VOLKSBANK AG

HALF-YEAR FINANCIAL REPORT

AS AT 30 JUNE 2014

KEY FIGURES

Euro million	30 Jun 2014	31 Dec 2013	31 Dec 2012
Statement of financial position VBAG Group [1]			
Total assets	**18,782**	**20,904**	**27,640**
Loans and advances to customers	5,905	7,081	10,040
Amounts owed to customers	1,936	2,148	2,542
Debts evidenced by certificates	5,202	7,085	9,935
Subordinated liabilities	537	555	621
Own funds according to Basel III for the Association of Volksbanks credit institutions [2]			
Common equity tier 1 capital (CET1)	2,955		
Additional tier 1 capital (AT1)	0		
Tier 1 capital (T1)	2,955		
Tier 2 capital (T2)	1,103		
Own funds	4,058		
Risk weighted exposure amount - credit risk	22,656		
Total risk exposure amount market risk	782		
Total risk exposure amount operational risk	2,345		
Total risk for credit valuation adjustment	690		
Total risk exposure amount	26,473		
Common equity tier 1 capital ratio [3]	**11.2 %**		
Tier 1 capital ratio [3]	**11.2 %**		
Equity ratio [3]	**15.3 %**		
Income statement VBAG Group [4]	**1-6/2014**	**1-6/2013**	**1-6/2012**
Net interest income	104.2	132.7	116.7
Risk provisions	–23.6	–27.3	–73.8
Net fee and commission income	10.3	18.9	37.9
Net trading income	4.8	–26.8	23.6
General administrative expenses	–126.6	–126.2	–132.8
Other operating result	–23.8	66.0	–33.2
Income from financial investments	–7.0	–21.2	64.1
Income from companies measured at equity	–127.9	–59.9	–1.8
Income from discontinued operation	0.0	15.3	48.6
Result before taxes	**–189.7**	**–28.6**	**49.2**
Income taxes	3.9	–27.2	–18.8
Result after taxes	**–185.8**	**–55.8**	**30.4**
Non-controlling interest	–17.2	–12.5	–16.3
Consolidated net income	**–203.0**	**–68.3**	**14.1**
Key ratios [4]			
Operating cost-income-ratio	106.1 %	101.1 %	74.5 %
ROE before taxes	–33.8 %	–7.3 %	0.3 %
ROE after taxes	–33.2 %	–11.8 %	–7.4 %
ROE consolidated net income	–42.0 %	–16.6 %	–25.1 %
ROE before taxes (regulatory)	–29.4 %	–8.6 %	0.1 %
Resources [4]			
Staff average	1,820	1,877	1,960
of which domestic	1,078	1,122	1,178
of which abroad	742	755	782
	30 Jun 2014	**31 Dec 2013**	**31 Dec 2012**
Staff at end of period	1,810	1,853	1,912
of which domestic	1,074	1,101	1,137
of which abroad	736	752	775
Number of sales outlets	2	2	2
of which domestic	1	1	1
of which abroad	1	1	1

1) The comparative figures of 2012 were adjusted according to IAS 8.

2) Starting with 1 January 2014, own funds are calculated according to Basel III for the Association of Volksbanks of credit institutions. Before the figures were based on Basel II regulations and computed for the VBAG Group of credit institutions. As a comparison would be of limited information, no comparative figures were displayed.

3) In relation to total risk

4) The operating cost-income-ratio is the ratio between net interest income, net fee and commission income, net trading income and general administrative expenses. All ratios were displayed without including discontinued operation or disposal group.

CONTENT

Interim Report

Any role descriptions in this interim report that are used only in the masculine form apply analogously to the feminine form.
English translation by BBi (Scotland) Ltd.

INTERIM MANAGEMENT REPORT AS AT 30 JUNE 2014

Report on business development and the economic situation

Österreichische Volksbanken Aktiengesellschaft (VBAG) is the parent company of subsidiaries operating in Austria and abroad. Since its partial nationalisation April 2012, VBAG has been undergoing a transformation process that is based on a restructuring plan and consequently the requirements of the EU Commission and the Republic of Austria. VBAG is a winding-down bank that is required to discontinue or sell almost its entire proprietary business both in Austria and abroad.

In 2012, it was also decided to restructure the Volksbank sector into a banking association in accordance with section 30a of the Austrian Banking Act (joint liability and liquidity association): since 18 September 2012, the primary banks and VBAG have constituted the Association of Volksbanks, with VBAG as the central organisation. The responsibilities of VBAG are clearly defined within this association: as the central organisation, it undertakes far-reaching management and steering functions, including being responsible for risk and liquidity management across the association. Its business activities are now restricted to the provision and brokering of products and services for Volksbanks and their customers.

