

Teleios Capital Partners LLC

Baarerstrasse 12
6300 Zug
Switzerland

T: +41 41 506 56 56

W: teleioscapital.com

**The Supervisory Board
Aareal Bank AG
Attn: Prof. Dr Hermann Wagner, Chairman of the Supervisory Board
Paulinenstrasse 15
65189 Wiesbaden
Germany**

10th February 2022

Dear Mr Wagner,

Teleios Capital Partners LLC (including affiliated entities, "Teleios") has been a major shareholder in Aareal Bank AG ("Aareal" or the "Company") for almost three years, with a disclosed shareholding of 3,773,872 shares, representing an interest of 6.3% in the Company's issued share capital.

We are writing to express concerns we believe to be widely held amongst shareholders about longstanding breaches in elementary governance standards at the Company. We also wish to outline next steps to ensure that Aareal's Supervisory Board (the "Board") respects best practice principles, that all stakeholders including shareholders are treated fairly, and that Aareal's value potential is not squandered due to management ineptitude or unfettered self-interest.

We have taken the decision to make this letter public as we believe this matter has relevance for all Aareal stakeholders.

A Board-endorsed takeover offer that left shareholders – and due process – short-changed

Last November, Advent International Corporation and Centerbridge Partners L.P. (together, the "Bidders") announced their intention to launch a takeover bid for Aareal via a public tender offer at €29 per share (the "Offer").¹ The Offer represented a discount to Aareal's share price prior to COVID-19², and inferred a

¹ [Atlantic BidCo GmbH press release, 23 November 2021](#)

² Aareal's closing share price exceeded the initial €29.00 offer price on all trading days between 1 January to 24 February 2020; Bloomberg

book value multiple of just 0.3-0.4x for Aareal Bank³, imputing Advent's reported March 2021 holding valuation for Aareon⁴.

We believe the Offer significantly undervalued the Company on a sum-of-the-parts basis, and was structured to take advantage of Aareal's historically passive shareholder base that tends to follow the Company's recommendations, short-changing those shareholders who believed in Aareal's long-term potential. By setting a low minimum acceptance threshold of just 60%, the Bidders could easily have seized control of Aareal and proceeded to delist the shares shortly after⁵, pressurising those shareholders who did not support the Offer (in theory up to 40% of the register) into selling their increasingly illiquid interest to the Bidders at an even more depressed valuation.

It is the Supervisory Board's duty to act in the best interests of the Company and its shareholders, which in this case should have constituted protecting the Company's independence. Not only did the Supervisory Board fail in this duty, but to our shock, endorsed the Offer.

Major shareholders lined up to criticise the Supervisory Board's actions. Rather than prompting a rethink, what followed seemed like a desperate attempt by the Company and the Bidders to see the Offer succeed at all costs: moving goalposts of declining acceptance thresholds⁶; closed-door solicitation of individual Aareal shareholders by the Bidders and their advisors; misleading media comment suggesting that the Offer was close to succeeding⁷; and reports of questionable and intransparent side deals by the Bidders with select shareholders⁸.

It was announced on 4th February that the Offer had failed, and was subsequently revealed that only 42.55% of shareholders had accepted it, well short of the reduced 60% acceptance threshold.⁹ For all the Bidders' talk of a generous premium¹⁰, since the Offer fell by the wayside, Aareal's shares have hardly declined.¹¹

CEO Jochen Klösges has continued to defend Aareal's endorsement of the Offer as having been "in the best interests of the Company and its stakeholders", and suggested that the outcome means shareholders rather "wish to continue supporting [the Management and Supervisory Boards]".¹² We believe Mr Klösges is under no illusion that many shareholders like ourselves find his comments disingenuous and wishful thinking. Specifically, we believe that management's support for the Offer was not in stakeholder interests but unabashedly self-serving, and that support for Aareal's governing boards is at an all-time low.

Director duties relating to expressions of bidder interest

Following the failure of the Offer, it is distinctly possible that Aareal will receive unsolicited expressions of interest for the Company or its constituent divisions. We are aware of potential strategic buyers for each division that could be inclined to pay significantly more in aggregate than the consideration offered by the

³ Estimated price-to-book multiple for the Company excluding Aareon; assumes Aareon is sold at a \$1.55 billion enterprise value and the estimated capital gain on Aareal's 70% stake is returned to shareholders; Teleios estimates

⁴ As per a recent Bloomberg article, Advent "pegs Aareon's value at \$1.55 billion including debt as of the end of March last year"; [Bloomberg, 14 January 2022](#)

⁵ "Following the settlement of the Takeover Offer [...] the Bidder intends [...] to assess the effectuation of a withdrawal of the admission to trading of the Aareal Shares on the regulated market ("Delisting")."; [Offer Document, 17 December 2021](#)

⁶ On 18th January 2022, the Bidders lowered the minimum acceptance threshold from 70% to 60%; [Atlantic BidCo GmbH press release, 18 January 2022](#)

⁷ In early February, Bloomberg reported that "Bidders are said to near 50% in shareholder acceptance", implying that the takeover offer was close to meeting the 60% minimum acceptance threshold; [Bloomberg, 2 February 2022](#)

