

# Risk Report

As an international real estate investor, property owner and project developer, IMMOFINANZ is exposed to a variety of general and branch-specific risks in its business operations. An integrated risk management process provides the Group with a sound basis for the timely identification of potential risks and the assessment of the potential consequences.

Risks represent the possibility of deviating from planned targets as the result of "coincidental" disruptions caused by the unpredictable nature of the future. In this connection, negative variances are considered risks in the strict sense of the term and positive variances are seen as opportunities.

## Principles of integrated risk management

The structure of risk management is based on the rules of the Austrian Corporate Governance Code and the integrated framework of the COSO ERM\*, an internationally recognised framework concept for the design of risk management systems.

Based on the hedging and management instruments currently in use, no material risks can be identified at the present time that could endanger the company's standing as a going concern. The overall risk situation for the 2020 financial year was influenced by the COVID-19 pandemic through an increase in the uncertainty factors affecting the company and the entire market environment. The potential effects of the COVID-19 pandemic on the 2021 financial year are discussed in detail at the end of this risk report.

IMMOFINANZ has anchored the procedures for handling risk in a Group-wide risk management system, which is integrated in business practices and reporting paths and has a direct influence on processes and strategic decisions. Risk management takes place at all levels through internal guidelines, reporting systems and the internal control system (ICS) which is monitored by the internal audit department.

### Monitoring and control of the risk management system

The risk management system is monitored and controlled through two corporate channels. On the one hand, internal audit evaluates the effectiveness of risk management and contributes to its improvement. On the other hand, the auditor reviews the effectiveness of risk management in accordance with C-Rule 83 of the Austrian Corporate Governance Code (in the version released in January 2021) and reports to the Executive Board on the results of this analysis.

### Evaluation of the functionality of the risk management system

Deloitte Audit Wirtschaftsprüfungs GmbH, Vienna, evaluated the effectiveness of IMMOFINANZ's risk management system during the period from November 2020 to January 2021. This analysis covered the design and implementation of the measures and organisational procedures instituted by the company, but not their application in the sense of operating effectiveness. Based on the knowledge gained by Deloitte during the related activities, no circumstances were identified that would lead to the assumption that the risk management system instituted by IMMOFINANZ as of 31 December 2020 – based on the comprehensive framework for corporate risk management according to COSO – is not functional.

## Structure of risk management

The goal of risk management is to implement the strategy defined by the Executive Board with a minimum of risk. This implementation transfers the Group's strategic goals to the operating processes in which the measures for the identification, prevention and management of risks are embedded.

\* Committee of Sponsoring Organisations of the Treadway Commission – Enterprise Risk Management; [www.coso.org](http://www.coso.org)



The Executive Board, as a whole, is responsible for risk management in the IMMOFINANZ Group and defines the corporate goals and related risk strategy.

Risk management is a staff function which reports directly to the Chief Financial Officer (CFO). It monitors the corporate risks that are not related to specific business areas, aggregates risk data and reports, and actively supports the business areas and country organisations in the identification of risks and economically feasible countermeasures. Risk management reports regularly to the Executive Board and quarterly to the Supervisory Board.

At the business area and country organisation levels, the heads of the respective business area or country organisation are responsible for risk management. Risk positions are reported to the Executive Board at least once each quarter by the business area managers and at least twice a year by the country management. Acute risks are reported immediately to the Executive Board.

### **Risk management process**



## Major market and property-specific risks

The development of the real estate markets is dependent on cyclical and macroeconomic factors. The related risks include events on the global financial and capital markets as well as political, micro- and macroeconomic issues in the countries where IMMOFINANZ is active. These factors can have a significant effect on the market value of properties, earnings and development plans as well as investment and sales activities.

Concentration risk and the risk associated with the property portfolio are addressed through the diversification of property investments by sector and region. IMMOFINANZ focuses on two commercial asset classes – office and retail – in Austria, Germany and CEE. In addition to the diversification of the portfolio by sector and region, a differentiated tenant structure is also important for minimising risk. IMMOFINANZ has a balanced and diversified tenant mix.

