billion (€ 2.1 billion), resulting in a slight portfolio increase to € 18.4 billion (€ 15.9 billion).

The Rhineland Funding conduit, which was consolidated retrospectively, increased its investment portfolio to € 12.7 billion (€ 9.7 billion).

Balance sheet

Total assets as at 31 March 2007, amounting to € 54.3 billion, were 17.8% up on 31 March 2006. The total loan volume as at 31 March 2007 was € 39.0 billion and thus € 7.2 billion higher than on the same reporting date of the previous year (€ 31.8 billion). The total loan volume as at the reporting date comprises loans and advances to banks, loans and advances to customers, securitised lending (in the form of debt securities), and guarantees.

Loans and advances to customers rose by € 2.7 billion compared with 31 March 2006, to € 24.9 billion. There was a noticeable rise in particular in the maturities from four years and beyond. Loans and advances to banks rose by 25.8 % to € 12.6 billion. Bonds, notes and other fixed-income securities totalled € 14.5 billion (€ 12.2 billion) as at the reporting date. This figure includes € 5.0 billion (€ 4.5 billion) in securitised lending. Investments and interests in affiliated companies increased to € 1.0 billion (€ 0.9 billion), whilst other assets amounted to € 1.2 billion (€ 0.8 billion).

We mainly financed the expansion of our business activities by issuing bonds, so that securitised liabilities duly rose by € 6.3 billion to € 27.8 billion. The issue volume was € 15.6 billion, compared with redemptions of € 9.3 billion. Liabilities to banks fell by € 0.4 billion to € 16.2 billion. Liabilities payable on demand rose by € 0.9 billion, to € 2.5 billion, whilst liabilities with agreed term or period of notice amounted to € 13.7 billion (€ 15.1 billion). Liabilities to customers increased by € 1.9 billion to € 4.7 billion.

Subordinated liabilities were up by € 0.2 billion, to € 1.9 billion. In contrast, there was a drop in profit-participation certificates as part of scheduled redemptions, down by € 42 million to € 0.6 billion. Silent partnership contributions of € 0.4 billion were at the previous financial year's level. Following a € 110 million transfer, the fund for general banking risks grew to € 190 million.

Shareholders' equity amounted to € 1.7 billion. Regulatory capital in accordance with section 10 of the German Banking Act (KWG) amounted to € 3.3 billion as at the reporting date.

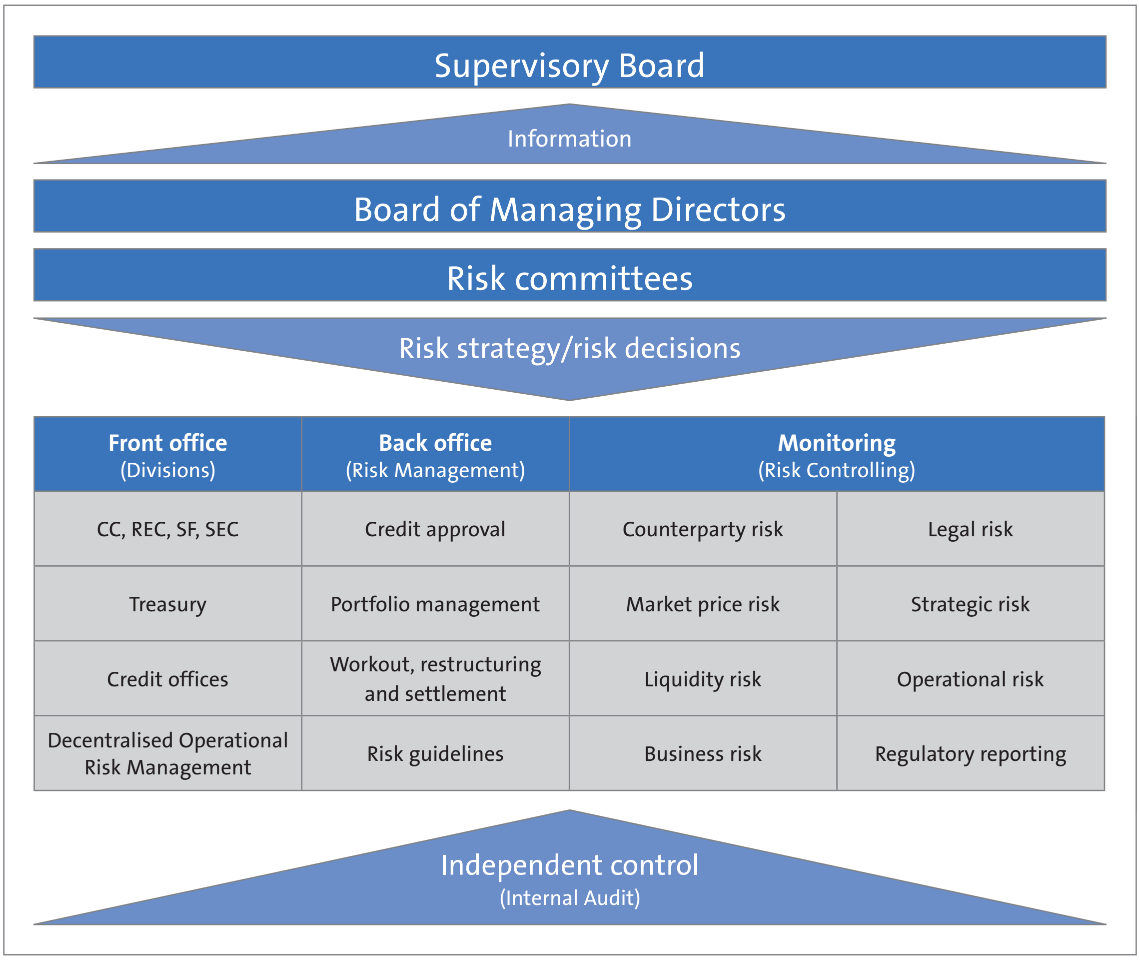
3.3 Risk Report

The Risk report describes the risk management organisation and processes as well as the instruments used in the 2006/07 financial year and hence before the onset of the crisis. In light of this, the following risk report only offers a comprehensive insight into the current risk situation provided it is viewed in conjunction with the Report on Material Events after the Reporting Date and the Outlook.

Risk management organisation.

Risk organisation. Individual tasks and areas of responsibility are described and documented in risk management rules and regulations, which define the principles of IKB's risk management system – taking due account of all statutory and internal requirements in conjunction with credit risk strategy – and provides specific organisational instructions.

Risk organisation in the 2006/07 financial year



Supervisory Board. The Board of Managing Directors is obliged to regularly provide the Supervisory Board at its meetings with detailed briefings on the risk situation and on risk management.

Board of Managing Directors. The Board of Managing Directors is responsible for IKB's risk management. It sets risk policy in the form of a clearly defined business and risk strategy, including the types of business conducted, defines the reasonable total risk within the scope of the Bank's overall risk-bearing capacity and incorporates risk control as an essential component of its processes and planning. The entire Board of Managing Directors is also responsible for dealing with risks related to the Bank's business strategy, and with reputational risks.

Within the Board of Managing Directors, the Chief Risk Officer was responsible during the year under review for the management of counterparty risk, legal risk, and compliance risk. The Chief Financial Officer monitored market price risk, liquidity and funding risks, and operational risks.

Risk committees. Specific committees (e.g. Credit Committee, Limit Committee etc.) manage and monitor decisions that are relevant to risk, supporting the Board of Managing Directors in its risk management operations and decision-making. These committees are responsible for fundamental issues, as well as for decision-making in relation to individual transactions on the basis of the framework laid down by the Board of Managing Directors. The committees are composed of members of the Board of Managing Directors and representatives from the operative business divisions and the responsible corporate centres.

Risk Management. The Risk Management unit is responsible for developing, implementing and complying with Group-wide standards for lending business and for credit portfolio management, as well as for the rating systems used to determine counterparty risk. Alongside the formulation of guidelines for credit analysis and credit decision-making, one of the main tasks of the Risk Management unit lies in the overall credit approval process, with the unit exercising its own credit authority. In other words, the Risk Management unit is the back-office unit for the purposes of the Minimum Requirements for Risk Management ("MaRisk") published by BaFin.

Special management units operate within Risk Management to deal with higher-risk exposures and workout, restructuring and settlement cases, which require specialist expertise and intensive handling. By implementing acceptable solutions at an early stage, this special management facility aims in the first instance to preserve the company as a going concern; or, should these efforts fail, to substantially reduce the financial fallout.

Credit/transaction management teams (which are classified as front-office units) provide support to Risk Management in monitoring and managing credit risk within the relevant business divisions. With the exception of minor decisions permitted under MaRisk, credit approvals are made by the back-office unit, as long as they are outside the remit of the Board of Managing Directors.

Risk Controlling. Risk Controlling, a unit that is independent from front office units and Risk Management, is responsible for monitoring the risk policy specified by the Board of Managing Directors, for internal and external risk reporting, capital planning and risk capital allocation, and for impartial monitoring of credit, market, liquidity and business risks. The unit is subdivided into Credit Risk Controlling, Market Price Risk Controlling, Results Controlling, and Capital Controlling units.

In addition to continuous, near real-time monitoring, analysis and reporting of credit risks on a portfolio level, Credit Risk Controlling is responsible for the ongoing development and validation of models used for quantifying risks and assessing credit quality. Further key issues involve aggregating all types of risk into an overall Group risk position, which is then used as an integral part of simulating and monitoring the Bank's risk-bearing capacity.

The core functions of Market Price Risk Controlling comprise the daily calculation, analysis and reporting of market price risks, monitoring the limits set by the Board of Managing Directors, as well as checking the models and procedures used to value financial instruments. Market Price Risk Controlling is also responsible for the continuous monitoring of, and reporting on, asset/liability management throughout the Bank.

Results Controlling ensures the ongoing monitoring of IKB's results of operations, and related reporting, by way of monthly performance analyses of existing and new business. Detailed financial reports are prepared to identify and analyse any divergence in income and assets from target values.

Capital Controlling is responsible for an integrated capital planning process for the IKB Group, taking into account regulatory and economic aspects, and monitoring the allocation of risk capital to individual operating units subject to a risk/return perspective.

Operational Risk Management. Operational Risk Management is responsible for the monitoring of operational risk throughout the IKB Group. This includes identifying, analysing, and reporting on operational risk, plus responsibility for defining the methodology used throughout the IKB Group to measure operational risk. The central Operational Risk Management unit is supported by a network of decentralised Operational Risk Managers in the business divisions, subsidiaries and corporate centres.

Internal Audit. Group Audit is organised as an independent part of the risk management system and internal control process in accordance with the Minimum Requirements for Risk Management (MaRisk). It operates on behalf of the entire Board of Managing Directors, with no duty to comply with instructions, as an independent body that reports directly to the Board of Managing Directors. Process-based audits are, as a general rule, used to examine all activities and processes across the Group. The focus is placed on particularly risk-sensitive qualitative processes, quantitative methods and the IT processes used in the lending and trading businesses. Group Audit is also responsible for conducting credit and business checks on individual exposures. Internal Audit submits an annual report to the Board of Managing Directors, in addition to individual audit reports comprising material and major audit findings and their current status. In turn, the member of the Board of Managing Directors responsible for audit regularly briefs the Supervisory Board on current results and developments.

Risk management process

Risk-bearing capacity. IKB's risk management process is based on the Bank's risk-bearing capacity; the use of its capital resources is assessed in terms of achieving an adequate risk/return ratio. As part of this management process, it is not only regulatory capital in relation to the targeted ratios and the minimum levels defined by the authorities that are monitored but also whether the Bank, from the perspective of non-subordinated creditors, has a sufficient cover assets pool to cover even those risks whose occurrence is extremely unexpected. The aggregate risk cover comprises mainly equity components including silent partnership contributions, profit-participation certificates and subordinated liabilities, unrealised measurement results, and the operating result before income taxes.

Regulatory capital requirement. The regulatory capital commitment of the individual business divisions is calculated on the basis of the tied-up tier 1 and tier 2 capital in accordance with the applicable regulatory provisions. Management of regulatory capital for the Bank as a whole is based on two key indicators:

- the tier 1 capital ratio (tier 1 capital to risk-weighted assets);
- the total capital ratio (total capital/“own funds” to risk-weighted assets).

With ratios of 7.1% and 12.2% respectively as at the reporting date, IKB clearly exceeds the minimum regulatory capital requirements of 4% (tier 1 ratio) and 8% (total capital ratio).

Economic capital requirement. Economic capital is calculated for the purpose of covering extreme and unanticipated risks. The relevant calculations take into account risk diversification and portfolio effects, using statistical simulations and stress scenario analyses. The risk provisioning budget, plus the annual additions to risk provisions, already cover “anticipated risk” incurred in IKB‘s business operations.

Calculations are made to determine the economic capital required to cover credit risk, market price risks (which IKB is exposed to largely as a result of interest rate and spread risks from the banking book), operational risk and general business risk. The Bank‘s own models are used for credit, market price and general business risk. Operational risk is calculated using the basic indicator approach stipulated by the supervisory authority. Liquidity and strategic risks are also monitored and checked continuously, but are not managed through risk capital. Rather, they are managed by means of other management tools (please see below).

Economic capital calculated by the individual types of risk is determined within the scope of an annual planning process, and in the course of the ongoing monitoring and reporting to the Board of Managing Directors and the Supervisory Board; it is taken into account in the Bank's management and reporting tools, applying the limits approved by the Board of Managing Directors. The limits imposed on individual risk types, portfolios and partial portfolios, clustering developments, and individual exposures, form a key component of the Bank's quantitative controls and reporting system.

The following table shows the percentage share of the economic capital requirement (excluding diversification benefits) across all types of risk. The previous year's figures for credit risk and operational risk were adjusted to reflect the methodological improvements implemented during the financial year under review.

Economic capital requirement

	31.3.2007		31.3.2006 (adjusted)		31.3.2006	
	in € million	in %	in € million	in %	in € million	in %
Credit Risk	473	62	455	54	368	44
Market price risk*	108	14	206	24	333	40
Business risk	98	13	95	11	95	11
Operational Risk	82	11	90	11	36	4
Total	**761**	**100**	**846**	**100**	**832**	**100**

* excluding € 71 million in economic capital required to cover market risk from spread changes (31 March 2007)

Compared with the adjusted figures for the previous year, the economic capital requirement as at 31 March 2007 (excluding diversification effects) fell by a total of € 85 million. This can be attributed to falls with regard to market price risk. Adjustments regarding market price risk were carried out on the basis of the improved methodology applied to the concepts used to measure interest rate risk exposure in the banking book (for details, please refer to "Measuring risks in the fixed-income fund, and in the investment portfolio"). Adjustments regarding credit risks were the result of methodological enhancements related to the quantification of the risk exposure from tradable assets. The fact that credit risk increased at a lower rate – relative to the growth in business volume – reflects both the improved credit quality structure in the traditional credit business in conjunction with the higher degree of diversification.

The credit risk arising from the liquidity facilities that have been made available for portfolio investment companies was incorporated taking into account the likelihood of the facilities being used. Comparative calculations show that, using IKB's specific risk measurement method, the ratio for credit risk rises only slightly, even if the risk from the assets held by the investment companies is fully taken into account. This slight increase is due to the fact that the external rating at the end of the financial year was still very good and hence, the low likelihood of these investments defaulting on the reporting date.

We have harmonised the methodology to determine economic capital requirements for operational risk with the regulatory parameters of the Basic Indicator Approach under the Basel II framework, also adjusting the figures for the previous financial year to enhance comparability.