The Non-core domain bundles all assets, including participating interests in subsidiaries, that no longer form part of VBAG's core business. In accordance with the restructuring plan, these must be wound down or sold while maintaining their value. In terms of subsidiaries and associated companies, these comprise in particular Volksbank Romania S.A. (VB RO), the VB Leasing International Group (VB LI) as well as Volksbank Malta and IK International Bank, Malta During the period under review, sales negotiations were concluded successfully for a number of companies. In addition, lending portfolios and further financing facilities that are allocated to the Non-core segment are gradually being wound down or sold.

Regulatory supervision (own funds and risk amounts) is exercised over the VBAG group both at the level of the consolidated financial statements of the financial holding group, as well as at the level of the Association of Volksbanks pursuant to section 30a of the Austrian Banking Act (BWG). Where key regulatory indicators are referred to below, these relate to the Association of Volksbanks. The scope of consolidation from a regulatory perspective is determined by the Capital Requirements Regulation (CRR, so-called Basel III) which has been valid since 1 January 2014, and which diverges from the financial statements for the VBAG Group prepared according to IFRS. Significant differences occur in the case of other companies outside the sector that are to be consolidated according to IFRS if the preconditions of IFRS 10 have been satisfied, or in the case of certain financial sector companies. The Association of Volksbanks is made up of banks from the primary sector, VBAG and its subordinated institutions.

Under the CRR, financial sector companies that are controlled or where a capital majority exists are fully consolidated. As a consequence, and in contrast to the VBAG consolidated financial statements, VB RO and VBI Beteiligungs GmbH continue to be included in the scope of consolidation pursuant to CRR. Institutions, banks and providers of ancillary services which are controlled, but which are immaterial for the presentation of banking groups pursuant to Article 19 (1) of the CRR, and which are consequently not consolidated, are deducted from own funds. Quota consolidation is applied where subsidiaries are managed jointly with third-party companies. Participating interests of between 10% and 50% in financial sector companies where no joint management occurs are also deducted from own funds unless they are voluntarily included on a proportional basis in the consolidated financial statements. Participating interests of less than 10% in financial sector companies are deducted from own funds under the eligibility rules pursuant to Article 46 of the CRR. All other participating interests are included in the measurement basis at their carrying amounts.

Economic environment

Austria's GDP grew only slightly in the first half year of 2014. Seasonally adjusted economic growth was 0.1% q/q in the first quarter and – according to estimates by the Austrian Institute of Economic Research – 0.2% in the second quarter. Private consumption, the most important element of GDP by far, increased in both quarters only moderately by 0.1% q/q respectively. The development of public consumption was more favorable. Growth was affected negatively by gross investments in the first and second quarter and by foreign trade in the first quarter. The euro zone showed a similarly weak development. Growth rates published by Eurostat were 0.2% q/q in the first quarter and 0.0% (according to estimates) in the second quarter.

The Austrian unemployment rate remained high throughout the first six months of the year, but was still the lowest in the euro zone. In June, it stood at 5.0%, up from 4.9% in May and 4.8% in April. By contrast, the unemployment rate in the euro zone contracted slightly – albeit from a much higher level. It stood at 11.5% in June on a seasonally-adjusted basis, compared to 11.8% at the start of the year. Greece and Spain recorded the highest rates (27.3% and 24.5% respectively).

According to the Harmonised Index of Consumer Prices (HICP), Austria's inflation rate fluctuated during the first six months of the year, moving within a narrow band ranging from 1.4% in March to 1.7% in June. Although it remained below the European Central Bank's target of just under 2%, inflation in Austria was consistently one of the highest in the euro zone. In the currency zone as a whole, the rate of inflation failed to reach even 1% in any of the first six months of the year. In June, inflation stood at 0.5%, with three member states (Greece, Portugal and Slovakia) even registering negative rates.

The European Central Bank left its key interest rate unchanged at 0.25% in the first quarter, but cut it by 10 basis points in June to 0.15%. The interest rate for the marginal lending facility was cut by 35 basis points to 0.40%, while the deposit rate moved into negative territory for the first time in the history of the European Central Bank after being lowered by 10 basis points to –0.10%. The three-month Euribor barely changed at all throughout the first half of the year, remaining at an extraordinarily low level. It stood at 0.21% at the end of June.

Yields on government bonds which are regarded as safe showed a marked downward trend in the first six months of 2013. At the end of the second quarter, yields on Austrian ten-year government bonds stood at 1.55%, and on German ten-year government bonds at 1.25%; in each case this is around 70 basis points lower than at the start of the year. Moderate economic development in Europe, low inflationary pressure and the resultant prospect of a continuation of expansionary monetary policy, coupled with heightened geopolitical risks (Ukraine, Middle East), were the main factors behind this trend.

Economic performance in Central and Southern Europe varied widely during the first half of the year. While Hungary and Poland were positive, Croatia was once again very weak.