Description of risk	Effects	Measures
<b>Rental risks</b>	Loss of income due to vacancies	Proactive rental management (close cooperation with tenants, high service orientation, continuous optimisation of offering and tenant mix)
	Default on rental payments due to deterioration of economic environment or tenant bankruptcies	Continuous monitoring of rental status, credit evaluation of tenants, security deposits, diversification of tenants
	Decline in rental income due to intense competition	Selection of attractive locations, granting of incentives for tenants
	Rental price reductions or costly incentives to retain tenants	Review and release of rental contracts and incentives as per corporate approval guidelines, granting of rental price reductions for a limited period
	Inflation risk	Index clauses in rental contracts
<b>Project development risks</b>	Reduction in income through limitations on use	Investments in quality and maintenance management, selection of professional service providers
	A location turns out to be suboptimal in relation to demand, competitive behaviour or economic power	Market, competitive and site analyses, if necessary exit from certain regions
	Delays in initial rentals	Definition of minimum pre-rental levels
	A project cannot be realised as planned, e.g. because of problems with financing, approvals or historical protection	Extensive analyses and project planning, timely communications with banks and public authorities, thorough due diligence
	Construction defects lead to delays and higher costs	Continuous monitoring of construction progress and quality
	Problems arise with general contractors or subcontractors	Selection of experienced business partners and continuous control of all contractors and subcontractors
<b>Property valuation risks</b>	A project cannot be realised as planned due to higher costs or delays	Detailed project organisation, regular cost, quality and schedule controls, variance analyses, selection of experienced partners, transfer of risks
	High dependence on macroeconomic environment, calculation method and underlying assumptions: decline in valuation due to negative market developments or as a result of lower "return" on the property	Market studies, analyses and forecasts, portfolio optimisation, continuous maintenance and modernisation
<b>Transaction risks</b>	High dependence on transaction market liquidity: a transaction is not realised as planned, e.g. because the seller drops out or the desired price is not achievable	Market analyses, legal, economic and technical due diligence, checklists for the transaction process, analysis of effects on the portfolio

## Major business and other risks

Description of risk	Effects	Measures
<b>Strategic business risks</b>	Increase in similar risks in the portfolio	Diversification by sector and region
	Capital market movements make it difficult to raise equity or debt	Balanced structure of equity and debt
	Loans for projects and transactions are not available	Medium-term planning, capital and liquidity management; investment grade rating provides access to new capital market segment
<b>Financial risks</b>	See note 7.2 to the consolidated financial statements	See note 7.2 to the consolidated financial statements
<b>Legal and tax risks</b>	Legal disputes with tenants, business partners, investors or public authorities	Continuous monitoring of legal developments, creation of provisions
	Changes in national tax schemes result in subsequent tax liabilities	Continuous monitoring of legal developments, compliance with disclosure requirements
<b>Organisational risks</b>	IT risks materialise, e.g. failure of technical systems, unauthorised data access or manipulation	Group-wide IT governance and compliance, continuous updating of security standards, penetration tests, connections to geographically separate back-up data processing facility, strengthen awareness among employees through specialised IT training
	Environmental risks, e.g. extreme weather conditions, natural disasters or man-made damages like ground contamination can result in damages to properties	Insurance to cover environmental damage
	HR risks like staff turnover lead to the loss of top performers or capacity bottlenecks	Personnel development and appropriate remuneration and bonus systems
	Compliance risks materialise, which can result in penalties and damage to the company's reputation	Strict compliance with legal regulations and regular training for employees
	Procurement risks, e.g. dependence on suppliers and subcontractor bankruptcies, can lead to supply shortages	Optimisation of supplier base, development of sourcing strategies, ongoing and comprehensive evaluation of suppliers
	Implementation of digitalisation strategy	Sufficient resources for individual projects, professional project management throughout the Group, proactive management of digitalisation process
<b>Investment risks</b>	Fluctuations in the fair value of the S IMMO investment	Continuous monitoring and evaluation
<b>Environmental and social governance risks</b>	Changes in the climatic conditions at the property locations lead to future expenses	An analysis of the standing investment portfolio based on climate models is planned; necessary adjustments will be made in connection with regular maintenance; development projects already reflect future climate conditions
	Today's commercial properties do not meet CO <sub>2</sub> -neutrality standards	Further development of existing concepts, integration of new technologies
	Implementation of circular economy in the real estate sector creates major challenges for companies	Prevention of future contamination in new construction, integration of new technologies
	Attainment of material equality between women and men	Career advancement for women in the company, measures to improve the work-life balance
	Demographic developments require a focus on diversity and inclusion	Further development of the corporate culture, conscious approach to the issues of diversity and inclusion

## Features of the internal control system

IMMOFINANZ's internal control system (ICS) comprises a wide range of measures and processes to protect assets and to ensure the accuracy and reliability of accounting. The goal of the ICS is to prevent or identify errors and therefore allow for early correction. The ICS also supports compliance with the major legal directives and the business policies defined by the Executive Board.