Risk types

- Counterparty default risk is the risk of a loss being incurred due to the insolvency of a debtor or counterparty. It also comprises country risk, defined as the risk of loss incurred due to a deterioration of the economic environment, political or social unrest, nationalisation or expropriation of assets, failure or refusal by a country to recognise foreign debt, foreign exchange controls, or the devaluation or complete loss of value of a currency.

- Market price risk is the risk associated with negative economic changes in market values caused by changes in market parameters, with a corresponding effect on performance. IKB‘s exposure to market price risks is essentially related to the interest rate and spread risks from the banking book.

- The liquidity and refinancing risk is the risk that IKB would cease to be able to fulfil its payment obligations on time, or to be able to acquire funding on the market at reasonable conditions.

- Operational risk is understood by IKB as the risk of losses due to the inadequacy or failure of internal processes, individuals or systems or as a result of external incidents.

- We define business risk (also encompassing risk associated with developments in the business environment and sector risk) as unexpected negative changes in profitability as a result of a deteriorating market environment, changes in the Bank’s competitive position or client behaviour, or of changes to the legal framework.

- Reputational risk is the risk of direct or indirect losses being incurred due to events that result in a loss of confidence in the Bank, irrespective of whether this loss of confidence occurs on the part of the public, rating agencies, the supervisory authorities, investors, business partners or employees. Reputational risks generally result from, and are compounded by, one of the aforementioned sources of risk.

- Strategic risk is the risk of negative effects on performance due to investment decisions based on existing or future overall business policy. Like reputational risk, this is not a directly quantifiable type of risk, and ultimately cannot be considered in isolation, but must be dealt with and controlled in conjunction with the above risk types.

Counterparty default risk

Definition. A distinction is made in terms of counterparty default risk between credit risk and counterparty risk. The concept of credit risk defines the risk that a loan cannot be repaid at all, or can only be partially repaid (in line with contractual agreement), in the case of default by a contractual partner. IKB is exposed to counterparty risk as a consequence of potential replacement risks related to interest rate and currency derivatives, which may be incurred in the event of counterparty default. Issuer risk and settlement risk are further variations of counterparty risk. Issuer risk is defined as potential loss resulting from the default of the issuer of securities held by IKB, whilst the concept of settlement risk refers to the risk of non-performance of a counterparty within the framework of a settlement process, after IKB has already made payment or delivery. Given the central importance of lending business as one of the Bank's core processes, credit risk is a priority.

Credit risk strategy. IKB's credit risk strategy is based on the Bank's risk-bearing capacity, risk policy and the risk management process. The credit risk strategy defines the framework for the medium-term direction of IKB's credit business. Particular attention is paid to growth in various target groups and products, with a strong focus on credit portfolio management. The objectives stipulated by the credit risk strategy are implemented in the Bank's operative business through guidelines for managing individual credit exposures and portfolio risks. These guidelines are applied in each individual credit decision; they ensure the quality of new business – and hence, compliance with the credit risk strategy – through minimum parameters for qualitative and quantitative standards, and continuous monitoring of compliance with these parameters:

- risk policy provisions for acquiring new business, as defined in the "Guidelines on Managing Individual Credit Risks";
- credit approvals and credit monitoring for individual transactions;
- credit portfolio monitoring, management and limitation on the basis of "Guidelines on Managing Portfolio Risk" as well as extensive credit portfolio analyses; and
- regular checks conducted by Internal Audit.

Risk policy. The starting point for risk management in the lending business is a joint planning process involving the Board of Managing Directors and the business divisions, supported by Corporate Development, Risk Management, and Finance, Controlling and Taxation. The risk-bearing capacity, and growth and earnings targets provide the basis for explicitly including risk in the planning process. The derived targets, as well as encompassing volume of new business, interest and commission income and material and personnel costs, also cover risk and capital costs. The structural credit quality and securitisation structure is also agreed during the planning of risk costs with a sustained effect on new business, management of the portfolio, and portfolio structure. Another key element is imposing limitations by type of business and product or by sector, as well as regarding exposure to international borrowers, to individual counterparties, or to corporate groups.

Credit approval process and monitoring of individual exposures in traditional lending business. Credit analysis is carried out by the Risk Management unit, which is independent of the divisions. This guarantees separation of business development activities and loan approval (in other words, separation of front-office and back-office functions).

With the exception of minor decisions concerning existing exposures, the credit approval process is conducted either centrally, by duly authorised persons in the Risk Management unit, or by the Board of Managing Directors, within the scope of the regulation of approval powers; the required approval depends on the size of the Group's existing credit exposure, the borrower's credit quality, the collateral provided, the term, and not least, the existing and planned structure of the portfolio. The principle of dual control is always observed. Legally-trained staff members from the Legal department, who are not directly involved in the market, carry out the subsequent loan disbursement and contract implementation.

Every credit approval is based on a detailed credit analysis which outlines and assesses all information pertaining to the decision, subsequently documenting it clearly and straightforwardly in a decision proposal.

In this respect, use is made of a further tool that IKB has developed itself – known as the Portfolio Adviser – with which to manage decision processes regarding our portfolio at the level of individual transactions and commitments. This tool calculates various different risk factors on the basis of the client's credit quality, transaction-specific features such as term and collateral, and portfolio-related indicators. This means that even at the stage of acquiring new business, key momentum can be generated in terms of portfolio management. At the same time, the Bank strongly emphasises the mobility of loans – defined as their eligibility for placement with third parties. This reflects the importance of synthetic securitisation for its portfolio management process.

Existing credit exposures are treated similarly to new credit approvals; the associated processes and approval procedures are applied every twelve months and decisions are reviewed. In additional, individual sub-portfolios (including major individual exposures) are analysed within the scope of annual reviews conducted between Risk Management and the divisions, and strategies on handling exposures derived on that basis.

Approval and monitoring process for portfolio investments. Decisions in conjunction with portfolio investments are made on the basis of the "Guidelines on the management of portfolio investments". These stipulate the suitable asset classes, the minimum requirements in terms of ratings awarded by internationally recognised credit rating agencies and rating-based figures for individual investments on and off the balance sheet. The Guidelines also incorporate quality-based criteria for the definition of suitable investments.

Until portfolio investment activities were spun off with the creation on 1 September 2006 of IKB CAM, Treasury & Financial Markets operated as a front-office unit as defined in MaRisk. This meant that Treasury was responsible for sourcing potential new investments and for preparing the financing decision/the decision proposal. The responsible Risk Management team was in charge of preparing the back-office decision.

The transfer of Treasury employees responsible for portfolio investments and the Risk Management unit of IKB AG to IKB CAM meant the spin-off of front-office credit decision-making and significant risk analysis functions. The internal workflow and decision-making structure at IKB CAM was such that the investment officer was responsible for sourcing transactions, whilst preparing the transaction analysis (portfolio, manager and deal structure) in the form of an investment proposal was the task of the credit analyst. Once the investment proposal has been drawn up, the issuing of an investment recommendation was decided at the IKB CAM Investment Committee. Represented at this meeting, alongside the Chief Investment Officer who made the decision on the investment recommendation, were the team managers from Research and Credit Analysis and the responsible investment officer and credit analyst.

With the establishment of IKB CAM, filter processes were agreed by the Board of Managing Directors of IKB AG for investment recommendations to IKB AG and the Rhineland Funding conduit advised by IKB AG, on the basis of which IKB CAM could issue a commitment. The decision on a potential investment for IKB AG submitted by IKB CAM was made by the Board of Managing Directors Investment Meeting (VIS) on the basis of IKB CAM's investment proposal and the decision prepared by the back office. In the event of a negative decision (rejection) the investment already made by IKB CAM had to be disposed of again. In the case of transactions that did not meet the filter criteria, IKB CAM could not enter into a commitment. In this case, the decision was made by VIS based on IKB CAM's investment proposal and the back-office decision.

The filter criteria were also applied to investment recommendations submitted by IKB CAM to Rhineland Funding. The setting-up of IKB CAM also involved the transfer of the investment advisory mandate to the company. Up until 20 December 2006, IKB AG continued to act as investment advisor for portfolio investments. This role has been assumed by IKB CAM since 21 December 2006. If the filter criteria are met, an investment recommendation based on the decision of the investment committee of IKB CAM is possible. If the criteria are not met, the written prior consent of a member of the Advisory Board of IKB CAM, who thereby assumes joint responsibility for the "risk prospect", is required. An investment recommendation may only be submitted to Rhineland Funding with the approval of such a member.

Rating process and procedures. Assessing the credit quality of clients and investments is a key element of the entire credit process. Strict demands are made in terms of credit quality, and substantial collateralisation of our exposure required, when selecting business partners and investments. This requirement is implemented via corresponding lending guidelines.

IKB employs a computerised rating system for assessing credit quality in traditional lending business. This is designed specifically for the corresponding client segment or specific type of financing solution. The relevant model-specific risk parameters are grouped in each procedure and each customer is assigned a rating class within an 11-level internal scale ranging from 1 (best rating) to 6.0 in increments of 0.5. This rating scale is calibrated by the probability of default, on the basis of a statistical analysis of historical defaults. As well as providing an instrument with which to assess credit quality, our rating procedures therefore also enable us to calculate risk-based and risk-differentiated margins and provide a basis for determining economic capital for credit risk.

In the Corporate Clients division, IKB uses its concept of rating medium-sized enterprises – known as IKB Mittelstandsrating – which has been subject to ongoing enhancement over the last few years. This concept is also applied, where appropriate, in other businesses. A mathematical and statistical process is used to assess the borrower's economic situation on the basis of financial indicators. The specific characteristics of the individual client and sector are then examined on the basis of an expert system, which takes into account the size of the company and exposure involved, incorporating qualitative information to an increasing extent. By combining the results from the two procedures, we ensure a very high degree of rating quality and precision.

A special rating procedure takes into account the particular features of project finance and special finance, emphasising the extent and sustainability of available cash flow to meet the interest and principal payments arising during the lifetime of the project. We employ quantitative models to assess each exposure using various scenarios and simulations; the results are complemented by qualitative criteria on sponsors, operators, sales and procurement markets, and the specifications of the transaction concerned. A special rating procedure developed on the basis of the "IKB Mittelstandsrating" concept is used for acquisition financings.

The real estate ratings used as part of the commercial real estate finance business assess credit quality using a variety of specific property data and investor information. This not only includes detailed information on each property's location and condition, but also explicit details about the tenant structure and quality, individual credit quality assessment of the investors in relation to assets and liquidity, and the property's ability to cover interest and principal payments from cash flows generated.

Country rating is determined using economic data and indicators on the country's economic performance and its liquidity situation in conjunction with a qualitative assessment of the country's political and social situation. We obtain our information from international databases, country reports and other external sources.

Sector risk is incorporated using a rating process which IKB carries out on a regular basis for around 370 different industry sectors. The rating process is based on an econometric model incorporating domestic and international macro-economic trends as well as cross-sectoral relationships. We leverage the vast knowledge of sector experts in the Economics department.

Validation tests carried out using available data show that the internal rating procedures used classify the risks appropriately. A high degree of precision leads to better risk selection and thereby supports the Bank's portfolio management.

In the case of portfolio investments, at least two ratings awarded by internationally recognised credit rating agencies are available, any changes to these are systematically recorded as they occur. The limits defined in the Guidelines on Managing Portfolio Investments are based on such factors as these external ratings. Investments must have a rating of at least "BBB" or "Baa2" at the time of the transaction being concluded.

Quantification of credit risk. To quantify credit risk, and with regard to traditional lending business and portfolio business, we have in each case developed a proprietary model that takes into account information on each individual loan/investment (loan/investment amount, collateralisation, term, sector affiliation, group affiliation, rating and if applicable likelihood of liquidity facilities being drawn upon), in addition to a variety of statistical variables, such as probabilities of default, collateral realisation proceeds and sector/asset correlations. These variables are derived from the Bank's own historical data, or based on external reference data. The distribution of losses on the credit portfolio – the focus of the observation – is subdivided into 'expected losses' and 'unexpected losses'.

‚Expected loss' is a statistically anticipated value (which is also referred to as 'standard risk costs'), that is covered by the calculated risk premium.

In contrast, ‚unexpected loss' (also known as 'credit value at risk') reflects the potential risk that may exceed the expected loss.

Quality assurance. Internal and external ratings and mathematical models are increasingly being integrated into the entire credit process. Given their resulting impact on the management of the Bank as a whole, quality assurance has become crucially important. Regular validation and benchmarking processes are applied both to the internal systems for assessing credit ratings, as well as to the approval, monitoring and management processes within the lending business. The ensuing results not only serve as the basis for developing the credit processes, taking the aforementioned regulatory requirements (MaRisk and Basel II) into consideration. We also use them for optimisation according to the Bank's own requirements.

Portfolio monitoring and management. In terms of portfolio monitoring, the focus is on the credit portfolio as a whole. The task is to monitor the portfolio such that the concentration of risk in individual exposures, countries, target groups and products is duly limited. It also involves determining the main drivers of risk for the overall portfolio. Consequently, the Bank employs a set of management tools which regularly monitor all credit risks, taking into consideration any association within corporate groups. The portfolio is oriented by country, business division, rating class and industry. This form of portfolio management for portfolio investments is essentially based on the rating grades assigned by the rating agencies. It is obvious (especially in hindsight) that the key drivers of risk for portfolio investments was above all US sub-prime risk, which accounted for a large share of the value of the investment, plus the fact that as a result, the main concentration risks were not recorded adequately.

The structural credit quality of IKB's credit portfolio has gradually improved over recent years, thanks to the consistent implementation of the guidelines formulated in the risk policy when acquiring new business, the use of loan securitisation and sub-participations to transfer credit risk, and the economic recovery staged by the German Mittelstand in the recent past.

Credit rating structure of lending business as at 31 March (excluding non-performing loans)*

in € billion	2007	2006	2005	2004	2003
1/1.5	13.1	8.8	6.5	6.0	6.6
2/2.5	8.9	10.1	9.5	9.2	8.8
3/3.5	5.5	5.2	6.0	6.0	7.2
4/4.5	2.2	2.1	2.4	3.2	3.9
5 or higher	1.3	1.6	1.9	2.5	1.8
	31.0	**27.8**	**26.3**	**26.8**	**28.2**

*) Any discrepancies in the totals are due to rounding differences

IKB's Economics department is responsible for the timely monitoring of sectors and market changes. This extensive sector expertise forms a core element of cluster analyses carried out as part of the Bank's risk management process. The purpose of such analyses – which incorporate our expectations – is to identify and contain sector risks in lending business as early as possible.

Regular portfolio monitoring by the Limit Committee (comprising representatives of Risk Management, the Economics department, Credit Risk Controlling, and the business divisions) is the starting point for determining concentration limits, which are oriented on the target figures set by our business strategy, as well as by risk policy guidelines. Limits are defined in terms of volume and risk contribution at the various levels of the lending portfolio, taking into account the existing structure, historical performance, and risk quantification of the credit portfolio and their changes over time, as well as sector-specific risks and the impact of economic trends identified by the economists. Additional maximum thresholds for individual loans or loans to corporate groups are defined to prevent concentration risk.

In combination with risk placements carried out by IKB, this approach ascertains a high degree of diversification and granularity in the loan portfolios of the Corporate Clients, Real Estate Clients and Structured Finance segments. Accordingly, the potential impact of recessions in individual sectors is kept to a minimum.

Country risk limits apply to the total exposure in all countries. This means that transactions involving country risk may only be approved if there is still scope within the country risk limit, even in cases where the clients concerned have a good or very good credit standing. The limits are stipulated by the Limit Committee and apply to all transactions in the country concerned. Utilisation of these limits is monitored in near-real time, using a reporting system which provides information on a regular basis.

