Bayerische Landesbank Group at a glance

Performance	01.01. – 30.06.03 EUR m	01.01. – 30.06.02 EUR m	Change in %*
Net interest income	1,101**	1,126	–2.2
Net commission income	154	206	–25.4
Administrative expenses	–595	–702	–15.2
Net result from financial operations	0	–13	
Operating profit before risk provisions	705	682	3.3
Cost/income ratio	47.4%	53.3%	

Balance sheet figures	30.06.03 EUR bn	31.12.02 EUR bn	Change in %*
Total assets	328.0	341.3	–3.9
Lending volume***	223.1	240.0	–7.1
Total deposits	193.3	199.6	–3.2
Securitised liabilities	104.4	108.2	–3.5
Own funds disclosed	17.1	18.0	–5.4

Derivatives transactions	30.06.03 EUR bn	31.12.02 EUR bn	Change in %*
Nominal volume	1,136.0	1,141.9	–0.5
Credit risk equivalent	10.0	9.5	4.7

Key banking regulatory data under the German Banking Act (KWG)	30.06.03	31.12.02	
Core capital ratio	7.3%	6.4%****	
Equity ratio (at Group level)	10.8%	10.3%****	

Number of employees	30.06.03	31.12.02	Change in %*
Whole bank	5,729	5,932	–3.5
Group	9,222	9,605	–4.2

* Percentage changes are based on figures that are not rounded.
** As in the case of other Landesbanks, interest expenditure for capital contributions of silent partners is disclosed under partial profit transfer (appropriation of profits).
*** Excluding amount due from banks on demand.
**** Based on balance sheet figures.

Global presence and German Centre in Shanghai

The BayernLB Group is present in all the world's major financial centres and growth markets. The Bank offers a wide range of financial products and services both to its own customers and to the customers of the Bavarian savings banks. In addition, BayernLB provides extensive practical support through the German Centre for Industry and Trade in Shanghai, especially to its SME customers, and offers a cost-effective solution for companies wishing to enter the Chinese market. More detailed information – including news of the New German Centre Shanghai currently under construction – and the contact address can be found on the internet at: www.germancentreshanghai.com.

Contact

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Interim report as at 30 June 2003

Bayerische Landesbank
Finanzgruppe

Bayerische Landesbank consolidated balance sheet

Group	30.06.03 EUR bn	31.12.02 EUR bn	Change in %*
Assets			
Cash reserves	1.0	1.1	–8.0
Due from banks	104.5	108.1	–3.3
Due from customers	133.5	138.9	–3.9
Bonds and other fixed-interest securities	68.2	73.0	–6.5
Shares and other non fixed-interest securities	3.1	3.1	–1.6
Investments and shares in affiliated companies	3.0	3.0	–0.4
Assets administered on behalf of third parties	8.9	9.0	–1.0
Tangible assets	0.4	0.4	–4.4
Other assets	5.4	4.7	13.6
Liabilities			
Due to banks	120.4	135.4	–11.1
Due to customers	72.8	64.2	13.4
Securitised liabilities	104.4	108.2	–3.5
Liabilities administered on behalf of third parties	8.9	9.0	–1.0
Other liabilities	4.5	6.4	–33.4
Subordinated liabilities	4.5	5.6	–19.0
Profit-participation certificates	2.8	2.9	–2.5
Fund for general banking risks	0.5	0.5	0.0
Capital and reserves	9.2	9.1	1.8
Total assets	328.0	341.3	–3.9

* Percentage changes are based on figures that are not rounded.

Ladies and Gentlemen

The macroeconomic outlook remains subdued in 2003. In the first half of the year, the economy in Germany stagnated and the number of company insolvencies rose 4.6% to around 19,200. The growing need for structural reform in many areas (including the labour market and social security systems) is exacerbating the situation in the financial sector. The withdrawal of the guarantee mechanisms (maintenance obligation and guarantee obligation) in July 2005 means that there is now a crucial need for the Landesbanks to adapt. They also have to comply with banking supervisory regulations at international level (e.g. Basle II) and national level (e.g. Minimum Requirements for the Credit Business of Credit Institutions).

Bayerische Landesbank (BayernLB) has reacted to the changed operating environment and the challenges it brings with a **strategic realignment** and the introduction of a **new business model**. The objective of the new business model is to achieve a long-term credit rating of at least A+ after the withdrawal of the guarantee mechanisms. Essentially, the initiative will bring a greater centralisation of functions and decision-making at Head Office in Munich and a clear focus on the Bank's core competencies. BayernLB intends to reduce its costs, enhance its earnings after risk provisions and strengthen its capital base.