In Romania, where the economy was still reporting strong growth of 3.9% y/y and by 0.2% q/q in the first quarter of this year, a marked cooling occurred during the second quarter. According to a preliminary estimate by Romania's statistical office, gross domestic product grew by just 1.2% year-on-year, and even shrank by as much as 1.0% in a quarter-on-quarter comparison, and on a seasonally adjusted basis.

The unemployment rate in Romania barely changed at all over the first six months of the year, totalling 7.1% in June according to Eurostat calculations. The inflation rate continued to fall from what was already a low level by historical standards (from 1.2% in January according to the HICP to 0.9% in June 2013). Low inflationary pressure enabled the National Bank of Romania to lower its key interest rate in two stages from 4.0% to 3.5% in January and February. The leu was relatively stable, closing the first half of the year slightly stronger than it was six months previously, despite cuts in the key interest rate.

Business development and material events in the first sixth month of 2014

VBAG's role and responsibilities changed permanently following its partial nationalisation in April 2012, the resolution regarding section 30a of the Austrian Banking Act and the banking association agreement based thereon. VBAG is a de facto bank in wind-down, meaning that nearly all of the bank's own business in Austria and abroad must be discontinued. In the Managing Board's opinion, the wind-down process should be driven forward as quickly and consistently as possible. The aim is to minimise restructuring expenses whilst also shaping the bank's future and that of the sector as swiftly as possible. The progress made with restructuring in the first six months of 2014 is outlined below.

Wind-down measures within the restructuring process

In the first half of 2014, loans within a real estate portfolio totalling around euro 400 million were sold and repaid early as part of the VBAG restructuring process.

Procedures for the sale of Investkredit International Bank plc, VB Leasing International Group and Volksbank Malta Ltd. were commenced in the 2013 business year. Contracts were signed in March 2014 for Investkredit International Bank plc and in April 2014 for Volksbank Malta Ltd. The sales of the aforementioned companies have not yet been closed. The contract on the sale of VB LEASING POLSKA S.A. and VB LEASING ROMANIA IFN S.A. was signed on 15 May 2014. Sales negotiations with potential buyers for other companies of the VB Leasing International Group are currently under way, but the sale of further subsidiaries depends both on the outcome of continued negotiations and on the agreement of the relevant local regulatory authorities. The aim is to complete all sales procedures in 2014. Due to existing uncertainties regarding the outcome of the sales negotiations, no reclassification according to IFRS 5 was carried out for VB Leasing's other subsidiary companies as at the reporting date.

An investment bank was engaged in April 2014 to support the sales process of Volksbank Romania S.A. According to the restructuring agreement of 26 April 2012, the sale of Volksbank Romania S.A. should be completed by 31 December 2015.

In the first half-year, the sale process was launched of a portfolio of non-performing loans with a nominal value of roughly euro 460 million, predominantly from the Real Estate segment. The transactions should be completed in the 2014 business year. Due to current unsecurity regarding the implementation as planned, no IFRS 5 reclassifications have been made.

Joint Risk Assessment and Decision (JRAD) and Internal Capital Adequacy Assessment Process (ICAAP)

In the second quarter of 2013 the Austrian National Bank carried out a comprehensive review under section 70 of the Austrian Banking Act regarding the implementation status of the Internal Capital Adequacy Assessment Process (ICAAP) at banking association level as per section 30a of the Austrian Banking Act. This on-site review also included a regulatory assessment of capital adequacy in the banking association as part of the Joint Risk Assessment and Decision (JRAD) process.

The review report by the Austrian National Bank revealed that the standardisation of the various ICAAP systems is still incomplete, while the risk management culture in the banking association is still weak and not yet sufficiently unified and centralised. The results of the review were used as an opportunity to launch an extensive project to process these findings. This will last the whole of 2014.

As part of the JRAD process that took place at the same time, the Financial Market Authority issued a decision in May 2014 stipulating an equity ratio of 13.6% for the banking association in accordance with section 30a of the Austrian Banking Act. The equity ratio was complied with for the first time as of 30 June 2014.

Asset Quality Review (AQR) and 2014 banking stress test

Since the European Central Bank (ECB) will also be taking on supervisory responsibilities for the Association of Volksbanks as part of the Single Supervisory Mechanism (SSM) as per section 30a of the Austrian Banking Act, a "Comprehensive Assessment" is being conducted at 128 institutions throughout Europe in preparation for SSM and to increase transparency regarding the recoverability of assets.

The Asset Quality Review forms part of this assessment: by examining the quality of assets. This provides an estimate of the adequacy of risk provisions recognised by the Association of Volksbanks as at 31 December 2013 – potentially requiring an increase in the equity ratio. Institutions must allow inspection of high-risk positions in accordance with standardised data definitions.