In addition to its lending business, IKB also invested in securitised international credit portfolios, in order to further enhance the diversification of its loan assets and the profitability of its portfolio. The volume of these investments stood at € 6.8 billion as at 31 March 2007. 98% of investments had an investment-grade rating at this time, of which approximately 73% had a triple-A or double-A rating.

Credit rating structure of IKB's portfolio investments as at 31 March (excluding Rhineland Funding)*

in € billion	2007	2006	2005	2004	2003
Aaa	2.1	2.2	1.8	1.4	0.8
Aa	2.9	2.5	1.7	0.7	0.5
A	1.2	1.2	1.0	0.5	0.2
Baa	0.5	0.5	0.3	0.3	0.3
Ba/B	0.0	0.1	0.2	0.1	0.1
Sub B	0.1	–	–	–	–
	6.8	**6.6**	**5.0**	**3.0**	**1.9**

*) Any discrepancies in the totals are due to rounding differences

Asset structure of IKB's portfolio investments as at 31 March (excluding Rhineland Funding)

in € billion	31 Mar 2007 Total		31 Mar 2006 Total	
Corporates	2.9	(42%)	2.9	(44%)
ABS	3.0	(45%)	2.8	(42%)
of which: including sub-prime exposures	2.4	(35%)	2.1	(32%)
CDO of CDO – ABS + Corporates	0.9	(13%)	0.9	(14%)
of which: including sub-prime exposures	0.2	(2%)	0.2	(3%)
Total	**6.8**	**(100%)**	**6.6**	**(100%)**

Alongside own investments, IKB has also advised portfolio investment companies (Rhineland Funding in particular) on their investments in securitised credit portfolios. IKB, in addition to other banks, provided these companies with liquidity facilities. The facilities provided by IKB had a total value of just under € 11.8 billion as at 31 March 2007, with approximately € 5.4 billion in liquidity facilities having been provided by the other banks.

These total liquidity facilities of € 17.2 billion existed as at the reporting date against some € 12.7 billion of investments, of which, as at the reporting date, € 11.5 billion are consolidated in the consolidated financial statements of IKB. The share of investments with a triple-A or double-A rating as at 31 March 2007 was around 85%.

Credit rating structure of Rhineland Funding portfolio investments as at 31 March*

in € billion	2007	2006	2005	2004	2003
Aaa	5.8	4.0	2.9	2.5	2.0
Aa	3.9	2.8	2.0	1.6	1.2
A	1.5	1.4	1.0	0.9	0.7
Baa	0.2	0.6	0.5	0.5	0.4
Ba/B	0.0	0.1	0.1	0.2	0.0
	11.5	**9.0**	**6.5**	**5.7**	**4.4**

*) Any discrepancies in the totals are due to rounding differences

Asset structure of Rhineland Funding portfolio investments as at 31 March*

in Mrd. €	31 Mar 2007 Total		31 Mar 2006 Total	
Corporates	0.4	(3%)	0.9	(10%)
ABS	10.3	(91%)	6.9	(77%)
of which: including sub-prime exposures	9.7	(85%)	5.9	(65%)
ABS + Corporates	0.3	(3%)	0.7	(7%)
of which: including sub-prime exposures	0.1	(1%)	0.1	(1%)
CDO of CDO – ABS + Corporates	0.4	(3%)	0.5	(5%)
of which: including sub-prime exposures	0.2	(2%)	0.2	(2%)
Total	**11.5**	**(100%)**	**9.0**	**(100%)**

Regional distribution of lending business (excluding IKB and Rhineland Funding portfolio investments). In addition to the investments in international credit portfolios referred to above, as at the reporting date € 7.6 billion of the total loan volume related to foreign countries, both within Europe and elsewhere. After deduction of exposures covered by credit insurance (such as Hermes) and placements with third parties, more than 99.4 % of this lending volume was classified in country risk classes 1 to 1.5, the two top grades.

Collateral, placement of risk with third parties and securitisations. In terms of IKB's traditional long-term lending business, classic forms of collateral (real property liens, transfer of ownership by way of security and guarantees) continue to be very important. Irrespective of whether a lending decision is imminent, the valuation of collateral provided in each case is continuously reviewed and updated.

This form of risk mitigation is supported by the portfolio-oriented placement of risks from individual exposures to third parties, by syndicating loans to other banks, or by placing risk through securitisation.

IKB is one of the leading issuers in securitisations of loans and advances to small and medium-sized enterprises. This is complemented by the securitisation of international structured finance and real estate finance exposures. This form of placement is used for the purposes of targeted portfolio management, enabling us to avoid any clustering of risks, and to optimise our use of regulatory capital.

Such domestic and foreign credit exposures have been placed in the capital market synthetically; whilst remaining in the IKB balance sheet, being refinanced and continuing to be looked after by the Bank in terms of the lending side, the counterparty risk exposure has been neutralised. We have used securitisation to place a total of just under € 18 billion with third parties over recent years. The total volume of loans and advances placed through securitisation exceeded € 7 billion at the reporting date. The current situation on the securitisation markets has led to a marked increase in hedging costs with regard to new securitisation transactions.

Identification and specific handling of exposures in danger of default. All exposures subject to credit risk are monitored on a permanent basis. This allows the Bank to draw up a current evaluation of the borrower's credit quality, and therefore to assess the risk structure of the loan portfolio. A computerised system is also used with regard to traditional lending business to facilitate early risk recognition, in order to implement suitable measures at an early stage, on the basis of risk indicators identified using sample patterns.

Specialist management units are responsible for managing exposures in danger of default. By implementing acceptable solutions at an early stage, this special management facility aims to preserve the company's ability to continue trading, or – should these efforts fail – substantially reduce the financial fallout.

Particular focus is placed on so-called non-performing loans. A loan is defined as being non-performing if insolvency proceedings have been instigated, if interest or principal payments are more than 90 consecutive days in arrears, or in the event of other clear signs that the debtor is unable to meet the contractual obligations and in the absence of any objective indications of subsequent payments or the realisation of collateral. In such cases account is taken of the liquidation value of the available collateral.

The following table provides an overview of the loans and advances that are classified as non-performing:

Non-performing loans

	31 Mar 2007 in € million	31 Mar 2006 in € million	Change in € million	Change in %
Domestic clients	1 750	2 225	–475	–21
Western Germany	943	1 166	–223	–19
Eastern Germany	807	1 059	–252	–24
International customers	82	98	–16	–16
Credit portfolio investments	128	0	+128	
Total	**1 960**	**2 323**	**–363**	**–16**
% of total loan volume[1)]	4.9	6.3		

[1)] The total loan volume comprises loans to customers, loans to credit institutions, securitised lending, operating and financing lease agreements, as well as guarantees and credit default swaps. Excluding the consolidated investments of RFCC

The reduction in non-performing loans is attributable to a stringent workout process (also refer to Note 33 “Provision for possible loan losses”), and to measures adopted on the basis of the early detection of risks.

Risk provisioning. With regard to financial instruments carried at amortised cost, as well as for contingent liabilities, risk provisioning takes the form of a provision, a write-down or a value adjustment, which is then carried in the income statement as the amortisation or value adjustment of receivables. Additions of provisions for possible loan losses are recognised in the income statement. With regard to products carried at fair value, any changes in value due to changes in credit quality are taken into account when determining fair value.

The corresponding value adjustments – which are determined by Risk Management – take into account both expected future cash flow and the value of collateral available. Each case is assessed individually by Risk Management, which in turn determines the workout strategy and estimates the incoming payments achievable in future. This procedure applies accordingly to on-balance sheet portfolio investments and, as at 31 March 2007, resulted in risk provisioning for these investments for the first time.

Financial instruments carried at amortised cost are also checked for the existence of any deferred impairment. For portfolios with similar credit risk characteristics we engage in lump-sum provisioning for possible loan losses if there are objective indications that loans may be at risk of being non-performing but cannot yet be individually calculated. Further details relating to provisions for possible loan losses can be found in Notes 22 and 33.

Overall, provisions for possible loan losses were down by just under 20%, from € 319 million in the previous financial year to € 259 million. The total allowance for possible loan losses thus amounted to € 1,142 million as at 31 March 2007.

Liquidity risk and market price risk

Liquidity risk. A distinction is made between two types of liquidity risk: the risk that current or future payment obligations cannot be met on time, or in full; and the risk that required funding can only be obtained at less favourable market conditions.

Regular liquidity analyses and cash flow forecasts were carried out during the reporting period to ensure that sufficient liquidity was available at all times. To secure liquidity, negotiable variable-rate securities were held that could be sold or used as collateral where appropriate. The Bank has also made regular use in the past of the Central Bank's tender facilities, through which the banking system is supplied with liquidity.

To quantify the level of back-up liquidity needed, a system is being established which is designed to take sustained market disruptions into account – through to the complete collapse of market activities – over a defined period, observing external requirements (specifically, the liquidity ratio according to the German Banking Act).

The Bank's long-term refinancing requirement based on balance-sheet assets is calculated and regularly updated in a process coordinated between the Treasury and the Finance, Controlling and Taxation department, on the basis of how we expect business to develop. Given IKB's broad refinancing basis and placement strength on the capital market up until July 2007, it was possible to procure adequate refinancing for all lending operations in terms of the required maturity structure and conditions – even in difficult market phases. Details on measures the Bank will take to secure liquidity in the future can be found in the Outlook.

Market price risk. Market price risks comprise interest rate, volatility, currency and price risks for shares and other assets. We manage these risks as part of a risk management process that conforms with the Minimum Requirements for Risk Management (MaRisk).

Limit system. Daily reporting to the Board of Managing Directors forms a cornerstone of managing market price risk, backed by a differentiated limit system that is geared primarily towards a market value-oriented limitation of interest rate, equity and exchange rate risks, and of risks from options positions. The Board of Managing Directors sets limits for the Treasury division, on the basis of the Bank's risk-bearing capacity as also set by the Board. Based on this limit system, the Treasury implements its market expectations in investment and refinancing strategies.

IKB differentiates between the portfolios of proprietary trading, proprietary investment (further broken down into two sub-portfolios: fixed-income fund and investment portfolio), and refinancing of lending operations. These portfolios are valued daily in relation to market risks. Their risk content is measured using a value at risk (VaR) system based on present values, which forms the basis for limiting market risks. The limit system combines performance and VaR limits for various scenarios at Group level and is strictly governed by the Bank's risk-bearing capacity.

Portfolios that are carried at amortised costs are not included here. Given their purpose as long-term investments held until final maturity, their market price fluctuations are not measured daily but only result in value adjustments in the event of long-term impairment.

Quantification of market price risk. IKB employs various mathematical models to quantify interest rate and spread risk. These models use historical simulation in order to determine the risk exposure inherent in the Bank's major positions. To ensure that the characteristics of each product are properly taken into account, this historical simulation also incorporates a revaluation of instruments, using observed yield curve data, and incorporating correlation effects. The exposure to currency risks in the total portfolio is insignificant. Currency risks are limited by means of restrictions with regard to the volume of open currency positions.

Risk measurement in proprietary trading. The basis for the quantification of the interest rate risk is a value at risk model which uses a variance-covariance approach with a confidence level of 95% and a holding period of ten days. During the risk measurement process, historical observation periods of 510 and 60 days are used. The higher value at risk figure of the figures calculated during the risk measurement process is used for risk reporting. In addition, the risk is calculated for worst-case scenarios which can be derived from historical interest rate developments. A scenario matrix approach implemented in the Kondor+ system is applied by IKB for options, in order to take account of interest rate and interest volatility risks. The equity price risk is calculated on the basis of the standard procedure as defined in the capital ratio according to the German Banking Act (Grundsatz I).

Risk measurement in the fixed-income fund, and in the investment portfolio. The main risks assumed by the Bank in these two portfolios are interest rate and volatility risks. Risks associated with equity prices and currency exchange rate movements are less important.

A historical simulation is primarily used to measure risk. When quantifying the risk exposure to own funds invested on a long-term horizon in the fixed-income fund, for the purpose of optimising net interest income, the simulation is based on corresponding assumptions regarding maturity and return. Simulation parameters are mirrored (and the number of simulation scenarios thus doubled) to determine VaR within the scope of stress testing. Maturity assumptions regarding the own funds invested in the fixed-income fund are not taken into account for stress test analyses.

Risk measurement in loan refinancing. In order to calculate the currency and interest rate risks associated with loan refinancing, IKB uses the discounted balances from the interest rate gap analyses and historical simulation.

Aggregation of risk measurement figures. For the purposes of risk aggregation, the risks of the trading book and the banking book are taken into account. The aggregation of the risk measures is performed by adding the VaR figures of the sub-portfolios, assuming full correlation of the results. This conservative procedure tends to result in an over-estimation of risk.

Quality assurance. Backtesting is regularly carried out in order to verify the accuracy of projections obtained using our models. The results are reported to the Board of Managing Directors. This backtesting has shown to date that our value at risk projections accurately forecast the daily profit fluctuations, in proprietary trading, proprietary investment, and lending refinancing.

Reporting. To monitor market risk and to support Market Risk Management, detailed information on the results of operations and risk exposure of the above-mentioned portfolios are submitted to the responsible members of the Board of Managing Directors and Treasury on a daily basis. Once a month, the member of the Board of Managing Directors responsible for Finance, Controlling and Taxation provides an extensive report to the entire Board on market developments, results and risk situation of these positions. In this context, the fundamental framework and interest rate assessment presented by our economists are reported, and their potential impact analysed jointly with representatives from Treasury and from Finance, Controlling and Taxation.

Operational and reputational risks

Operational risks reflect the risk of a loss being incurred due to a shortcoming or failure of internal processes, individuals and systems, or due to external events outside of the Bank’s control, irrespective of whether such loss was caused intentionally or by chance, or whether it occurred naturally.

Management of operational risks. The management of operational risk is coordinated and monitored by Operational Risk Management (ORM), which reports directly to the Chief Risk Officer. ORM is also responsible for analysing the loss potential throughout the Group, and for developing Group-wide operational risk management training concepts.

Each business division, corporate centre and subsidiary is responsible for managing risk at an operational level, within their respective area of control. In this context, the emphasis is not only on regular analysis and identification of deficiencies, and on approaches for optimising all business procedures and processes, but also on the development of the Bank's security organisation and on adapting the underlying processes. This ongoing development takes into account the increasingly complex and international nature of the IKB Group's business. For this purpose, ORM arranges for annual business impact analyses, the purpose of which is not only to reflect specific risk profiles of individual divisions or departments, but also to highlight potential risk areas.

All business units must report all losses that have occurred – as well as any "near misses" – to Operational Risk Management, which maintains a central loss database. All losses are examined to establish their causes and the impact on IKB's control principles. In this way, valuable recommendations for improvement are obtained and can subsequently be implemented.

Operational Risk Management is also responsible for business continuity planning throughout the IKB Group. This planning is kept up to date by means of regular business impact analyses. To guarantee transparency throughout the Group, all emergency plans are detailed in the Bank's intranet, and in printed form in the Business Continuity Planning manuals.

Regular drills conducted throughout all divisions and subsidiaries ensure the quality of these emergency plans.

The risk audits conducted up until the end of the reporting year showed that the Bank does not face any disproportionate risks from its operational risk fields. Measures have been implemented to avoid all identified risks, and opportunities for early recognition of negative developments and the relevant emergency precautions have been recognised. Where necessary, corresponding insurance cover has been arranged.