The BayernLB business model positions the Bank as a **wholesale bank with a focus on key regions**. Our target groups are medium-sized and large companies, financial institutions and real estate customers. We also see the Bavarian savings banks and municipalities, the Free State of Bavaria, municipalities outside Bavaria and other states and Länder as key customers. **Geographically,** we will focus on our core markets – Bavaria and the rest of Germany – and on neighbouring countries and selected economic and financial centres worldwide. In this connection, the Bank's network of entities in Germany and abroad will be significantly rescaled.

The implementation of the **Central Bank to the Savings Bank Function** as an organisational interface within BayernLB underlines the importance we attach to the Savings Banks Association in Bavaria. Together with the savings banks, we will deliver banking services throughout Bavaria. BayernLB will be further developed into a **"network bank"**. This means that in future the network of binding, mutually beneficial service agreements between the legally and economically independent members of the association will be even more tight-knit and closely structured. Currently we are working with the Bavarian savings banks on four subprojects to determine the specific structure of the network so that, for instance, joint marketing initiatives in Bavaria can be further optimised.

The **rescaling of operations** means that staff numbers must be adjusted and appropriate staff training provided. A mechanism based on personnel law has been developed to this end and will be implemented in line with social aspects. Redundancies will only be considered as a last resort.

BayernLB is to further deepen and consolidate its successful **strategic cooperation** with Landesbank Hessen-Thüringen (Helaba). The joint Transaktionsbank (TxB) was awarded bank status for securities settlement in February 2003 and is now successfully offering its range of services to third parties. Negotiations are also underway with further partners. Recently, Helaba and HSH Nordbank signed a letter of intent for the merger of the two transaction banks, TxB and Plus Bank.

It is vital for the success of the new business model and therefore the future of BayernLB that the **risk, earnings and cost targets** are met simultaneously by 2005/2006. These targets are specifically for the core bank (BayernLB excluding LBS and Labo) to reduce its net risk provisions from an average of around EUR 1 billion over the last five years to approximately EUR 400 million p. a.; to increase its margins in order to stabilise earnings; and to reduce costs from EUR 858 million to around EUR 600 million p. a.

The rigorous implementation of the new business model, for which we can count on the full support of our shareholders – the Free State of Bavaria and the Association of Bavarian Savings Banks – puts us in a good position to improve our profitability after risk provisions on a sustainable basis and to achieve a competitive rating. We are setting about the task of implementation with great resolve and are confident that, together with our shareholders and staff, we can meet these ambitious targets and go forward with renewed strength as a reliable and expert partner for our customers.

The Board of Management

Results and business performance in the first half of 2003

Results

In the first half of 2003, operating conditions were difficult both in Germany and in the international markets. Consequently, operating earnings did not quite match the high level of the year-earlier period. However, as a result of rigorous cost-cutting measures, administrative expenses were much lower than in 1H02.

Despite a slightly improved margin on new business, there was a small decline in net interest income (-2.2% to EUR 1,101 million) due to a sharp decline in trading volumes.
In line with general practice, interest expenditure for capital contributions of silent partners is now reported under partial profit transfer. The fall in commission income to EUR 154 million (-25.4%) is mainly due to the outsourcing of securities settlement to LB Transaktionsbank (TxB).

Net income from financial transactions, which was nil as at 30 June 2003 due to the application of the imparity principle, is expected to be comfortably in the black by year-end.

Administrative expenses were reduced by 15.2% compared with the year-earlier period: staff costs were 16.9% lower, while operating expenditure was cut by 13.3%. This was achieved through outsourcing measures, reductions in headcount and cuts in voluntary social benefits.

Business performance

Consolidated total assets fell 3.9% to EUR 328.0 billion in the first six months of 2003. The lending volume contracted more sharply (-7.1% to EUR 223.1 billion). In particular, there was a decline in the volume of lending business outside Germany, where exchange rate trends made an impact.

On the funding side, there was an encouraging increase in customer deposits, which rose 13.4% to EUR 72.8 billion. Securitised liabilities fell 3.5% to EUR 104.4 billion. In response to the lower funding requirements, interbank liabilities were also scaled back (-11.1% to EUR 120.4 billion). Own funds disclosed were reduced by EUR 0.9 billion to EUR 17.1 billion. This was mainly attributable to subordinated liabilities no longer needed falling due. The systematic reduction in risk assets led to an increase in the core capital ratio from 6.4% to 7.3%, and pushed up the equity ratio (at Group level) from 10.3% to 10.8%.

Outlook for full-year results 2003

We expect earnings to stabilise further in 2H03 – in line with the objectives of our new business model. Earnings in the previous year were impacted to a significant extent by exceptional factors. Administrative expenses will be appreciably below the previous year's figure as a result of the cost-cutting measures taken. Risk provisions in lending business currently look set to come in below the previous year's high level. These trends will be accompanied by a continued focus on business activities that can deliver sustained profitability, particularly at the foreign entities. Based on these assumptions, we expect 2003 operating earnings before risk provisions to be at the same level as in 2001.