A team of representatives from the ECB, the Austrian National Bank and external experts examined processes, procedures and accounting practices at the Association of Volksbanks, analysed credit exposures and risk provisions, and measured collateral and real estate assets. These were accompanied by checks of data consistency, comparative portfolio analyses and an in-depth inspection of data and assumptions entered into models. The on-site audit, carried out from March to July 2014, included amongst other things a detailed credit file review based on a sample specified by the Austrian FMA and agreed upon procedures. The gathered data is currently being consolidated and subjected to quality assurance by the ECB.

In this context, the association structure presented a significant challenge that set the Association of Volksbanks apart from other banks being inspected as part of the AQR. The test sample covered all institutions in the association: primary Austrian banks, Volksbank Romania, VBAG itself and VBAG subsidiary companies in Austria and abroad.

In preparation for this, VBAG as the central organisation of the Association of Volksbanks, launched an association-wide project in the fourth quarter of 2013, which was taken forward in 2014 with the following key objectives in particular:

- Transforming ECB data definitions into internal banking association data requirements
- Preparing and producing a solution for adequate AQR data storage. This includes, inter alia, setting up a data room, checking data availability and data quality, preparing and supplying the portfolio indicators defined by the Austrian FMA in accordance with the portfolio template and preparing the supply of transactions identified as “high-risk portfolios” at individual transaction level as per the ECB “loan tape” data definition
- Preparation for credit evaluation by external advisors.

As the central organisation, VBAG’s aim with this project was to prepare the Association of Volksbanks for the supervisory process in the most efficient manner possible.

The results of the AQR and the stress test are not yet available. They should be available in early autumn, and will be published by the ECB in October.

Other events during the first half year of 2014

In November 2013, Sberbank of Russia filed a lawsuit against VBAG at the International Court of Arbitration in connection with the VBI sale. Negotiations resulted in the lawsuit being withdrawn at the International Court of Arbitration in April 2014.

With regard to the outstanding Alpine Group financing we would point out that the Republic of Austria is contesting among other things the proper fulfilment of the information obligations required of the finance provider, as set out in Austrian company liquidity law (ULSG), and that so far guarantee payments totalling euro 15 million for the ULSG financial facility provided by VBAG have not been made.

On 27 March 2014, ratings agency Moody’s downgraded VBAG’s issuer rating from Baa3 to Ba1. This means that VBAG’s senior unsecured bonds are rated below investment grade and are therefore outside the investment profile of some institutional investors. Consequently, some institutional investors sold their bond holdings. Private investors were also induced by the rating downgrade to sell VBAG bonds. Overall the sales were on a par with the repurchase programme for certain bonds announced by the bank in autumn 2013. Therefore, Moody’s rating downgrade had no significant negative impact on the Group’s liquidity.

Financial position and Group results for the first half year of 2014

VBAG’s result before taxes amounted to euro −190 million, while the result after taxes and non-controlling interests totalled euro −203 million.

Net interest income for the first half of 2014 totalled euro 104 million, euro 29 million less than the result in the previous period (1-6/2013: euro 133 million). This is primarily due to the winding down of interest-bearing assets and their refinancing as part of the restructuring process.

Risk provisions for the first half of 2014 totalled euro 24 million, a decrease of euro 3 million compared to the previous year’s figure of euro 27 million. This is largely attributable to the winding down of Non-core loans as part of the restructuring and to the lower need for write-downs as a result.

Net fee and commission income in the reporting period totalled euro 10 million, down by euro 9 million in comparison to the previous period (1-6/2013: euro 19 million). This is particularly driven by wind down measures in non-core areas.

Net trading income is up year-on-year (1-6/2013: euro −27 million). Net trading income stood at euro 5 million during the first half of 2014. The increase compared with the previous year is especially attributable to interest-related business connected with restructuring of hedges. This served to optimise hedge accounting which fed through to an improvement in net trading income.

General administrative expenses remained practically unchanged on the previous year at euro 127 million (1-6/2013: euro 126 million). The headcount declined by 43 compared to the end of 2013 and now totals 1,810 employees, 736 of whom are employed outside Austria.

The other operating result for the first half of 2014 amounted to euro −24 million (1-6/2013: euro 66 million). Significant components in the first six months of 2014 included the valuation of disposal groups in accordance with IFRS 5 totalling euro −35 million as well as a reimbursement of value added tax totalling euro 15 million from a now closed legal procedure. The asset guarantee provided by the Republic of Austria on 15 March 2013 was recognised in the previous year's reporting period at euro 65 million.

Income from financial investments totalled euro −7 million in the reporting period and is therefore euro 14 million higher than in the comparative period (1-6/2013: euro −21 million). The main reason for this is that the valuation of guarantees for capital-guaranteed funds fell by euro 20 million in the reporting period. Investment property in the first half of 2014 was valued at euro −6 million (1-6/2013: euro −18 million) while investments in real estate companies were carried at euro −5 million (1-6/2013: euro −5 million). The result from a sale of htm positions (euro 11 million, 1-6/2013 euro 1 million) had a counteracting effect.