Legal risks. Also included as a form of operational risk is legal risk, in other words the risk of losses being incurred as a result of new statutory regulations and as a result of amendments to or interpretations of existing statutory provisions (such as supreme court judgements) that are detrimental to the Bank. The responsibility for limiting legal risks lies with IKB's Legal department, which in turn relies on the support of external legal advisors where necessary. All standard contracts are continuously monitored to determine whether adjustments are required on the basis of changes to the statutory provisions or to case law. Legal risks arising after the onset of the crisis will be explained in the Report on Material Events After the Reporting Date.

IT risks. IT risks focus on the measures required to develop our business continuity planning, as well as on the security of the Bank's IT systems and of its data inventory. Measures taken in this context have included the implementation of a uniform safety standard (ISO 17799 "Code of practice for information security management" and ISO 27001 "Information technology – Security techniques – Information security management systems – Requirements"); the roll-out of new technologies to avert external threats in order to enhance the Bank's network security and to comply with increasing requirements regarding the mobility and availability of IT systems; as well as the extension of backup systems which allow the further reduction of operational risk exposure concerning the Bank's communications, IT and settlement systems. At the same time, the Bank's IT employees undergo continuous training so that they are prepared for every eventuality. IKB's implementation of a suitable management system for information security was certified by TÜV Rhineland during the past financial year.

All of these measures are further reinforced through regular reviews and emergency drills. By means of the measures taken, the Bank has accounted for all material risks.

Compliance risks. Very strict statutory provisions apply to the financial sector in particular. Additional rules and regulations were implemented to ensure that our employees always conduct themselves correctly and consistently with the relevant laws: most importantly, conflicts of interest need to be avoided and market manipulation or insider trading prevented. This was the reason behind our developing a Code of Conduct which reflects IKB's values and beliefs. The principles laid down in the IKB Code of Conduct represent the standards of conduct which apply to all members of staff throughout the IKB Group. These rules form a binding framework, guiding the Bank's employees in their day-to-day business.

Personnel risks. Operating entities – in cooperation with Human Resources – are responsible for managing personnel risks. Besides making sure that adequate personnel cover is available to fulfil operational and strategic requirements, this also includes ascertaining that staff have the skills and experience that they need to perform their duties and fulfil their responsibilities. To maintain the high level of staff qualification, IKB employs an extensive, continuous system to manage training and CPD measures. The risk of a sustained disruption of operations caused by absence of employees, or staff leaving the company, is contained by IKB through clearly-defined substitution regulations and guidelines to preserve functional availability. These are reviewed on a regular basis, and amended if necessary.

Reputational risks. Reputational risks are the risks of losses, falling revenues, rising costs or loss in value due to a deterioration in the Bank's public reputation, and particularly in its reputation amongst clients, shareholders, rating agencies, and employees. Risks to reputation frequently arise from other risk types, reinforcing the original risk through the related publicity.

Strategic risks

Strategic risks are defined as potential threats to the Bank's long-term profitability. These can be triggered not only by changes in the legal or social environment, but by the market or competitive environment, IKB's customers, or its refinancing partners.

Since there is no regularity to strategic risks, they are difficult to quantify as special risks in an integrated system. They are therefore specially monitored by the Board of Managing Directors and Corporate Development, and are subject to constant analysis. This includes regular checking of business division strategies within the framework of the strategic planning process, and of the resulting strategic initiatives and investments.

Business risk

Business risk is defined as the risk of negative deviations from target levels of income (comprising commissions and interest) and expenses.

Each business division, corporate centre and subsidiary is responsible for managing general business risk – defined as the threat of deteriorating profitability, within the framework defined by the business strategies agreed upon with the Board of Managing Directors – on an operative level, within their respective area of control. The Results Controlling unit, part of Finance, Controlling and Taxation, monitors earnings and cost developments during the course of a financial year, via on-going target/actual comparison, and reports its results to the Board of Managing Directors and to the divisions on a monthly basis.

General business risk is quantified by way of statistical analysis, using empirical volatility data for earnings and costs. The model employed calculates the extent by which actual net commission income and net interest income, and costs, have deviated historically from the corresponding targets. The economic capital tied up as a result is taken into account for the regular analysis of the Bank's risk-bearing capacity.

Risk reporting and communication

All relevant information compiled from the trading and credit businesses, from Risk Management, from Finance, Controlling and Taxation, and from Human Resources as well as from the other units is processed and examined. This is then presented and explained in detail, at least once a month, to the Board of Managing Directors, and to the heads of divisions.

The credit risk report contains the information relevant to the Group's total risk position, and contains comprehensive information on the credit risk to which the Bank is exposed. Besides structural developments within the portfolio (credit quality data, collateralisation, loan terms, sector and country diversification), it also outlines the development of impaired or non-performing receivables, and provisions for possible loan losses, in an up-to-date and comprehensive presentation. These details also include measurements on the level of concentration with the portfolio. In addition to the presentation and explanation of special exposures and developments, the report also contains an overview (including a quantification) of all individual types of risk, to monitor the Bank's risk-bearing capacity also in stress scenarios, and information regarding utilisation of all economic capital limits. Nevertheless, sub-prime risks were not seen as special risk factor in the portfolio.

We regularly match the risk/return figures of the lending business with up-to-date planning and target figures, and report the results to the Board of Managing Directors and to the heads of business divisions. This allows us to counter deviations at an early stage.

All business divisions and corporate centres therefore have access to extensive, necessary and up-to-date information. Within the scope of market price risk reporting, in addition to daily monitoring of, and reporting on, limit utilisation, Risk Controlling prepares a daily briefing for the responsible members of the Board of Managing Directors, Treasury and other units involved. This includes marking the Bank's positions to market, together with accrued and risk-free net interest income generated from the Bank's refinancing activities and proprietary investments. This briefing also includes a statement of the present value exposure under a stress scenario, the utilisation of various market price risk limits, and comments on particular developments.

Operational Risk Management keeps the Board of Managing Directors informed regarding operational risk, as well as individual losses and their distribution amongst the divisions.

Core content of the risk situation

The 2006/07 financial year was characterised by a reduction in provisioning for possible loan losses, and in non-performing loans. Within the scope of the annual review, we adjusted the credit risk strategy during the 2006/07 financial year where necessary, in line with the strategic orientation of the credit business.

The strategy for managing operational risk was updated during the financial year under review, and implemented throughout the IKB Group; reporting lines were harmonised and linked with the various sources of operational risk data.

All remaining projects for the implementation of Minimum Requirements for Risk Management (MARisk) were completed during the 2006/07 financial year. We remained committed to continuing the project that involved preparations for Basel II; it was successfully completed at the end of 2007.

Observation of the Bank's risk-bearing capacity over the 2006/07 financial year indicated that, from the perspective of a non-subordinated lender, the aggregate risk cover was sufficient even in cases of unexpected risks under stress scenarios materialising. The measurement systems and processes implemented within IKB's framework of risk monitoring and management are generally suitable for the early identification and adequate capture of risks. However, following the reporting date, the previous methods used to value those portfolio investments for which active markets ceased to exist in late July are seen to be no longer sufficient.

4. Remuneration Report for the Financial Year 2006/07

This Remuneration Report relates to the remuneration of the members of the Board of Managing Directors and Supervisory Board in/for the 2006/07 financial year and describes how the remuneration systems in/for this financial year are designed. It takes into account the regulations of the German Commercial Code as amended by the German Act on the Disclosure of Remuneration of Management Board Members (Vorstandsvergütungsoffenlegungsgesetz – VorstOG), as well as by the general principles of the German Corporate Governance Code. At the same time, it should be regarded as an integral part of the Group Management Report.

The remuneration system for members of the Board of Managing Directors

Several significant changes took place regarding the composition of the Board of Managing Directors in the financial year 2006/07. The following were members of the Board of Managing Directors during the period to which this Remuneration Report relates: Stefan Ortseifen, Frank Braunsfeld, Dr. Volker Doberanzke, Dr. Markus Guthoff, Claus Momburg, Joachim Neupel and Frank Schönherr. Frank Schönherr and Joachim Neupel retired from the Board as at 30 November 2006 and 31 December 2006 respectively. Dr. Volker Doberanzke was appointed as a member of the Board of Managing Directors with effect from 1 June 2006, and Frank Braunsfeld was appointed with effect from 1 March 2007.

The total remuneration of the members of the Board of Managing Directors consists of a fixed annual basic remuneration, a performance-based variable remuneration as well as additional benefits and pension commitments. There are no stock option plans or similar schemes. The structure of the remuneration system for the Board of Managing Directors is subject to regular discussion and review by the Supervisory Board, as proposed by the Executive Committee of the Supervisory Board.

Given the current situation facing the Bank and also due to the fact that a new major shareholder could have a key influence on the remuneration of the Board, no work is currently being undertaken to develop a new structure. The remuneration of the Board of Managing Directors is determined on an individual basis by the Executive Committee.

The criteria for the reasonableness of remuneration are, in particular, the tasks of the respective member of the Board of Managing Directors, his personal performance, the performance of the Board of Managing Directors as a whole, as well as the economic situation, the performance and outlook of the Company, taking into account its peer companies. The appropriateness of the respective total remuneration is also reviewed regularly. Any remuneration from offices held within the Group is taken into account for this purpose.

Non-performance-related remuneration components. The non-performance-related basic annual remuneration is paid monthly in form of a salary. In addition, the Board members receive additional benefits in the form of remuneration in kind which mainly consist of insurance premiums, use of a company car and the property value of the rented company accommodation of Joachim Neupel and Stefan Ortseifen to be applied in accordance with tax laws. These additional benefits must be disclosed as remuneration in each Board member's personal tax return. The actual amount of these benefits varies according to the individual circumstances of each Board member. Loans and advances were not granted to the Board members in the year under review.

Performance-based remuneration components. The amount of the variable remuneration is determined by a target agreement system: for financial year 2006/07, this included targets that depend on the success of the company (65%) and individual targets (35%). The targets depending on the company's success relate to the operating result, the cost/income ratio and the return on equity in the consolidated financial statements. The individual targets include divisional, functional, and project-related targets. The first step in this process is to set a target bonus. The bonuses earned are then determined according to the extent to which the targets have been reached. As a rule, it is not possible to change the agreed performance targets retroactively. In the 2006/07 financial year, the variable remuneration amounted to approximately 63% of the total remuneration paid; this figure is based on the payments made before the onset of the crisis affecting the Bank. The maximum bonus actually paid amounts to 200% of the target bonus, the minimum bonus is 30% of the target bonus.

The variable remuneration for the 2006/07 financial year was determined at the meeting of the Executive Committee on 13 February 2007, in other words a relatively long time before the outbreak of the crisis in late July 2007, and was paid immediately following approval on 27 June 2007 of the financial statements presented in May 2007. The restatement of the financial statements as at 31 March 2007 made it necessary to review and reset the targets agreed upon with members of the Board of Managing Directors. Demands will be made to repay the variable remuneration, except the minimum bonus.

In accordance with the recommendations of the German Corporate Governance Code, the monetary components of the total remuneration comprise fixed and variable components. Except for the 30% minimum of the target bonus, the variable remuneration component is risk-based, as it does not constitute guaranteed remuneration. As a rule it is not possible to change the agreed performance targets retroactively.

Pension provisions. Having retired from the company, the members of the Board of Managing Directors are entitled to pension payments in the following cases: upon reaching the standard retirement age limit of currently 63 years, permanent disability, early retirement or the non-renewal of the service contract. In the case of the latter, the member of the Board of Managing Directors receives a reduced pension payment, as a so-called transition payment, until his 63rd birthday. This payment is made provided that early retirement or the non-renewal of a contract has not been caused due to his negligence (gross negligence or intentional damage) or by the rejection of equal or more favourable terms offered in relation to extending the contract. No transition payments will be made to members of the Board of Managing Directors who resigned as a consequence of the crisis.

The annual pension entitlement amounts to between 30% and 75% of the final basis annual remuneration and is dependent on the member's term of office on the Board of Managing Directors. The transition payment, which amounts to between 5% and 75% of the final basic annual remuneration, depends on the age of the member of the Board of Managing Directors and on his term of office on the Board. Pension claims and earnings otherwise acquired will be offset to a certain extent against the pension payments made by the Company. Current pensions will be adjusted annually in accordance with the performance of the German consumer price index.

After the death of an active or former member of the Board of Managing Directors, a reduced pension is paid out as a provision for dependants. Widows receive up to 60% of the pension for the rest of their lives. The widow's benefit is discontinued upon remarriage. Dependant children receive 15% of the pension until their 18th year, and up to maximum their 25th year for the term of their education including national or civil service. If the aggregate of the widow's benefit and orphan's allowance exceeds the pension payment, the orphan's allowance is reduced by the excess amount.

The company has recognised pension provisions in accordance with German Commercial Code for future pension claims of members of the Board of Managing Directors.

The new members of the Board appointed on 29 July 2007 and 15 October 2007 have no pension provisions or have pension provisions that differ from the terms set out here.

Change of control. In the event of a term of office as member of the Board of Managing Directors being ended prematurely due to a change of control, the members of the Board who were in office during the 2006/07 financial year shall have a general entitlement under their contract to payment of a one-off settlement payment and a transitional allowance. According to the rules, a change of control is deemed to have occurred in the event that a third party, either alone or through the voting rights attributable to that third party in accordance with Section 22 of the German Securities Trading Act (Wertpapierhandelsgesetz – WpHG), acquires a share of voting rights that, at an ordinary general meeting of the Company, would have led to that third party holding a share of voting rights in the amount of at least half of the share capital present at the meeting and entitled to vote. If a change of control leads to the early termination or non-renewal of the service contract, regardless of whether under the instruction of the company or of a member of the Board of Managing Directors, because the change of control impacts significantly on the Board member in question, the member is entitled to severance pay of at least three times the variable annual remuneration as well as a transition payment until his 63rd birthday, after which time the member shall be entitled to pension payments in accordance with the aforementioned regulations on pension provisions. Different rules on settlement payments may result from individual termination agreements.

The agreements entered into with members currently active on the Board of Managing Directors do not contain a change-of-control clause.

No member of the Board of Managing Directors received payments or corresponding commitments from a third party during the past financial year in relation to his activity as member of the Board of Managing Directors.

Details of the remuneration paid to the members of the Board of Managing Directors for the financial year 2006/07 are shown in the following table:

	Annual remuneration				**Pensions**	
€ thousand	Fixed remuneration	Variable amounts*)	Value of ancillary benefits*)	Total	Annual remuneration at retirement as at 15 Feb 2008	Additions to pension provisions as at 31 Mar 2007
Stefan Ortseifen	504	1 000	93	1 597	326	232
Frank Braunsfeld (from 1 Mar 2007)	25	35	14	74	77	437
Dr. Volker Doberanzke (from 1 June 2006)	300	750	32	1 082	38	113
Dr. Markus Guthoff	384	750	59	1 193	131	89
Claus Momburg	384	750	53	1 187	308 ***)	116
Joachim Neupel ****) (until 31 Dec 2006)	288	563	96	947		
Frank Schönherr****) (until 30 Nov 2006)	256	470	31	757		
Total	**2 141**	**4 318**	**378**	**6 837**	**n. a.**	**987**

*) Variable remuneration paid; following the restatement of the financial statements for the 2006/07 financial year, the Supervisory Board will demand repayment of variable components paid to members of the Board of Managing Directors
**) Including remuneration of € 225,000 received for directorship functions carried out at subsidiaries.
***) Assumes the Board member will remain in office until his 63rd birthday
****) Total remuneration of former members of the Board of Managing Directors and their dependants include pensions/transfers to pension provisions of Joachim Neupel und Frank Schönherr

For the financial year 2005/06, the annual remuneration of the entire Board of Managing Directors amounted to € 6,068,000, of which € 2,368,000 related to fixed remuneration components and € 3,700,000 to variable components.