⁸ Handelsblatt reported that the Bidders received a call option for 6.85% of shares outstanding from one large shareholder, who chose a "complicated structure" and managed to also secure put options for his shares; [Handelsblatt, 31 January 2022](#)

⁹ [Atlantic BidCo GmbH press release, 7 February 2022](#)

¹⁰ The Bidders claimed that the "Offer Price constitutes an attractive consideration" and "represents a significant premium to relevant value benchmarks"; [Offer Document, 17 December 2021](#)

¹¹ Shares declined by only 5.8% on 7th February 2022, the next trading day after it was announced that the takeover failed; Bloomberg

¹² [Aareal press release, 4 February 2022](#)

previous Bidders. To the detriment of shareholders, such prospective bidders seem thus far to have been shunned by Aareal, whose self-interest may have deterred them from engaging with other parties.

We remind the Board that it is bound by law to take any expression of interest seriously. For the avoidance of doubt, we will regard any out-of-hand rejection of a serious approach as a potential breach of fiduciary duty, and that failing in such duties might make the members of the Board personally liable for damages.

Stakeholders deserve a clean break from Aareal's compromised governance culture

Our discourse with Aareal dates back several years¹³ and has centred on our long-running concerns that under the Board's supervision, Aareal has acted improperly in key matters, such as proceeding with the sale of a 30% stake in Aareon without first performing an independent review of all strategic alternatives¹⁴, and leaving the Company without an active CEO for ten months¹⁵. The recent recommendation of a contentious takeover offer raises new questions as to whether the Supervisory Board has fulfilled its duty:

- Why did they recommend an offer that drastically undervalued Aareal on a sum-of-the-parts basis, while still giving the Bidders leeway to break up the Company? Management had reportedly accepted that selling software business Aareon could make sense in the medium term¹⁶, so why not properly evaluate this option before seeking to sell the whole Company at a discount, in return for an empty promise to keep it intact?¹⁷
- Why would they ever recommend that a controlling stake in the Company be sold at an acceptance level as low as 60%¹⁸, especially in the face of reasoned public opposition from major shareholders?
- Having received expressions of interest from other potential bidders in the past, why did they not run a competitive process and actively reach out to such bidders, especially those who would stand to realise significant synergies, in order to maximise the selling price?

With such a chequered governance track record, it did not surprise us when shareholders voted off three Supervisory Board members last December, including the former chair, Marija Korsch, only for their seats to be filled almost immediately with candidates that seemed self-servingly picked by the incumbents to help preserve a substandard status quo.¹⁹

It is the Supervisory Board's statutory duty to examine and assess the appropriateness of a bidder's offer carefully and free from any conflicts of interest against the background of the Company's shares' fair value, taking into account all relevant information available to it or obtainable within the time available. This also includes the examination of possible third party offers and the potential synergies associated with them. In our judgement, Aareal's Supervisory Board has long failed to perform this role, and has therefore lost legitimacy in its current composition.

¹³ [Teleios letter, 26 September 2019](#); [Teleios letter, 15 October 2019](#)

¹⁴ Teleios sent a letter to the Board on 26th September 2019 outlining concerns that a structured and independent review of all strategic alternatives for Aareon had not been undertaken. In Aareal's letter of response on 7th October 2019, management declined our request for a strategic review and misleadingly referred to an internal exercise that fell well short of our request; [Teleios letter, 26 September 2019](#) and [Aareal response, 7 October 2019](#)

¹⁵ On 8th November 2020, Aareal announced that its then chief executive Hermann Merken would not be able to perform his duties for health reasons for an expected period of three to four months. The new chief executive Jochen Klösger was appointed more than seven months later on 15th June 2021 and assumed office more than ten months later on 15th September 2021; [Aareal press release, 8 November 2020](#) and [15 June 2021](#)

¹⁶ [Reuters, 13 January 2020](#)

¹⁷ The Bidders do "not intend to pursue any plans to break up the Aareal Group" but per the Offer document "it is possible that the Bidder may change its intentions"; [Offer Document, 17 December 2021](#)

¹⁸ Aareal's Management and Supervisory boards continued to recommend the Offer, even as the minimum acceptance level was reduced from 70% to 60%; [Aareal press release, 20 January 2020](#)

¹⁹ Aareal's largest shareholder stated that the candidates were nominated "at the expense of diversity and independence"

The Company's forthcoming general meeting on 18th May (the "AGM") is an ideal time for a clean break from the lackadaisical governance culture that has for some years cast a shadow over Aareal, and to install new independent directors who are not connected to the old guard, can bring their pedigree sector expertise to bear for all stakeholders' benefit, and take their duties seriously.

We expect the principal protagonists of the failed Offer debacle, including the Board's chairman Mr Wagner, to acknowledge their misjudgement and resign now, and not offer themselves for re-election at the AGM.

We believe we speak for all stakeholders when we say that we are eager for the Board to establish proper corporate governance and refresh its composition. We look forward to making or supporting shareholder proposals in the coming weeks for independent replacement candidates to be appointed at the AGM.

Yours faithfully,



Adam Epstein
Partner