The income from companies measured at equity during the first half of 2014 reflected charges of euro 128 million arising from the planned measures to strengthen the own funds of VB Romania S.A. The previous year's result includes the measurement arising from the euro 60 million capital increase in October 2013.

No deferred tax assets were recognised on the loss in VBAG in the first half of 2014 since they cannot be used over the next four years. Deferred tax income on differences derived from the valuation of derivatives and securities was recognised to the extent that deferred tax liabilities were incurred from other valuation differences.

Statement of financial position and own funds

As at 30 June 2014, total assets amounted to euro 18.8 billion, down by euro 2.1 billion compared with 31 December 2013 (euro 20.9 billion).

The cash reserve declined from euro 1.7 billion to euro 0.4 billion which is attributable to repurchases of own issues.

Loans and advances to credit institutions totalled euro 6.0 billion, rising by euro 0.2 billion compared to 31 December 2013 (euro 5.8 billion).

Loans and advances to customers amounted to euro 5.9 billion as at 30 June 2014, down by euro 1.2 billion compared with 31 December 2013 (euro 7.1 billion). Declines were registered mainly in the Non-core business segments. During the first half of 2014, loans totalling almost euro 1 billion were reclassified from loans and advances to customers to assets held for sale.

Sales and repayments reduced financial investments by euro 0.4 billion to euro 3.0 billion compared to the end of 2013 (euro 3.4 billion).

Assets held for sale include loans, shares, participations and financial investments where a sale has already been contractually agreed or is highly likely.

Amounts owed to credit institutions fell by euro 0.4 billion to euro 7.3 billion compared to the end of 2013 (euro 7.7 billion).

Amounts owed to customers stood at euro 1.9 billion, down by euro 0.2 billion compared to the end of 2013 (euro 2.1 billion). This is connected with the winding down of customer portfolios.

Debts evidenced by certificates amounted to euro 5.2 billion as at 30 June 2014, which represents a fall of euro 1.9 billion compared to 31 December 2013 (euro 7.1 billion). This reduction is largely attributable to scheduled repayments as well as early repayments.

Owing to the result for the first half of 2014, equity decreased compared with the end of the previous year and stands at euro 1.0 billion.

As a bank that is undergoing a substantial winding down of operations, strategic objectives are focused less on result and more on capital ratios and the strengthening of own funds. VB Holding Group's own funds amounted to euro 4.1 billion as at 30 June 2014. The total risk of the VB Holding Group was euro 26.5 billion as at 30 June 2014. The common equity Tier 1 capital ratio based on total risk was 11.2%, and the Tier 1 capital ratio was also 11.2%. The equity ratio amounted to 15.3%.

The return on equity (ROE) before taxes as at 30 June 2014 totalled –33.8% (31 December 2013: –5.3%), while ROE after taxes was –33.2% (31 December 2013: –7.4%). ROE before taxes is calculated by dividing result before taxes by average equity capital as at the reporting date and the previous year's reporting date, while ROE after taxes is calculated by dividing result after taxes by average equity capital as at the reporting date and previous year's reporting date.

The operating cost-income-ratio of VBAG Group in the reporting year totalled 106.1% (31 December 2013: 109.9%).

Report on the company's future development and risks

Future development of the company

Economic environment

The Austrian economy is set to grow by 1.4% this year, according to a forecast published in June by the Austrian Institute of Economic Research (WIFO). Although the International Monetary Fund downgraded its global economic growth forecast in July's update to its World Economic Outlook, it left its growth forecast in the euro zone unchanged at 1.1%. Since then, however, geopolitical risks have increased. Conflict in Ukraine is already placing pressure on trade relationships with Russia, and the situation in Iraq, as well as in the Gaza Strip and Israel, present risks to economic growth.

Given low inflationary risks and a weak growth outlook, the European Central Bank has stated that it will not increase its key interest rate for some considerable time. Longer-term interest rates, which have reached record lows in the euro zone, could begin to rise slightly due to the end of the Fed's bond-buying programme. High levels of geopolitical uncertainty and the weak economic situation, however, should prevent a sharp rise in yields.

Inflationary risks in Romania are also barely discernible. In August, this enabled the central bank to cut its key interest rate by a further 25 basis points to a new low of 3.25%, which should support growth prospects for the current year. The leu exchange rate, however, remains susceptible to changes in risk appetite due to geopolitical tensions.

Business development

The VBAG Group is undergoing a massive restructuring process. According to the requirements laid down by the European Commission, business areas and holdings that are not part of core business must be wound down or sold in accordance with their repayment profile in the medium term. This will continue to impact on earnings, not least because of the difficult economic climate and the resultant discounts for the Non-core portfolio. This means the Group is likely to make significant losses in 2014 as well.