Former members of the Board of Managing Directors and members who retired before the end of the 2006/07 financial year. Total remuneration paid to former members of the Board of Managing Directors and to members who retired before the end of the 2006/07 financial year and their surviving dependants in the form of disbursements, personal and non-cash contributions and pension provisions amounted to € 5,622,000 (previous year: € 3,147,000). A total of € 37,227,000 in provisions was recognised for pension obligations to former members of the Board of Managing Directors and their surviving dependents.

Further information on the remuneration package for members of the Board of Managing Directors is disclosed in the Notes to the Consolidated Financial Statements.

The remuneration system of the Supervisory Board

The remuneration of the Supervisory Board is governed by Article 11 of the Memorandum and Articles of Association of IKB. In line with legal requirements and in accordance with the provisions of the German Corporate Governance Code, this remuneration takes into account the responsibility and the scope of activities of the Supervisory Board members, as well as the economic situation and the performance of the IKB Group. The members of the Supervisory Board receive a fixed remuneration component as well as two variable, performance-based remuneration components. The short-term component is based on the dividend, whilst the long-term component depends on the three-year average for Group net income per share but is only paid if a dividend of at least 4% of the share capital is paid out. The members of the Supervisory Board receive a fixed remuneration in the amount of € 20,000.00 for each financial year, in addition to the reimbursement of their expenses, which shall also include value-added tax incurred on their remuneration. In addition, the Supervisory Board members receive a variable remuneration for each financial year in the amount of € 200 for each € 0.01 by which the dividend distributed to shareholders exceeds € 0.30 per share for the past financial year. Furthermore, the Supervisory Board members receive another variable remuneration in the amount of € 90 for each € 0.01 by which the three-year average of net income per share for the year exceeds € 0.30.

The Chairman of the Supervisory Board shall receive twice the amount of a normal member of the Supervisory Board, while each deputy shall receive one and a half times as much as a normal member. The remuneration is further increased for each membership in a Supervisory Board committee by 25% of the remuneration of a Supervisory Board member, and for each chairmanship in a committee by 25% of the remuneration of a Supervisory Board member. The additional remuneration for committee work may not exceed the amount of the remuneration for a Supervisory Board member. For members of the Supervisory Board who have not been Board or committee members for the full financial year, remuneration is paid on a pro-rata basis for each commenced month of their activities.

The remuneration of the Supervisory Board depends on other key figures than the remuneration of the Board of Managing Directors, which means that an unintended harmonisation of the remuneration interests of both corporate bodies is not possible. The fixed annual remuneration of € 20,000 is intended in particular to take account of the Supervisory Board‘s independence, which is necessary for the Board to perform its supervisory function. The new system is also aimed at ensuring an appropriate minimum remuneration that does not depend on the economic success of the Company. The aim of the dividend-based remuneration component is to create a certain harmonisation of the Supervisory Board's remuneration interests with the return expectations of the shareholders. By linking another part of the variable remuneration to the three-year average of the net income for the year, the Supervisory Board‘s remuneration also contains a component which is based on the Company‘s long-term success.

The remuneration of the Supervisory Board. No variable remuneration will be paid to the members of the Supervisory Board for the 2006/07 financial year assuming that, in light of the Company's situation, no dividend will be paid.

During the year under review, the members of the Supervisory Board did not receive any further remuneration or benefits for personally rendered services, in particular advisory and agency services, over and above their fixed remuneration.

Details for the remuneration of the members of the Supervisory Board for the financial year 2006/07 are shown in the following table:

€ thousand	Total (fixed component only; no variable remuneration since no dividend will be paid)
Dr. Ulrich Hartmann	55
Detlef Leinberger (since 31 Aug 2006)	30
Hans W. Reich (until 31 Aug 2006)	19
Dr. Alexander v. Tippelskirch	40
Dieter Ammer	20
Jörg Asmussen	20
Dr. Jens Baganz	20
Dr. Jürgen Behrend	20
Wolfgang Bouché	23
Hermann Franzen	20
Dr. Mathias Kammüller	20
Wilhelm Lohscheidt (until 31 Aug 2006)	8
Jürgen Metzger	20
Roland Oetker	20
Dr. Eberhard Reuther	20
Randolf Rodenstock	20
Rita Röbel	20
Dr. Michael Rogowski	20
Jochen Schametat (since 31 Aug 2006)	13
Dr. Carola Steingräber	22
Dr. Martin Viessmann	20
Ulrich Wernecke	20
Andreas Wittmann	20
Subtotal	**510**
Total travel expenses/VAT for the Supervisory Board	183
Total	**693**

For the 2006/07 financial year, the fixed annual remuneration paid to the Supervisory Board amounted to € 693,000, of which € 183,000 related to travel expenses and VAT.

For the financial year 2005/06, the annual remuneration of the Supervisory Board amounted to € 1,247,000, of which € 510,000 related to fixed remuneration components and € 571,000 to variable components. A further amount of € 166,000 related to travel expenses and VAT.

Further details can be found in the Notes to the Consolidated Financial Statements.

5. Other Financial Information

Disclosures required under sections 289 (4) and 315 (4) of the German Commercial Code (Handelsgesetzbuch – "HGB")

The company's share capital amounted to € 225,280,000 as at 31 March 2007, and comprised 88,000,000 notional no-par value bearer shares (bearer unit shares). On 07 January 2008, IKB issued a € 54.3 million mandatory convertible bond, excluding shareholders' pre-emptive rights, which was subscribed by KfW Banking Group. The convertible bond was convertible into shares in the Company of up to 10% of its share capital. The terms of the convertible bond provide for an early conversion obligation if certain conditions are met. These conditions have subsequently been met, triggering the conversion obligation; as a result, IKB is obliged to issue shares from conditional capital. These shares from conditional capital are expected to be issued to the holder(s) of the bonds on the day preceding the General Meeting on 27 March 2008. Therefore, IKB's issued share capital is expected to amount to € 247,794,332.16 at the time of the General Meeting, consisting of 96,794,661 shares. All shares entitle the holder to the same rights. Each share grants the holder one vote and determines the participation in profit.

The Federal Republic of Germany holds an 80% stake in the KfW Banking Group, based in Frankfurt am Main. Through its wholly-owned subsidiary KfW-Beteiligungsholding GmbH, Frankfurt am Main, the KfW Group holds 37.8% of the voting rights in IKB. The Stiftung zur Förderung der Forschung für die gewerbliche Wirtschaft (Industrial Research Foundation), Cologne, also holds an 11.8% interest in the company. The remaining capital is held by institutional and private shareholders.

The members of the Board of Managing Directors are appointed and dismissed by the Supervisory Board in accordance with section 84 of the German Stock Corporation Act (Aktiengesetz – "AktG") and Article 6 of the Memorandum and Articles of Association. The Board of Managing Directors is composed of at least two members, with the number of members being determined by the Supervisory Board. The appointment is made for a maximum term of office of five years. This term of office may be renewed or extended for a maximum of five years in each case. The Supervisory Board may revoke the appointment of a member of the Board of Managing Directors on serious grounds. The Articles of Association may only be amended by means of a resolution adopted at the General Meeting in accordance with Section 179 (1) of the AktG and Article 17 of the Memorandum and Articles of Association. Any resolution to amend the Memorandum and Articles of Association must be supported by two thirds of the share capital represented at the meeting, with the exception of cases where the German Joint Stock Corporations Act prescribes a larger majority. Any changes to the Memorandum and Articles of Associations that only affect the wording thereof may also be adopted by the Supervisory Board.

Pursuant to a resolution adopted by the General Meeting of 9 September 2004, the Board of Managing Directors was authorised, subject to approval by the Supervisory Board, to issue convertible bonds and/or bonds with warrants with an aggregate nominal value of up to € 300,000,000 with or without a limited term, and to grant the holders of such bonds conversion or option rights relating to shares in the Company accounting for up to € 22,528,000 of the share capital in accordance with the stipulated conditions up until 8 September 2009. Use has been made of this authorisation and of the related conditional capital as described in relation to the development of share capital.

Report of the Board of Managing Directors in accordance with sections 289 (4) and 315 (4) of the German Commercial Code (HGB)

The Board of Managing Directors has made disclosures in the Company's Management Report and in the Group Management Report in accordance with sections 289 (4) and 315 (4) of the HGB, with reference to which it comments as follows:

- The composition of share capital is based on Article 5 of the Memorandum and Articles of Association. The Company has only issued ordinary shares. No preference shares vesting special rights for individual shareholders have been issued

- IKB, in the KfW Banking Group and Stiftung Industrieforschung, has a group of shareholders that is committed to medium-sized businesses and that supports the focus on long-term corporate finance.

- Members of the Board of Managing Directors are appointed and dismissed in accordance with the statutory regulations and pursuant to the conditions of our Memorandum and Articles of Association. In accordance with the Internal Rules of Procedure for the Supervisory Board, the Supervisory Board elects the Chairman of the Board of Managing Directors from the members of the Board of Managing Directors. Changes to the Memorandum and Articles of Association are made to the extent permitted by law.

- The arrangements in place with the members of the Board of Managing Directors relating to a potential change of control are also set out in the remuneration report and do not require further clarification. The employment contracts of the employees do not contain any provisions relating to a change of control.

Disclosures in accordance with Section 312 of the German Stock Corporations Act (AktG)

IKB has prepared a subordinate status report in accordance with section 312 of the AktG. This report is not published. The final declaration of the Board of Managing Directors in the subordinate status report reads as follows: "IKB received appropriate consideration for each legal transaction set out in the report on transactions with related parties. This assessment is based on the circumstances known to us at the time of issues subject to reporting requirements. We did neither take nor omit to take any measures within the meaning of Section 312 of the German Stock Corporation Act (AktG)."

Restated Financial Statements of IKB Deutsche Industriebank AG

Restated Balance Sheet of IKB Deutsche Industriebank AG

Assets	in € thousand*		31 Mar 2007 in € thousand	31 Mar 2006 in € thousand
Cash reserve				
a) Cash on hand			30	37
b) Balances with central banks			28 253	43 969
of which: with Deutsche Bundesbank	28 090	(43 907)		
c) Balances in postal giro accounts			102	27
			28 385	**44 033**
Loans and advances to banks				
a) Payable on demand			590 632	1 477 483
b) Other loans and advances			11 983 287	8 515 857
			12 573 919	**9 993 340**
Loans and advances to customers			**24 933 791**	**22 231 093**
of which: Loans to local authorities	1 531 686	(1 567 807)		
Debt securities and other fixed-income securities				
a) Bonds and notes				
aa) Public-sector issuers			866 251	315 380
ab) Other issuers			13 562 175	11 830 551
			14 428 426	12 145 931
of which: Securities eligible as collateral with Deutsche Bundesbank	4 031 209	(5 556 287)		
b) Own bonds issued			45 094	50 861
Nominal amount	44 645	(49 481)		
			14 473 520	**12 196 792**
Equities and other non-fixed income securities			**2 300**	**1 186**
Equity investments			**12 886**	**436**
of which: Interests in banks	263	(263)		
Interests in affiliated companies			**1 020 663**	**898 128**
of which: Interests in banks	–	(264 839)		
of which: Interests in financial services providers	8 000	(–)		
Trust assets			**1 804**	**3 175**
of which: Trustee loans	1 160	(2 431)		
Intangible assets			**15 889**	**5 700**
Tangible fixed assets			**32 157**	**44 842**
Other assets			**1 069 523**	**537 771**
Prepaid expenses			**110 664**	**116 069**
Total assets			**54 275 501**	**46 072 565**

* Previous year's figures shown in brackets

as at 31 March 2007

Shareholders' Equity and Liabilities	in € thousand*		**31 Mar 2007 in € thousand**	31 Mar 2006 in € thousand
Liabilities to banks				
a) Payable on demand			2 509 983	1 566 386
b) With agreed term or period of notice			13 723 863	15 064 676
			16 233 846	**16 631 062**
Liabilities to customers				
Other liabilities				
a) Payable on demand			567 208	290 224
b) With agreed term or period of notice			4 126 627	2 529 154
			4 693 835	**2 819 378**
Securitised liabilities				
Bonds issued			**27 822 135**	**21 516 009**
Trust liabilities			**1 804**	**3 175**
of which: Trustee loans	1 160	(2 431)		
Other liabilities			**495 063**	**391 012**
Deferred income			**170 448**	**99 434**
Provisions				
a) Provisions for pensions and similar obligations			141 686	131 698
b) Tax provisions			127 738	97 684
c) Other provisions			178 033	156 248
			447 457	**385 630**
Subordinated liabilities			**1 915 140**	**1 723 880**
Profit-participation certificates			**608 565**	**650 597**
of which: Due within two years	81 807	(173 839)		
Fund for general banking risks			**189 620**	**80 000**
Shareholders' equity				
a) Subscribed capital			225 280	225 280
Conditional capital:	22 528	(22 528)		
b) Silent partnership contributions			400 000	400 000
c) Capital reserve			567 416	567 416
d) Retained earnings				
da) Legal reserves			*2 399*	*2 399*
db) Other retained earnings			*502 493*	*502 493*
			504 892	504 892
e) Net profit (Bilanzgewinn)			0	74 800
			1 697 588	**1 772 388**
Total shareholders' equity and liabilities			**54 275 501**	**46 072 565**
Contingent liabilities				
a) Contingent liabilities from discounted forwarded bills			351	567
b) Liabilities from guarantees and indemnity agreements			8 958 393	4 896 401
			8 958 744	**4 896 968**
Other commitments				
Irrevocable loan commitments			**12 685 729**	**11 582 804**

* Previous year's figures shown in brackets

Restated Profit and Loss Account of IKB Deutsche Industriebank AG

Expenses	in € thousand*		2006/2007 in € thousand	2005/2006 in € thousand
Interest expenses			**4 476 398**	**3 702 195**
Commission expenses			**29 917**	**7 399**
Net expenditure on financial operations			**10 138**	**–**
General administrative expenses				
a) Personnel expenses				
aa) Wages and salaries			115 063	103 067
ab) Compulsory social security contributions and expenses for pensions and other employee benefits			30 831	27 105
of which: Pension expenses	*17 079*	*(14 766)*		
			145 894	130 172
b) Other administrative expenses			105 688	88 578
			251 582	**218 750**
Amortisation/depreciation and write-downs of intangible and tangible fixed assets			**7 309**	**7 759**
Other operating expenses			**31 805**	**43 943**
Amortisation/depreciation and write-downs of receivables and specific securities, as well as additions to loan loss provisions			**304 002**	**484 179**
Transfers to the fund for general banking risks (section 340g of the HGB)			**109 620**	**–**
Taxes on income			**22 965**	**17 908**
Other taxes not reported under Other operating expenses			**1 018**	**573**
Annual net profit			**0**	**149 200**
Total expenses			**5 244 754**	**4 631 906**
Annual net profit			**0**	**149 200**
Transfer to retained earnings				
To other retained earnings			**0**	**–74 400**
Net profit			**0**	**74 800**

* Previous year's figures shown in brackets

for the period from 1 April 2006 to 31 March 2007

Income	2006/2007 in € thousand	2005/2006 in € thousand
Interest income from		
a) Lending and money market transactions	4 299 047	3 708 045
b) Fixed-income securities and debt register claims	459 637	388 366
	4 758 684	**4 096 411**
Current income from		
a) Equities and other non-fixed income securities	1 448	215
b) Investments	6 570	175
c) Interests in affiliated companies	20 999	90 338
	29 017	**90 728**
Income from profit-pooling, profit transfer, and partial profit transfer agreements	**69 916**	**29 535**
Commission income	**194 040**	**132 066**
Net result from financial operations	**–**	**509**
Other operating income	**193 097**	**282 657**
Total income	**5 244 754**	**4 631 906**

Restated Notes

Overview of the changes resulting from the restatement of the single-entity financial statements as at 31 March 2007

In view of the developments on the loan securitisation markets and the existential threatening crisis facing the Bank, we regard a revaluation of the individual circumstances as necessary, taking into consideration the current findings. We have presented a detailed summary of the restatements we carried out to the Bank's Annual Report as at 31 March 2007 at the beginning of the Notes section. A restatement of the previous year's figures in accordance with the German Institute of Public Accountants (IDW) opinion on accounting practices "Restatement of annual and consolidated financial statements" (IDW RS HFA 6) has not been carried out.