The ICS is integrated in individual process flows. The key features of the ICS in accounting processes are the appropriate segregation of duties, the application of the four-eyes principle in all order and invoice release procedures, compliance with internal guidelines (e.g. IMMOFINANZ's IFRS accounting manual), the review of accounting data by Group controlling for correctness, plausibility and completeness, the integration of preventive and detective controls in processes as well as automatic key controls through specific software settings.

### Monitoring by internal audit

Internal audit is responsible for the independent review of the effectiveness of the ICS and, in this way, contributes to its quality control. This department also evaluates the effectiveness of risk management and supports its continuous improvement. Based on an annual audit plan approved by the Supervisory Board, the internal audit department independently and regularly reviews operating processes and business transactions. The priorities for this schedule are defined in accordance with risk criteria and organisational goals.

The results of the audits are reported to the IMMOFINANZ Executive Board on a regular basis and to the Supervisory Board twice each year. As part of an annual report, the internal audit department gives an account of its performance and presents a summary of the major audit areas and results.

## Opportunity and risk position in 2020

### Overview of opportunities and risks as of 31 December 2020



**COVID-19 (1)**

The risk position during the 2020 financial year and at the beginning of 2021 was influenced by the COVID-19 pandemic and its impact on the real estate sector and the entire economy. In the retail business, the government-ordered temporary shutdown of commercial enterprises in the IMMOFINANZ core markets had a negative effect on rental income. The VIVO! shopping centers were hit harder than the STOP SHOP retail parks, which have very limited common areas and focus on everyday, cost-efficient products. In order to offset the temporary decline in rental income from the retail business on cash flow, the Executive Board introduced a cost savings programme in March 2020. It includes, among others, the postponement of non-essential investments and expenditures, the reduction of overheads and the renegotiation of supplier contracts. An unsecured, revolving corporate credit line was also arranged to give IMMOFINANZ greater financial flexibility. The office business was not affected by the government-ordered, temporary shutdowns, but most of these tenants followed the call to introduce home office as a measure to contain the pandemic. Tenants received support in returning to work with back-to-office plans that included room concepts, distance guidelines, disinfection, protective measures and access rules. A separate task force was installed to manage hygiene procedures for the common areas to ensure the safe use of office and retail space. Project development was faced with temporary limitations on construction and the resulting delays, which differed by country but were not material.

The COVID-19 pandemic was also responsible for price disruptions on the international capital markets, which were reflected in the development of the IMMOFINANZ share price. The annual low of EUR 11.50 was reached on 30 October 2020 (-51.9% versus the 2019 closing price). As a means of supporting the capital markets and the economy, the ECB resumed its bond purchase programme and injected additional liquidity into the banking sector. The European Union launched an assistance package for the countries most affected by the pandemic, and national governments implemented measures to increase household consumption and support companies. The outlook for the 2021 financial year shows that further negative macroeconomic developments and the negative effects of the crisis on Group results cannot be excluded. They involve, among others, a downstream wave of bankruptcies due to the expiration of government assistance. This potential increase in insolvencies is connected with the risk of a deterioration in the financing situation for companies. Banks affected by receivables write-offs could be lost as financing partners, which could lead to a dangerous shortage of liquidity on the capital market.

IMMOFINANZ took a proactive step in July 2020 to strengthen its equity through the placement of shares and a mandatory convertible bond. The EUR 500.0 million benchmark bond issued in October 2020 marked a further step by IMMOFINANZ to increase its financial flexibility and optimise the capital structure.

The expected long-term effects of the COVID-19 pandemic include, for example, changes in consumer behaviour and in the modern working world that will have an impact on the property solutions offered by IMMOFINANZ. In the retail business, this can range from more conscious purchasing behaviour to the avoidance of public areas. In the office business, the increased use of home office and the current recession can lead to changes in the demand for office space. The Executive Board sees IMMOFINANZ well positioned to address these challenges with its cost-efficient STOP SHOP and VIVO! retail concepts and its high-quality, innovative office solutions.

**Macroeconomic conditions (2)**

Private household consumption was a key driver for economic growth in the individual IMMOFINANZ core markets during the years prior to 2020. Rising unemployment and a growing shift towards savings had a negative effect on consumer spending in 2020, a development which government support measures – like short-time work – were unable to offset. However, the momentum in private consumption will play a decisive role in overcoming the economic effects of the pandemic. This is important for IMMOFINANZ, above all, in the retail business. In the office business, a longer recession or only slight recovery after the pandemic could lead to weaker demand and, as a result, to higher vacancies and/or pressure on rental levels.

**Legal proceedings (3)**

IMMOFINANZ has settled numerous historical legal disputes in recent years. The proceedings over restitution demands for the VIVO! shopping centers in Cluj and Constanța, Romania, are still in progress. There were no decisive changes in these proceedings during the past year.