Material risks and uncertainties

The Managing Board of VBAG has launched a range of measures over the past two years to strengthen VBAG's capital base at individual bank and Group level, and hence that of the Association of Volksbanks by virtue of VBAG's role as the central organisation of the Association of Volksbanks in accordance with the banking association agreement as per section 30a of the Austrian Banking Act (BWG). They include in particular:

- conversion or repurchase of supplementary, hybrid and subordinated capital, following approval from the regulator and the European Commission, with an effect on CET1,
- introduction of a 95% base amount for cooperative capital, which prevented its phasing out, and consequently secured CET1 of more than euro 110 million for the banking association,
- adjustments to the issue conditions of various Tier I and Tier II instruments in order to meet Basel III requirements, and consequently retain them as own funds of more than euro 100 million in the banking association,
- various RWA reduction measures,

- implementation of substantial wind-down measures that markedly improved VBAG's risk position (at individual bank and Group level), and thus indirectly that of the banking association, which is clearly reflected in the steady rise in the equity ratio,
- substantial improvement in the quality and effectiveness of risk management.

RWAs within the Group and the Association of Volksbanks were reduced further by cutting risks arising from the Non-core area on an ongoing basis. Total risk (risk-weighted amounts pursuant to CRR, to be applied from 1 January 2014) stood at euro 26.5 billion for the association as of 30 June 2014. As a result of the aforementioned measures, the Tier 1 capital ratio and the core capital ratio of the Association of Volksbanks amount to 11.2%. The equity ratio stands at 15.3%.

Following the FMA's JRAD decision issued in May 2014 for VBAG in its function as the central organisation for the Association of Volksbanks as per the association agreement pursuant to section 30a of the Austrian Banking Act (BWG), a 13.6% equity ratio was prescribed for the Association of Volksbanks on the basis of Basel III, which was to be complied with for the first time as of the 30 June 2014 reporting date.

This figure was decided on the basis of the lending portfolio and the risk regime as of the 31 December 2012 reporting date. It is impossible to gauge the extent to which the scheduled 2014 JRAD, based on the 30 June 2014 reporting date, will acknowledge the association's wind-down achievements – which are far ahead of schedule – and its handling of section 70 audit findings – which have largely been resolved – in terms of reducing the capital requirement in the coming years. It is also impossible to say at present how the results of the current AQR process and the subsequent stress test will affect the prescribed equity ratio for the banking association.

Based on current planning by VBAG and the Volksbanks, a banking association equity ratio of 13.6% can be expected by the end of 2014 in accordance with Basel III.

These forecasts, and consequently the fulfilment of these requirements, could be jeopardised if potential charges arising from the AQR/stress test or winding-down of VBAG's Non-core portfolio, for example, prove higher than expected, although such a scenario is not anticipated at present.

However, the current medium-term forecast anticipates a marked decline in equity ratios within the banking association from 2015 onwards. This is primarily due to equity reductions resulting from:
- agreements with the Republic of Austria and the European Commission (government participation capital of euro 300 million no longer eligible, non-controlling interest and capital differences of almost euro 500 million no longer eligible following the sale of VBLI and VB Romania in 2014 and 2015),
- various Basel 3 effects (phasing out of members' uncalled liabilities [Haftsummenzuschlag] totalling more than euro 300 million, and of private participation capital within the banking association totalling euro 180 million),
- foreseeable charges arising from the continued wind-down of VBAG's Non-core portfolio.

Current forecasts indicate a shortfall in equity funding in the banking association in 2017 on the basis of the 13.6% equity ratio based on the JRAD decision. As far as the Managing Board can see, regulatory authorities in Europe currently vary in their approach to the legal status of an SREP ratio under a JRAD process. Hence it is currently difficult to predict the extent of measures and sanctions which would be required or imposed by the regulatory authorities in the event of non-compliance.

As a precaution, a number of further initiatives have already been set in motion. Various programmes introduced in the past to relieve the burden of RWAs within the banking association have already reduced these at primary banks. VBAG's Managing Board believes that these initiatives should also be continued over the next two years to achieve a decrease in RWAs that exceeds the level currently planned. A feasibility study has been commissioned to determine whether switching to the IRB approach could result in a significant fall in RWAs. Other opportunities and requirements are also being assessed with a view to issuing new Basel III-compliant bonds (even though the ability to issue bonds seems limited at present). Finally, discussions will be held with shareholders and owners of participation capital regarding measures to optimise further the existing capital structure.

Following the government support provided in 2012, the European Commission and the Republic of Austria required VBAG to undertake an ambitious downsizing programme. This wind-down programme is legally binding on VBAG and is to be implemented by VBAG's governing bodies. As a result, the winding-down, in particular the associated compulsory sale of equity investments within the narrow timeframe prescribed by the European Commission, cannot be halted, even to prevent the loss of non-controlling interests.