1. Interest income from fixed-income securities and debt register claims

The change made to this line item relates to structured securities with a term of up to 30 years where the nominal value is increased annually by the amount of the accrued interest. The securities are characterised by two different contractually agreed interest rate periods. Interest is based on fixed coupons in the first years and in some cases considerably exceeds the applicable market interest rate for normal 30-year bonds. Afterwards, interest is based on variable coupons on an inverted basis. During the floating rate period the securities are subject to a minimum and a maximum interest rate (floor, cap). Upon the beginning of the floating rate period, the issuer may switch the coupon into Euribor for the total remaining term (coupon flip). An early termination of the contract is also possible.

The structured securities have to be accounted for as single assets since the requirements for separate accounting are not fulfilled. Subsequently, the Bank had recognised the related interest income in accordance with the coupon agreed under civil law. In order to enhance the presentation of the economic substance of the securities, we decided to base the recognition of income earned from the securities primarily on economic criteria. On the basis of a comparison of the agreed coupons with interest coupons of zero coupon bonds without conversion rights, the amount to be deferred for the premiums inherently included in the fixed interest coupons with respect to the conversion rights granted was calculated at € 77.9 million as at 31 March 2007, of which € 26.6 million relates to the financial year 2005/06. Interest income was reduced by the same amounts.

In addition, due to the changes made as described in No. 7, € 49.6 million in premiums on credit default swaps for the financial year 2006/07 was reclassified from interest income to fee and commission income. This did not result in any measurement adjustments and the related effect on the income statement.

See also the comments under "Notes to the balance sheet – Deferred income and prepaid expenses".

2. Amortisation and write-downs of receivables and specific securities, as well as additions to loan loss provisions

In accordance with the Auditing Practice Statement (*Prüfungshinweis*) of the IDW Auditing Standard "The Audit of Counterparty Risks and the Credit Business of Credit Institutions" (*IDW Prüfungsstandard "Prüfung der Adressenausfallrisiken und des Kreditgeschäfts von Kreditinstituten"*) (IDW PS 522, Tz. 30), the expected realisation period has to be taken into account by discounting the collateral provided using a market interest rate for an adequate maturity. The resulting discounting effect was recognised in the provision for possible loan losses in these HGB financial statements by analogy with IFRS. The amount recognised was € 34.4 million.

See also the changed amounts in the balance sheet item "Loans and advances to customers".

3. Other administrative expenses

Pursuant to Article 11 of the Memorandum and Articles of Association of IKB, the variable remuneration for members of the Supervisory Board is subject to payment of a dividend. On the basis of the envisaged approval of the changed financial statements (restatement), no dividend is intended to be paid. Therefore, the variable remuneration for the Supervisory Board in the amount of € 0.6 million will be dispensed with.

See also the changed amounts in the balance sheet item "Other provisions".

4. Transfer to retained earnings

The changes made within the scope of the restatement require that the originally planned transfer to retained earnings has to be reduced almost completely (by € 70.4 million) so that the remaining amount to be transferred totals € 1.1 million.

See also the changed amounts in the balance sheet item "Shareholders' equity" and the section "Changes in capitalisation".

5. Transfer to the fund for general banking risks (section 340g of the HGB)

An additional amount of € 33.5 million was transferred to the fund for general banking risks after all measures with effect on earnings had been accounted for (see 1.- 4. above).

6. Net retained profit

The remaining net retained profit, after the above-mentioned adjustments, amounts to € 40 thousand.

See also the changed amounts in the balance sheet item "Shareholders' equity" and the section "Changes in capitalisation".

7. Liabilities from guarantees and indemnity agreements

The banking book of IKB AG as at 31 March 2007 includes collateralised debt obligations (CDO) as well as credit-linked notes (CLN) which are exposed to issuer risks as well as default risks due to embedded derivatives.

According to the regulations regarding accounting for structured products (IDW RH BFA 1.003), the credit derivatives included in the aforementioned financial instruments (in particular credit default swaps) should be accounted for separately and reported as contingent liabilities under the balance sheet. Similar reporting of contingent liabilities from credit default swaps to be accounted for separately was not included in the Annual Report 2006/07 in order to avoid double reporting of the risks. Accordingly, the amount of contingent liabilities (liabilities from guarantees and sureties) posted in the restated Annual Report increased by € 4.9 billion. The credit default swaps included in that figure were reported with a positive market value of € 41 million as well as with a negative market value of € 65 million.

The Bank's risk position did not increase as a result of the additional reporting of credit derivatives under the balance sheet since the underlying securities were already fully accounted for in the balance sheet.

Accordingly, the Bank reallocated the premiums resulting from the imbedded credit default swaps from the item "net interest income" to "net commission income" (see also the effects described in point 1).

Additionally, we refer to the restated figures in the item "contingent liabilities."

Notes to the Single-Entity Financial Statements

The single-entity financial statements of IKB Deutsche Industriebank AG for the financial year 2006/07 are prepared in accordance with the provisions of the German Commercial Code (Handelsgesetzbuch – "HGB"), in conjunction with the German Accounting Directive for Banks (Verordnung über die Rechnungslegung der Kreditinstitute – "RechKredV") as well as with the relevant provisions of the German Public Limited Companies Act (Aktiengesetz – "AktG"). The financial statements also comply with the provisions of the EU Bank Accounts Directive (86/635/EC).

Accounting policies

Receivables

Loans and advances to banks and customers are disclosed at their nominal value, less specific and general loan loss provisions (risk provisioning). Differences between repayment amounts and nominal values are included in deferred income, and reversed on schedule.

We have formed general loan loss provisions to cover expected loan losses which have been incurred but not identified as such at the balance sheet date. General loan loss provisions are based on proprietary historical loan loss data and weightings.

Securities

Securities are disclosed under the heading "Debt securities and other fixed-income securities", as well as "Equities and other non-fixed income securities"; to the extent that they form part of current assets, they are valued at the lower of cost or market, i.e. at their costs of purchase or the lower market price. Pursuant to section 280 of the HGB, we were obliged to write up the value of securities that had been written down in previous years to their current market value to a maximum amount of their historical costs of purchase.

Individual securities holdings, together with allocated interest rate hedges (interest rate swaps) form a valuation unit (micro hedge). In these cases, as a result of the interest rate hedges, it is permitted to waive securities write-downs if these are based on changes in market interest rates; if the issuer's creditworthiness is sustainably impaired, write-downs to net present value (*Teilwert*) are made.

Long-term investment securities exclusively comprise issues from international industrial companies (corporate bonds and credit-linked notes), which we purchased with the intention of holding them to final maturity.

Structured products are generally accounted for as one single asset. In accordance with the provisions of "IDW Accounting Practice Statement BFA 1,003 on 'The Accounting of Structured Products'" (*IDW Rechnungslegungshinweis "Zur Bilanzierung strukturierter Produkte"*), credit derivatives carried as fixed assets and embedded in structured financial instruments (especially credit default swaps) have to be accounted for and measured separately as individual assets or liabilities when the deployed capital is not only exposed to the credit risk related to the issuer based on the embedded derivatives, but also to additional risks. In accordance with the provisions of the HGB, embedded credit derivatives are shown as contingent liabilities off the balance sheet.

Participations and interests in affiliated companies/Tangible fixed assets

Interests in affiliated companies and enterprises with a participatory interest, as well as in associated enterprises, are carried at amortised cost.

Tangible fixed assets are valued at their cost of purchase or historical cost, less scheduled depreciation. In the case of sustained impairment, the assets are subject to unscheduled write-downs. Low-value assets are written off in full during their year of purchase.

Liabilities

Liabilities are carried at their repayment amount. Any difference between the repayment amount and the amount received is carried as prepaid expenses, and reversed according to schedule.

Provisions

Provisions for pensions and similar obligations are carried as a liability in accordance with actuarial principles, based on Prof. Dr. Heubeck’s mortality tables and a 6% rate of interest, and using the cost (German “Teilwert”) method for pension expectancies and the net present value of current pensions.

We form provisions for taxes and uncertain liabilities in the amount in which these are likely to be incurred. We have discounted provisions for anniversary bonus commitments – to the extent needed – in accordance with the tax regulations at 5.5%.

At the end of March 2007, assets assigned as cover for pension obligations were spun off through an external Contractual Trust Agreement (CTA). There are no net effects under German commercial and tax law; the corresponding assets and obligations continue to be carried on a gross basis.

Derivatives transactions

Derivative transactions (swaps, futures/forwards, options) are pending items and are not subject to a compulsory disclosure requirement on the balance sheet. They are allocated to the banking or trading book when they are concluded, in line with their purpose. To the extent that derivative financial transactions are to be allocated to the trading book, these are valued in line with the principle of imparity and realisation, based on their current market values. In order to hedge and manage interest rate and market risks for the banking book, together with financial transactions recognised on the balance sheet, derivative financial transactions implemented are subject to uniform control and evaluation of the risk of interest rate changes. Changes to the market value of these transactions are thus not subject to monitoring on an individual basis.

Currency translation

On- and off-balance sheet transactions denominated in foreign currency are translated in accordance with the principles of section 340h of the HGB. Fixed assets denominated in foreign currency that are not specifically hedged have been translated at their historic exchange rates at the time of their acquisition.

All other assets, liabilities and other outstanding spot transactions denominated in foreign currency are valued at the reference rate of the European Central Bank (ECB) on the balance sheet date. If foreign exchange forwards are concluded in order to hedge interest-bearing items on the balance sheet, premiums and discounts on the spot rate are offset against the net interest income on a pro-rata basis. Hedged income or expenses are translated at the contracted forward rate.

In the income statement, only expenses from currency translation according to section 340 h (2) of the HGB are taken into account.

Currency translation adjustments related to balance sheet items are directly recognised in other assets or other liabilities.

Notes to the Balance Sheet

Maturities of select balance sheet items by residual terms

in € million		up to three months	more than three months until one year	more than one year until five years	more than five years
Loans and advances to banks*)					
	31.3.2007	8 057	3 454	111	361
	31.3.2006	6 010	2 255	111	140
Loans and advances to customers					
	31.3.2007	2 931	3 145	10 871	7 987
	31.3.2006	3 158	2 675	9 580	6 818
Liabilities to banks*)					
	31.3.2007	2 820	3 203	4 317	3 384
	31.3.2006	6 301	2 344	3 426	2 994
Liabilities to customers*)					
	31.3.2007	819	101	1 008	2 199
	31.3.2006	219	182	871	1 257

*) Excluding loans and advances or liabilities payable on demand

Of the debt securities and other fixed-income securities, € 856 million (2005/06: € 961 million) will mature in the next financial year. Of the debt securities included in securitised liabilities, € 9.2 billion (€ 6.4 billion) will mature in the next financial year.

Fixed assets

in € million	Purchase or/ production cost	Additions	Disposals	Depreciation cumulative	Depreciation financial year	Net book value 31 Mar 2007	Net book value 31 Mar 2007
Tangible fixed assets	114.1	4.1	27.4	58.6	5.2	32.2	44.8
Intangible assets	6.5	12.5	–	3.1	2.4	15.9	5.7
Equity investments	0.4	12.5	0.0	–	–	12.9	0.4
Interests in affiliated companies	957.3	450.0	327.5	59.1	–	1 020.7	898.1
Equities and fixed income securities	7 639.1	1 282.3	672.8	19.3	19.3	8 229.3	7 639.1

Fixed assets include debt securities and other fixed-income securities, plus equities of € 8.2 billion (2005/06: € 7.6 billion). These are issues from international industrial companies (corporate bonds and credit-linked notes) which we have acquired as part of our credit business. As we intend to hold these until maturity, we treat these holdings in line with loans. At the reporting date, there were € 232 million in unrealised losses on these securities holdings.

On 31 March 2007, the book value of the land and buildings used by the Bank amounted to € 17.5 million (€ 17.8 million).

Operating and office equipment is included under the fixed assets, and totals € 12.9 million (€ 14.8 million).

Securities negotiable at a stock exchange

The negotiable securities contained in the following balance sheet items listed below are differentiated as follows:

in € million	Total	Listed	Unlisted
Debt securities and other fixed-income securities	14 129.2	12 850.2	1 279.0
Equities and other non-fixed income securities	2.3	2.0	0.3
Interests in affiliated companies	58.6	0.0	58.6

Loans and advances, and liabilities to associated and affiliated companies

in € million	Affiliated companies	Equity investments
Loans and advances to banks	8 069.4	2.9
Loans and advances to customers	1 397.8	243.2
Liabilities to banks	2 683.2	5 885.6
Liabilities to customers	373.4	6.4
Subordinated liabilities	475.1	0.0

Trustee business

in € million	31 Mar 2007	31 Mar 2006
Loans and advances to customers	1.2	2.4
Equity investments	0.6	0.8
Trust assets	**1.8**	**3.2**
Liabilities to customers	1.8	3.2
Trust liabilities	**1.8**	**3.2**

Subordinated assets

Subordinated assets are included in the following balance sheet asset items:

in € million	31 Mar 2007
Loans and advances to banks	100.0
Loans and advances to customers	380.4
Debt securities and other fixed-income securities	119.1

Foreign currency assets and liabilities

The recognised foreign currency balances, translated into EUR, are shown in the following overview. The differences between assets and liabilities are mostly covered by currency hedging transactions.

in € million	31 Mar 2007	31 Mar 2006
Assets	10 456.3	6 115.8
Liabilities	6 327.8	4 811.3

Other assets and other liabilities

The largest single item in other assets constitutes proportionate interest from interest rate swaps and cross-currency-swaps, totalling € 381 million. Tax refund claims were recognised in the amount of € 53 million. The remaining amount disclosed under this item mostly relates to receivables under profit transfer agreements, and trade accounts receivable.

Other liabilities include € 35 million in amounts distributed on profit-participation certificates for the financial year 2006/07, as well as € 45 million in pro rata interest for subordinated liabilities and silent partnership contributions. At € 314 million, pro rata interest on interest rate swaps accounted for the largest single item of Other liabilities. The remaining amount under this item mostly relates to trade accounts payable.

Deferred income and prepaid expenses

Prepaid expenses include € 82 million in differences pursuant to section 250 (3) of the HGB and section 340e (2) sentence 3 of the HGB (discounts from liabilities carried at their nominal value).

Deferred income includes € 35 million in differences pursuant to section 250 (2) of the HGB and section 340 e (2) sentence 2 of the HGB (discounts from loans and advances carried at their nominal value). The deferral of option premiums of certain securities of the fixed-income fund (see section “Overview of the changes resulting from the restatement of the single-entity financial statements as at 31 March 2007 – 1. Interest income from fixed-income securities and debt register claims”) led to a recognition of € 78 million as deferred income.