**Investments (4)**

IMMOFINANZ AG acquired 19,499,437 bearer shares in S IMMO AG through share purchase contracts dated 18 April 2018. The transaction closed on 21 September 2018. The S IMMO share is listed in the Prime Segment of the Vienna Stock Exchange and is therefore exposed to market price risks. This material investment is included in the consolidated IFRS financial statements at equity. The S IMMO share lost 23.9% of its value during 2020 and closed the year at EUR 16.96. The decline represented an impairment trigger and led to a write-down of EUR 88.6 million to the investment. As of 31 December 2020, the carrying amount of the S IMMO investment equalled EUR 363.6 million, or 5.3% of IMMOFINANZ's total assets. The investment was not financed externally. The significant improvement in the price of the S IMMO share since 31 December 2020 provided objective indications of an increase in the value of this investment at the end of the first quarter of 2021. Therefore, an increase in the carrying amount of the investment up to the realisable amount of EUR 459.8 million (based on the closing price of EUR 21.45 on 31 March 2021) is possible as of 31 March 2021.

**Valuation risks (5)**

The pandemic has influenced property valuation through the general increase in risk and the subsequently higher market yields. The retail properties, in particular, were affected by this development. The external appraisals by CBRE reflected slightly higher market yields (increase of up to 50 basis points in the retail segment) as well as changed assumptions concerning re-rentals in the portfolio properties. Revaluation results for the 2020 financial year totalled EUR -166.5 million.

The COVID-19 pandemic led to an increase in market yields, above all in the retail segment, and consequently to the recognition of impairment losses. The 2020 recession and the expiration of government support measures could result in weaker demand for office space and an increase in yields during 2021.

**IT risks (6)**

IMMOFINANZ has set a goal to digitalise its corporate processes up to the customer. These projects are connected with corresponding risks, which are being addressed with professional project management. The projects scheduled for 2020 were realised as planned, and there are currently no indications of increased risk for the projects planned for 2021. Furthermore, the issues of data protection and cybersecurity represent a focal point of risk analysis. IMMOFINANZ not only addresses these issues through the involved systems, but also gives high priority to employee training. Corporate processes are also being optimised to guarantee the highest possible level of security. Based on the previously established procedures the risk for critical corporate processes can be considered very low.

### **Energy efficiency (7)**

Energy efficiency in properties is crucial for the reduction of CO<sub>2</sub>. IMMOFINANZ's goal is to identify opportunities for savings and continuously improve the portfolio with regard to energy efficiency and the contribution to climate protection. One project group is working to develop measures to make the portfolio climate-neutral over the long term. Preparations have also started to implement the EU's Taxonomy Regulation. The focus on energy-efficient properties and activities which are considered "sustainable" under the EU taxonomy will create numerous opportunities, for example in the areas of tenant satisfaction, financing, positioning on the capital market and the contribution to climate protection.

### **Climate and environmental risks (8)**

Global warming leads to climate change over the long term and, in turn, creates challenges for real estate investors. These challenges include, for example, an increase in serious weather phenomena, like heavy rains, flooding, dryness, hail etc., which can cause damage to IMMOFINANZ's buildings and result in higher insurance premiums. However, climate change also makes it necessary to evaluate the site of every property in light of future conditions and to undertake necessary construction measures today. A further aspect involves the changing regulatory conditions in the real estate sector. The government goal to achieve CO<sub>2</sub> neutrality as well as new legal requirements, like the EU Taxonomy Regulation, require the further improvement of buildings and can question the viability of individual business areas. The goal to realise a circular economy against the backdrop of resource conservation represents a significant challenge for the real estate branch from the current point of view. At the same time, it creates competitive advantages for companies that can offer solutions to these issues.

### **Portfolio risks (9)**

The overall occupancy rate for IMMOFINANZ's portfolio remained high at 96.0% as of 31 December 2020, which represents a decline of 0.8 percentage points since 31 December 2019. The occupancy rate equalled 93.7% (31 December 2019: 95.3%) in the office properties and was constant at a high 98.1% (31 December 2019: 98.3%) in the retail properties.

The development projects currently under realisation by IMMOFINANZ (property under construction) have a combined carrying amount of EUR 300.8 million (31 December 2019: EUR 177.5 million). The outstanding construction costs for these development projects totalled EUR 62.2 million as of 31 December 2020 (31 December 2019: EUR 111.9 million). The pipeline projects, including real estate inventories, had a carrying amount of EUR 191.8 million as of 31 December 2020 (31 December 2019: EUR 173.2 million).