A comprehensive strategy project was launched for the Association of Volksbanks in 2013 to improve its current medium-term planning. The aim is to leverage all earning potentials and cost synergies within the banking association in the short to medium term. Under the Managing Board's current plans, 55 Volksbanks and specialist institutions are to be merged into nine provincial Volksbanks and three specialist institutions. Based on harmonised structures and workflows, with their regional focus and market dominance, these Volksbanks should benefit from a group-like divisional structure. This programme is expected to make an additional and significant contribution to earnings by 2018. These extra earnings will however be offset by implementation costs, particularly in the years 2014-2016.

In the long run, these measures are expected to improve the banking association's equity ratios. Whether the medium-term improvement this will bring about in the banking association's earning power will create a basis for attracting capital from outside depends on whether potential investors consider the new approach to be sustainable.

Conversely it is possible, though unlikely on a present view, that the costs of the ongoing wind-down of the Non-core portfolio may turn out higher than anticipated in the medium-term planning, thereby countering any positive effects.

Following the JRAD assessment, the regulatory authorities raised the equity ratio for the Association of Volksbanks well above the statutory minimum capital requirements and also the capital requirements adopted for the purposes of state aid legislation – at least in the short term. It will be possible to comply with this equity ratio for the time being. Over the medium term, however, it will only be possible to adhere to the equity ratio of 13.6% imposed on the Association of Volksbanks as part of the scheduled JRAD process, which not only exceeds statutory minimum capital requirement but is also higher than the capital requirements adopted for the purposes of state aid legislation, if:

- sufficient opportunities and satisfactory conditions can be created to improve the association's ability to issue bonds, and/or
- the equity ratio that was increased very sharply and at short notice as part of the scheduled JRAD process can be reduced again in acknowledgement of the wind-down measures that have been successfully implemented in line with the requirements set out in the European Commission's decision on state aid rules, and/or
- suitable measures can be implemented in order to optimise VBAG's existing equity structure, or increase equity on the part of the owners.

Based on requirements set out in the restructuring agreement with the Republic of Austria dated 26 April 2012 and the European Commission's decision of 19 September 2012 based upon this, VBAG is required to dispose of key business areas and holdings in Austria and abroad over the coming years.

Previous experience in Austria and abroad has shown that these wind-down processes often involve higher costs than were previously foreseeable. VBAG's Non-core segment is also exposed to this uncertainty.

VBAG has a substantial real estate portfolio in Austria, and Central and Eastern Europe. In addition to credit risks, valuation haircuts may also be imposed as a result of spread risks when selling parts of this portfolio.

VBAG holds a 51% interest in Volksbank Romania S.A. (the company is measured at equity in the consolidated financial statements due to its being controlled jointly with non-Group third parties). Volksbank Romania S.A. plans various measures in 2014 in connection with this restructuring of its lending portfolio and the continuing build-up of primary deposits. In the equity planning, this results in a significantly higher equity requirement. The measures planned to strengthen the equity of VB Romania S.A. in the second half of 2014 resulted in a charge to earnings of euro 128 million as of 30 June 2014 arising from at equity accounted participating interests within the VBAG Group.

As at 30 June 2014, refinancing of euro 0.6 billion (31 December 2013: euro 0.8 billion) provided by VBAG to VB Romania was still outstanding. VBAG currently assumes, based on the measures planned under the sales process and the expected build-up of primary deposits at VB Romania, that repayments will be made on schedule. However, it is conceivable – though currently unlikely – that the difficult and volatile macroeconomic environment could give rise to stress scenarios that might impact the carrying amount of refinancing provided by VBAG to Volksbank Romania S.A.

The risk profile will also become clearer once Volksbank Romania's forecasts for the years 2015 and beyond have been presented, and a better estimate is available for the market environment in relation to the sale of Volksbank Romania S.A., which is to be concluded by 31 December 2015 at the latest.

The continuing economic malaise, particularly in the banking sector, poses a risk of lower incomes and distributions from equity participations. This may lead to lower market values in the future.

Regulators at European and national level are demanding that institutions comply, both now and in the future, with ever more extensive requirements. This constitutes a huge drain on Group resources in terms of personnel, as well as project and IT costs, but also has an impact due to potentially higher capital requirements that far exceed the minimum regulatory requirement under Basel II and Basel III. In this context, please refer to the detailed information provided in connection with the joint risk assessment and decision (JRAD), the asset quality review (AQR) and the 2014 bank stress test.