Subordinated liabilities

Subordinated liabilities are eligible as equity within the meaning of the German Banking Act (Kreditwesengesetz – "KWG") and thus qualify as liable capital. There is no early repayment commitment. In the event of bankruptcy proceedings or liquidation, they may not be redeemed until all unsubordinated creditors have been satisfied.

Subordinated liabilities amounted to € 1.9 billion; related interest expenses totalled € 85.3 million (2005/06: € 79.6 million) in the financial year under review.

Individual items which exceed 10 % of the total amount:

Year of issue	Book value in € million	Issue-currency	Coupon in %	Maturity
2004/2005	400.0	EUR	4.06	29 Jul 2033
2003/2004	310.0	EUR	4.50	9 Jul 2013

Profit-participation certificates

Profit-participation certificates totalling € 608.6 million meet the requirements set out in section 10 (5) of the KWG in the amount of € 523.6 million and thus qualify for inclusion in the Bank's liable capital. The total amount of these certificates may be used to cover losses. Interest payments are made solely on the basis of any net retained profits. The rights of holders of profit-participation certificates to redemption of capital are subordinated to the rights of other creditors.

Profit-participation certificates can be broken down as follows:

Year of issue	Book value in € million	Issue-currency	Coupon in %	Maturity
1995/1996	81.8	DM	8.40	31 Mar 2007
1997/1998	102.3	DM	7.05	31 Mar 2009
1999/2000	20.0	EUR	7.23	31 Mar 2010
2001/2002	100.0	EUR	6.50	31 Mar 2012
2001/2002	74.5	EUR	6.55	31 Mar 2012
2004/2005	30.0	EUR	4.50	31 Mar 2015
2005/2006	150.0	EUR	3.86	31 Mar 2015
2006/2007	50.0	EUR	4.70	1 Aug 2017
	608.6			

For the financial year 2006/07, interest on profit-participation certificates in the amount of € 37.3 million (2005/06: € 41.7 million) was recognised as interest expenses.

For the financial year 2006/07, interest on profit-participation certificates in the amount of € 37.3 million (2005/06: € 41.7 million) was recognised as interest expenses.

The Board of Managing Directors was authorised at the Annual General Meeting on 30 August 2002 to issue profit-participation certificates until 30 August 2007, with a total nominal value of up to € 300 million. Having been used for issues in an aggregate amount of € 230 million, the remaining authorisation amounts to € 70 million.

The holders of such profit-participation certificates may be granted conversion or option rights for up to 8,800,000 bearer shares of IKB Deutsche Industriebank AG with an interest in the Company's share capital of up to € 22,528,000.00. No use has been made of this authorisation to date.

Changes in capitalisation

1. Treasury shares

The General Meetings held on 9 September 2005 and 31 August 2006 authorised the Bank to acquire its own shares for the purpose of securities trading.

During the financial year 2006/07, a total of 1,017,230 treasury shares were purchased at an average price of € 29.88 per share, and the same quantity was sold at an average price of € 29.78 per share. The net loss from these transactions totals € 0.1 million and has been recognised in the net result from financial operations. The largest amount of treasury shares held on any one day totalled 0.21% of the Company's share capital. Our affiliated companies did not sell or purchase IKB shares. No treasury shares were held by the Bank as at the reporting date.

In order to allow employees to purchase employee shares, 13,683 shares were purchased at an average price of € 27.60 in the year under review. 9,910 shares were resold to employees of IKB Deutsche Industriebank AG at a preferred price of € 13.20. A further 4,300 shares were acquired by employees of the Group, at the same conditions. The resulting charges amounted to € 0.2 million, and are included in personnel expenses.

2. Shareholders' equity

Subscribed share capital amounted to € 225,280,000.00 on the balance sheet date and comprises 88,000,000 notional no-par value bearer shares ("bearer unit shares").

There is conditional capital totalling € 22.5 million for the purpose of granting conversion or option rights to the bearers of convertible bonds or bonds with warrants to be issued until 8 September 2009 with an aggregate nominal value of € 300 million. In addition, there is conditional capital totalling € 22.5 million for the purpose of granting conversion or option rights to the bearers of profit-participation certificates with conversion or option rights to be issued until 30 August 2007. Furthermore, an authorised capital totalling € 76.8 million was created. This authorisation expires on 30 August 2007.

None of these authorisations has been exercised to date.

3. Hybrid capital

Hybrid tier 1 capital of € 400 million as at 31 March 2007 was unchanged compared to the previous year. This capital complies with the requirements of section 10 (4) of the KWG and is therefore attributed to our tier 1 capital for regulatory purposes.

Hybrid capital includes issues in the form of capital contributions made by silent partners. In the case of silent participations – basically issued as perpetuals – only the issuer is allowed to terminate the contract after 10 years at the earliest.

Moreover, in the case of insolvency hybrid capital instruments are subordinated to all subordinated liabilities and profit-participation certificate issues.

The interest expenses for hybrid capital issues amounted to € 28.4 million (2005/06: € 29.4 million).

4. Changes in capitalisation

in € million	2007	2006
Balance on 1 April of the previous period	1 772.4	1 693.6
Disbursement of net profit from previous year	–74.8	–70.4
Appropriation of net income to retained earnings	0.0	74.4
Net profit as at 31 March	0.0	74.8
Balance at 31 March	**1 697.6**	**1 772.4**

The regulatory capital in accordance with the German Banking Act (KWG) totalled € 3.3 billion.

Contingent liabilities and other commitments

Contingent liabilities	31 Mar 2007 in € million	31 Mar 2006 in € million
Guarantees, warranties, other	8 789.1	4 677.0
Assumptions of liability	169.6	220.0
Total	**8 958.7**	**4 897.0**

Other commitments	31 Mar 2007 in € million	31 Mar 2006 in € million
Commitments for up to one year	10 139.5	9 667.9
Commitments for more than one year	2 546.2	1 914.9
Total	**12 685.7**	**11 582.8**

At the balance sheet date, Contingent liabilities also comprised credit default swaps (where IKB has assumed the position of protection seller) amounting to € 1.3 billion (2005/06: € 1.6 billion), within the Guarantees, warranties, other item. As seller of protection we have assumed the risk of counterparty default for certain credit portfolios, given the occurrence of pre-defined credit events. More than two-thirds of the individual portfolios are rated in the best rating classes Aaa to A by Moody’s, the independent external rating agency.

Moreover, derivative components of structured products amounting to € 4.9 million which were previously reported under the item “Debt securities and other fixed-income securities” will be additionally included in the item “Liabilities from guarantees and indemnity agreements” without resulting in a change of the overall risk position of the Bank.

Other commitments comprise liquidity facilities in the form of loan commitments to special purpose entities (primarily to the conduit entities of Rhineland Funding) for a total equivalent of € 8.1 billion. These commitments can be drawn upon by these entities in the case of short-term liquidity bottlenecks, or upon events of default (as defined in agreements entered into).

Notes to the Income Statement

Geographical analysis of sources of income (information as defined in section 34 (2) of the RechKredV)

The aggregate of (i) interest income; (ii) current income on equities and other non-fixed income securities, and on equity investments and interests in affiliated companies; (iii) commission income; and (iv) other operating income is broken down by geographic region below:

in € million	2006/07	2005/06
Federal Republic of Germany	3 018.8	2 915.0
Europe excl. Germany	2 226.0	1 717.0
Total	**5 244.8**	**4 632.0**

We allocate income to geographic regions according to the respective location of our offices.

Administration and intermediation services rendered to third parties

We provide management services for lending and custodial accounts, in particular for guarantees. The income from these services is included under commission income.

Miscellaneous other operating income

Other operating income mainly comprises profits from the disposal of investment securities, and of investments (€ 180.2 million; 2005/06: € 270.6 million), plus € 6.0 million (€ 5.9 million) in Group overheads charged, and € 2.4 million (€ 3.7 million) in rental income.

Other operating expenses

Other operating expenses mainly comprise € 9.5 million (2005/06: € 22.8 million) in value adjustments on options transactions, € 8.9 million (€ 11.6 million) for buildings used by third parties, € 2.0 million (€ 1.7 million) in social security costs, as well as € 1.1 million (€ 1.3 million) in Group overheads paid.

Other Disclosures

Shareholding in accordance to § 285 sentence 1 no. 11 HGB	Letter of comfort	Equity-interest	Equity in € thousand	Results in € thousand
1. Foreign banks				
IKB International S.A., Luxemburg	x	100	530 652 [4]	94 200 [3]
2. German companies				
AIVG Allgemeine Verwaltungsgesellschaft mbH, Düsseldorf	x	100	5 811	355
IKB Autoleasing GmbH, Hamburg	x	100	4 000	– [1] [3]
IKB Beteiligungen GmbH, Düsseldorf	x	100	401 515	0
IKB Credit Asset Management GmbH, Düsseldorf	x	100	8 000	– [1]
IKB Data GmbH, Düsseldorf	x	100	20 000	– [1]
IKB Grundstücks GmbH, Düsseldorf	x	100	89	19
IKB Grundstücks GmbH & Co. Objekt Degerloch KG, Düsseldorf	x	100	6 663	71
IKB Grundstücks GmbH & Co. Objekt Hamburg KG, Düsseldorf	x	100	2 715	–282
IKB Grundstücks GmbH & Co. Objekt Holzhausen KG, Düsseldorf	x	100	9 734	325
IKB Grundstücks GmbH & Co Objekt Uerdinger Straße KG, Düsseldorf	x	100	8 620	–158
IKB Immobilien Management GmbH, Düsseldorf	x	75	948	572
IKB Leasing Berlin GmbH, Erkner	x	100	8 000	– [1] [3]
IKB Leasing GmbH, Hamburg	x	100	30 000	– [1] [3]
IKB Private Equity GmbH, Düsseldorf	x	100	97 500	– [1] [3]
IKB Projektentwicklung GmbH & Co. KG, Düsseldorf	x	100	20 040	1 422
IKB Projektentwicklungsverwaltungsges. mbH, Düsseldorf	x	100	22	1
IMAS Grundstücks-Vermietungsges. mbH, Düsseldorf	x	100	268	62
ISTOS Beteiligungsverwaltungs- und Grundstücks-vermietungsges. mbH, Düsseldorf	x	100	34	2
ISTOS Erste Beteiligungsverwaltungs- und Grundstücks-vermietungsges. mbH & Co. KG, Düsseldorf	x	100	2 485	–12
Movesta Lease and Finance GmbH, Düsseldorf		50	10 335	4 021 [3]
3. Foreign companies				
IKB Capital Corporation, New York		100	48 508	7 075
IKB Finance B. V., Amsterdam	x	100	11 060	1 482
IKB Financière France S.A., Paris	x	100	72 083	1 923
IKB Funding LLC I, Wilmington	x [2]	100	75 057 [4]	–37
IKB Funding LLC II, Wilmington	x [2]	100	400 064 [4]	12
IKB Lux Beteiligungen S. à.r.l., Luxemburg	x	100	428 878	0

[1] There is a profit and loss transfer agreement
[2] Subordinated letter of comfort
[3] Indirect shareholding
[4] Incl. silent partnership contributions/preferred shares

The full list of shareholdings will be submitted to the German Electronic Federal Gazette (elektronischer Bundesanzeiger) and made available on the website of the company register. It may be obtained from IKB free of charge.

Disclosure of auditors' fees pursuant to section 285 sentence 1 no. 17 of the HGB

The following auditors' fees were paid to the German auditor during the financial year 2006/07:

in € million	2006/07
Auditing fees	1.7
Other audit or valuation services	0.5
Tax advisory services	0.4
Other services	0.2
Total	**2.8**

Other financial commitments

Funding commitments from shares, interests in German limited liability companies (GmbHs), and interests in associated companies which have not been fully paid up, amounted to € 1,000 as at the reporting date.

The Bank has a pro rata additional funding obligation for the investment in Liquiditäts-Konsortialbank GmbH, Frankfurt am Main, Germany. IKB is also contingently liable pro rata for the fulfilment of the additional funding obligations of other shareholders belonging to the Association of German Banks (*Bundesverband deutscher Banken e.V.*). In addition, pursuant to Section 5 (10) of the Statutes for the Joint Fund for Securing Customer Deposits (*Statut für den Einlagensicherungsfonds*), the Bank has committed itself to indemnify the Association of German Banks from any losses arising due to measures in favour of banks in which it owns a majority interest.

Letters of comfort

In accordance with section 285 no. 11 of the HGB, IKB ensures, excluding political risk, that subsidiaries carried in the list of investments of IKB Deutsche Industriebank AG and marked as being covered by the letter of comfort, will be able to meet their contractual liabilities.

Collateral for own liabilities

IKB has assigned or transferred assets and accepted collateral for the following liabilities:

in € million	31 Mar 2007
Liabilities to banks	6 336
Liabilities to customers	18
Total	**6 354**

We provide collateral above all for loans granted by KfW Bankengruppe and other development banks. These institutions have made the issue of such loans contingent upon the provision of collateral.

Assets pledged as collateral for own liabilities

Fixed-income securities totalling € 6.0 billion (prior year: € 5.3 billion) have been pledged with Deutsche Bundesbank as collateral for the European Central Bank's repurchase agreement process (collateral pool). As at the balance sheet date, credit facilities amounting to € 0.8 billion (prior year: € 3.3 billion) had been drawn upon.

We have provided various banks with cash collateral in connection with credit derivative transactions, in the amount of € 290.0 million (€ 540.0 million).

We have provided cash collateral for interest rate derivatives as part of the Company's collateral management, in the amount of € 217.6 million (€ 210.7 million).

In order to fulfil payment obligations for securities transactions, securities with a market value of € 3.5 million (€ 3.5 million) have been deposited as collateral at Clearstream Banking AG, Frankfurt, and a security with a nominal value of € 7.0 million (€ 7.0 million) has been deposited as collateral at Clearstream Banking S.A., Luxembourg. Within the scope of trading at Eurex Germany, securities with a nominal value of € 20.0 million (€ 5.0 million) have been pledged with BHF-Bank AG, Frankfurt/Main and Berlin, as well as with Citigroup, London, to cover margin requirements.

In addition, securities with a nominal value of USD 67 million were pledged with WestLB AG, London branch, as collateral within the scope of an issue. USD 390 million in securities have been pledged to KfW Banking Group, Frankfurt/Main, as additional cover supporting joint business concepts.

Forward transactions/market value of derivatives/interest rate risks

IKB engages in forward transactions (swaps, forward rate agreements, and futures); these are predominantly used to manage and hedge interest rate risks, predominantly in the loan refinancing portfolio and the investment portfolio. These instruments are used for trading purposes only to a limited extent. The Bank's interest rate risk exposure is restricted by a limit system adopted by the Board of Managing Directors, and is constantly monitored by our Risk Management unit. In addition, counterparty limits apply to the volume of forward and derivative transactions.

The **loan refinancing portfolio** is used to manage interest rate risk exposure on loans granted, and on the corresponding refinancing. For this purpose, long-term loans are largely refinanced on a matched-maturity basis. Derivatives are used to neutralise or reduce maturity mismatches, and interest rate or currency risks.

The **investment portfolio** largely comprises liquid securities, most of which are eligible as collateral for transactions with the ECB (such as repo tenders). The portfolio includes floating-rate notes, which offer price stability due to regular coupon resets. The variable interest of floating-rate notes is optimised using derivatives.

Market value of derivatives

in € million	Nominal value	Positive market value	Negative market value
Interest-based transactions	27 771	211	–606
Currency-based transactions	8 034	95	–137
Equity/index-based transactions	0	0	0
Total	**35 805**	**306**	**–743**

Negative market values are incurred on interest rate derivatives in the loan refinancing portfolio where the Bank is a net interest payer, and the market level of interest rates has fallen between the trade date and the balance sheet date (since the Bank would otherwise have been able to enter into a similar transaction on the balance sheet date, at more favourable terms). Negative market values in the Bank's investment portfolio are incurred in a similar way, however, these derivatives are used to hedge interest income rather than expenditure.

As explained above, these derivatives are generally used to manage interest rate risks. Expenditure incurred on the derivatives are balanced by income from loans and fixed-income securities, in a similar amount. Negative market values of derivatives are offset by positive valuation effects on fixed-rate loans and securities. Given the Bank's intention to hold the derivatives until maturity, such negative market values are not recognised in income unless positions have to be closed out in the event of limit transgressions.

Positive or negative market values are calculated on the basis of stock exchange prices. Where no stock exchange prices are available, fair values are determined using the discounted cash flow method, based on a comparison with similar market transactions, or using other valuation models. The discounted cash flow method is based on the estimated future cash flows and applicable discount rates. The valuation models include parameters such as yield curve data, time values and volatility factors. The fair values reported include interest accrued, in accordance with market practice.

Remuneration and loans to executive bodies

A detailed description of the remuneration for the members of the Board of Managing Directors and of the Supervisory Board (together with the corresponding remuneration principles) is included in the Remuneration Report, which is included in the Management Report.

The remuneration for the members of the Board of Managing Directors

For the financial year 2006/07, the remuneration of the entire Board of Managing Directors amounted to € 7,824 thousand, of which € 6,837 thousand related to annual remuneration, and € 987 thousand to additions to pension provisions.

Former and retired members of the Board of Managing Directors

The total remuneration for former and retired Board members and their surviving dependents amounted to € 5,345 thousand (prior year: € 2,871 thousand) in form of cash payments or additions to provisions. A total amount of € 29,680 thousand was provided for pension obligations to former members of the Board of Managing Directors and their surviving dependents.

The remuneration for the members of the Supervisory Board

For the financial year 2006/07, the remuneration of the entire Supervisory Board amounted to € 693 thousand, including € 183,000 related to travel expenses and VAT.

Remuneration of the Advisory Board

The members of the Advisory Board received € 403 thousand (prior year: € 390 thousand), including VAT.

Loans extended to members of executive bodies and of the Advisory Board

No loans were extended to members of the Board of Managing Directors. Loans to members of the Supervisory Board, and of the Advisory Board were granted in an aggregate amount of € 1.4 million (2005/06: € 2.4 million).

Average number of employees for the financial year

(based on full-time employees)

	2006/07	2005/06
Male	715	682
Female	441	413
Total	**1 156**	**1 095**

Corporate governance

The Bank has issued the Declaration of Compliance as stipulated in section 161 of the AktG, and made it continuously available to shareholders.

(69) Executive bodies

The following list of members of the Supervisory Board and Board of Managing Directors shows:

a) their membership in other statutory supervisory boards; and

b) similar offices held in comparable governing bodies of German and foreign companies.

Supervisory Board

Chairman

Dr. h.c. Ulrich Hartmann, Düsseldorf
Chairman of the Supervisory Board of
E.ON AG

a) E.ON AG (Chairman)
Deutsche Bank AG
Deutsche Lufthansa AG
Hochtief AG (until 26 July 2007)
Münchener Rückversicherungs-Gesellschaft AG

b) Henkel KGaA

Deputy Chairman

Hans W. Reich, Frankfurt (Main)
Chairman of the Board of Managing Directors of
KfW Bankengruppe (retired)
(until 31 August 2006)

a) Aareal Bank AG (Chairman)
HUK-COBURG Haftpflicht-Unterstützungs-Kasse kraftfahrender Beamter Deutschlands a.G.
HUK-COBURG-Holding AG
ThyssenKrupp Steel AG

b) Citigroup Inc.
DePfa Bank plc.

Detlef Leinberger, Frankfurt (Main)
Member of the Board of Managing Directors of
KfW Banking Group
(from 31 August 2006)

b) Europäische Investitionsbank (EIB)

Dr. Alexander v. Tippelskirch, Düsseldorf
Deputy Chairman of the Supervisory Board
IKB Deutsche Industriebank AG

a) Alba AG (Chairman)
GELITA AG (Chairman until end of July 2007)
P-D INTERGLAS TECHNOLOGIES AG (Deputy Chairman)

b) Hako-Holding GmbH & Co. (until December 2007)
Hako-Werke Beteiligungsgesellschaft mbH (until December 2007)
Krono-Holding AG
Meyra GmbH & Co. KG
nobilia-Werke J. Stickling GmbH & Co.
Schmolz & Bickenbach KG
Schmolz & Bickenbach AG
Hans Martin Wälzholz-Junius Familienstiftung
Eckart Wälzholz-Junius Familienstiftung
Dietrich Wälzholz Familienstiftung

Members

Dieter Ammer, Hamburg
Chairman of the Board of Managing Directors of
Conergy AG

a) Beiersdorf AG (Chairman)
Conergy AG (Chairman until 15 November 2007)
Tchibo GmbH (Chairman until 15 June 2007)
GEA AG
Heraeus Holding GmbH
tesa AG

Jörg Asmussen, Berlin
Ministry Director in the
German Federal Ministry of Finance

a) Euler Hermes Kreditversicherungs-AG
Postbank AG

b) Bundesanstalt für Finanzdienstleistungsaufsicht
(German Financial Services Supervisory Authority)
(Deputy Chairman)

Dr. Jens Baganz, Düsseldorf
State secretary in the Ministry for the
Economy, Small and Medium-Sized Enterprises and Energy
in the State of North-Rhine Westphalia

a) Messe Düsseldorf GmbH

b) NRW.INVEST GmbH (until April 2007 traded under
GfW Gesellschaft für Wirtschaftsförderung
Nordrhein-Westfalen GmbH, Chairman)
NRW.International GmbH (Chairman)
Entwicklungsgesellschaft Zollverein mbH
Forschungszentrum Jülich GmbH
NRW.BANK
NRW Japan K.K.
ZENIT GmbH

Dr. Jürgen Behrend, Lippstadt
Managing Director and General Partner of
Hella KGaA Hueck & Co.

a) Leoni AG (until 2 May 2007)

Wolfgang Bouché, Düsseldorf
Employee representative

Hermann Franzen, Düsseldorf
General Partner of
Porzellanhaus Franzen KG

a) SIGNAL IDUNA Allgemeine Versicherung AG
(Deputy Chairman)
IDUNA Vereinigte Lebensversicherung aG
SIGNAL IDUNA Holding AG

b) BBE Unternehmensberatung GmbH (Chairman)
(until March 2007)

Dr.-Ing. Mathias Kammüller, Ditzingen
Chairman of the Management of
TRUMPF Werkzeugmaschinen GmbH + Co. KG

a) Carl Zeiss AG

b) Bürkert GmbH & Co. (until 31 December 2008)
HUBER VERPACKUNGEN GmbH & Co. KG
Viessmann Werke GmbH & Co. KG
Freudenberg & Co. Kommanditgesellschaft

Wilhelm Lohscheidt, Düsseldorf
(until 31 August 2006)
Employee representative

Jürgen Metzger, Hamburg
Employee representative

Roland Oetker, Düsseldorf
Managing Partner of
ROI Verwaltungsgesellschaft mbH

a) Mulligan BioCapital AG
(Chairman until 28 November 2007)
Deutsche Post AG
Volkswagen AG

b) Dr. August Oetker KG (Deputy Chairman)
RAG-Stiftung

Dr.-Ing. E.h. Eberhard Reuther, Hamburg
Chairman of the Supervisory Board of
Körber Aktiengesellschaft

a) Körber AG (Chairman)

Randolf Rodenstock, Munich
Managing Partner of
Optische Werke G. Rodenstock KG

a) E.ON Energie AG
Rodenstock GmbH

Rita Röbel, Leipzig
Employee representative

Dr. Michael Rogowski, Heidenheim
Chairman of the Supervisory Board of
Voith AG

a) Voith AG (Chairman)
Carl Zeiss AG
HDI Haftpflichtverband der Deutschen Industrie V.a.G.
Klöckner & Co. AG
Talanx AG

b) European Aeronautic Defence and
Space Company EADS N.V. (until December 2007)
Freudenberg & Co.

Jochen Schametat, Düsseldorf
(from 31 August 2006)
Employee representative

Dr. Carola Steingräber, Berlin
Employee representative

Dr. Martin Viessmann, Allendorf (Eder)
Chairman of the Managing Board of
Viessmann Werke GmbH & Co. KG

a) Messe Frankfurt GmbH
Schott AG
Sto AG (until 30 June 2007)

Ulrich Wernecke, Düsseldorf
Employee representative

Andreas Wittmann, Munich
Employee representative

Board of Managing Directors

Dr. Günther Bräunig
(from 29 July 2007)

b) IKB Autoleasing GmbH
IKB Leasing Berlin GmbH
IKB Leasing GmbH
IKB Private Equity GmbH

Frank Braunsfeld
(from 1 March 2007 until 15 October 2007)

b) IKB Credit Asset Management GmbH
IKB Capital Corporation
IKB Immobilien Management GmbH

Dr. Volker Doberanzke
(from 1 June 2006 until 7 August 2007)

b) IKB Data GmbH (Chairman)
IKB Credit Asset Management GmbH
IKB Capital Corporation
IKB Autoleasing GmbH
IKB Leasing GmbH
IKB Leasing Berlin GmbH
IKB Private Equity GmbH
IKB International S. A.

Dr. Dieter Glüder
(from 29 July 2007)

b) IKB Credit Asset Management GmbH (Chairman)
IKB International S.A. (Chairman)
IKB Autoleasing GmbH
IKB Capital Corporation
IKB Leasing Berlin GmbH
IKB Leasing GmbH

Dr. Reinhard Grzesik
(from 15 October 2007)

b) IKB Immobilien Management GmbH (Chairman)
IKB Data GmbH
Movesta Lease and Finance GmbH

Dr. Markus Guthoff
(until 15 October 2007)

a) Carl Zeiss Meditec AG

b) IKB Capital Corporation (Chairman)
IKB Credit Asset Management GmbH (Deputy Chairman)
IKB Private Equity GmbH (Chairman until 31 March 2007)
IKB International S. A. (from 1 April 2007)
Movesta Lease and Finance GmbH
Poppe & Potthoff GmbH

Claus Momburg

b) IKB Autoleasing GmbH (Chairman)
IKB Credit Asset Management GmbH
(Deputy Chairman from 26 October 2007)
IKB International S. A. (Deputy Chairman)
IKB Leasing Berlin GmbH (Chairman)
IKB Leasing GmbH (Chairman)
IKB Private Equity GmbH (Chairman from 1 April 2007)
Movesta Lease and Finance GmbH (Deputy Chairman)
Argantis GmbH

Joachim Neupel
(until 31 December 2006)

a) Aareal Bank AG

b) IKB Immobilien Management GmbH (Chairman)
Movesta Lease and Finance GmbH (Chairman)
IKB Leasing GmbH
IKB Leasing Berlin GmbH
IKB Autoleasing GmbH
IKB Private Equity GmbH

Stefan Ortseifen
(until 29 July 2007)

a) Coface Deutschland AG
Coface Holding AG

b) IKB International S. A. (Chairman)
IKB Credit Asset Management GmbH (Chairman)
DEG – Deutsche Investitions- und
Entwicklungsgesellschaft mbH (Deputy Chairman)
IKB Autoleasing GmbH (Deputy Chairman)
IKB Capital Corporation (Vice Chairman)
IKB Leasing Berlin GmbH (Deputy Chairman)
IKB Leasing GmbH (Deputy Chairman)
IKB Private Equity GmbH (Deputy Chairman)
Kreditanstalt für Wiederaufbau

Frank Schönherr
(until 30 November 2006)

b) IKB Capital Corporation (Chairman)
IKB Financière France S.A.
(Président Directeur Général)

Offices held by employees

As at 31 March 2007, the following employees were represented in statutory supervisory boards of large corporations:

Rolf Brodbeck
Spiele Max AG

Roland Eschmann
Oechsler AG
ODS Optical Disc Service GmbH

Stefan Haneberg
MASA AG

Klaus Reineke
(until 30 September 2007)
GKD Gebr. Kufferath AG

Düsseldorf, 15 February 2008
IKB Deutsche Industriebank AG
Düsseldorf
The Board of Managing Directors

Auditors' Report

We have audited the annual financial statements, comprising the balance sheet, the income statement and the notes to the financial statements, together with the bookkeeping system, and the management report of IKB Deutsche Industriebank Aktiengesellschaft, Düsseldorf, for the business year from April 1, 2006 to March 31, 2007. The maintenance of the books and records and the preparation of the annual financial statements and management report in accordance with German commercial law are the responsibility of the Company's management. Our responsibility is to express an opinion on the annual financial statements, together with the bookkeeping system, and the management report based on our audit.

We conducted our audit of the annual financial statements in accordance with § 317 HGB ["Handelsgesetzbuch": "German Commercial Code"] and German generally accepted standards for the audit of financial statements promulgated by the Institut der Wirtschaftsprüfer [Institute of Public Auditors in Germany] (IDW). Those standards require that we plan and perform the audit such that misstatements materially affecting the presentation of the net assets, financial position and results of operations in the annual financial statements in accordance with German principles of proper accounting and in the management report are detected with reasonable assurance. Knowledge of the business activities and the economic and legal environment of the Company and expectations as to possible misstatements are taken into account in the determination of audit procedures. The effectiveness of the accounting-related internal control system and the evidence supporting the disclosures in the books and records, the annual financial statements and the management report are examined primarily on a test basis within the framework of the audit. The audit includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall presentation of the annual financial statements and management report. We believe that our audit provides a reasonable basis for our opinion.

Our audit has not led to any reservations.

In our opinion, based on the findings of our audit, the annual financial statements comply with the legal requirements and give a true and fair view of the net assets, financial position and results of operations of the Company in accordance with German principles of proper accounting. The management report is consistent with the annual financial statements and as a whole provides a suitable view of the Company's position and suitably presents the opportunities and risks of future development.

We issue our auditor's report on the basis of our proper audit completed on June 4, 2007 and on our supplementary audit which related to changes in the items of the balance sheet and income statement (as already stated in the notes) and to the change of the management report. In the changed notes reference is made to the reasons given by the company for these changes. The supplementary audit did not result in any objections.

Without qualifying this opinion we refer to the comments made by the company in the management report (section 2 of the forecast report) in which it has been pointed out that the continued existence of the company is dependent on its ability to achieve greater access to the capital market again in the next business year also for unsecured longer-term refunding. For this purpose, it is particularly necessary that

- the planned capital increase is approved in the required amount, entered in the Commercial Register and carried out promptly;
- the measures planned to generate liquidity, especially new borrowing necessary on a short term basis and the extension of secured money market refunding, are implemented;
- a significant portion of portfolio investments is disposed of, and
- no legal action is taken against the measures set out above, or against the entire risk shield, this applies in particular to any action taken by the EU.

Düsseldorf, June 4 , 2007/February 15, 2008

KPMG Deutsche Treuhand-Gesellschaft
Aktiengesellschaft
Wirtschaftsprüfungsgesellschaft

Wohlmannstetter	Ufer
Wirtschaftsprüfer	Wirtschaftsprüfer