If capital regulations were to be infringed due to additional risk provisioning arising from the AQR or the stress test basis scenario, such infringements would need to be remedied within six months. If shortfalls in capital were to be identified on the basis of adverse stress tests, such shortfalls would need to be covered within nine months. When implementing recapitalisation measures to cover capital shortfalls, capital instruments of the highest quality are to be utilised to the extent that the shortfalls cannot be reduced with other funding sources. The results of the AQR and the stress test are not yet available. It is currently difficult to predict the scope of measures and sanctions that the regulatory authorities might apply in the event of non-compliance.

Entirely independently of the AQR and the stress test, reference has been made in the last two years to a further requirement for capital that might arise as a result of the necessary winding-down of business areas and participating interests. In particular, in order to avoid further charges, an extensive strategy project was launched across the banking association in summer 2013 with the ultimate objective of improving its Internal financing power and the access to the capital markets.

Moody's issued new rating information in early August, downgrading VBAG by two notches from Ba1 to Ba3. This downgrade reflects Moody's belief that the Republic of Austria is now less prepared to support VBAG, and banks in general. At the same time, Moody's confirmed VBAG's Standalone Bank Financial Strength Rating. Moody's acknowledges the "substantial progress" made in the winding-down of the non-core portfolio.

As in March, Moody's rating downgrade had no significant negative effects on the Group's liquidity situation.

Shortly after Moody's announcement, Fitch also published new rating information relating to the Association of Volksbanks and VBAG, in which express reference is also made to the progress achieved in winding down VBAG's non-core portfolio both last year and this year. In contrast to Moody's, Fitch confirmed its A rating for the association, for all association banks and for VBAG. This signifies "safe investment, unless unforeseen events should occur". The outlook at Fitch remains "negative" – both for the association and VBAG. Fitch justifies confirmation of its A rating by referring to the fact that the Association of Volksbanks commands a significant market share of 7%. Hence it is regarded as systemically relevant by the Austrian authorities, as the Volksbank network covers rural areas where few alternatives exist.

Fitch now justifies the confirmation of its "negative outlook" by referring to the fact that "a clear intention exists in the EU to reduce state support for banks. This is demonstrated by a number of statutory, regulatory and political initiatives. Given also the ad hoc legislation for Hypo Alpe Adria, it is further expected that the Republic of Austria's willingness to support VBAG, and banks in general, will diminish." Unless this changes by the next credit review, it must be anticipated that Fitch will reduce the support uplift in the medium term (rating improvement through potential state support), which would negatively affect the rating for the Association of Volksbanks. The potential extent of such a reduction is currently unclear.

FINANCING SEGMENT

The Financing segment comprises the business areas Commercial Business – Syndicate Services and Structured Financing (focusing on subsidies and export finance), as well as VB Leasing Finanzierungsgesellschaft m.b.H. and VB Factoring Bank AG.

The Financing segment is responsible for supporting the regional Volksbanks in the management of existing customer relationships and for providing advice and support in relation to new business opportunities.

Segment results

The result before taxes for the Financing segment amounted to euro −4 million, less than in the comparable period. This was mainly the result of an increase in general administrative expenses, reflecting higher costs passed on. Net interest income increased slightly, while risk provisions were stable.

Commercial Banking

A new business unit was added to the Commercial Banking area in spring 2014, which now includes the “Active Credit Management (ACM)” department in addition to the “Syndicate Services (CRM Customer Relationship Management)” and “Structured Financing” departments.

ACM

The Active Credit Management department is a traditional mid-office unit and is responsible for activities relating to ongoing credit management to relieve some of the pressure on Syndicate Services, as well as for data and system maintenance tasks. It also supervises specially defined customer segments based on risk and return considerations with the aim of optimising resources.

Syndicate Services

The core task of the Syndicate Services department is to make the existing portfolio held on a syndicate basis with the Volksbanks profitable – in particular, by optimising RWAs and leveraging earnings potential. Furthermore, the department’s declared aim is to win select new clients in the SME segment together with local Volksbanks. By providing needs-based services and advice, the Syndicate Services department helps to improve the risk/return profile for the Association of Volksbanks in this customer segment.

In the first six months of the year, Syndicate Services recorded a modest decline in loan portfolios owing to unscheduled repayments (especially for long-term loans). While interest margins stagnated, increases in interest-like income (primarily processing and commitment commissions) contributed to the improved result.

Structured Financing

Subsidies and export finance are among the Volksbank sector’s core products. These products support Austrian SMEs in their growth and reduce credit risk via public-sector guarantees, and therefore RWAs (risk weighted assets) too that must be backed with equity. Project-based, long-term refinancing is also provided via funding agencies.

Development of selected product groups

At the end of the first half-year, the total volume of European Recovery Programme (ERP) loans fell from around euro 156 million (as at 31 December 2013) to approximately euro 145 million. This year-on-year decline is due to the focus on Volksbanks’ small and medium-sized customers who generally apply for low volumes of credit, while large customers are no longer a strategic target group for the Association of Volksbanks because VBAG no longer has any own business. However, the number of loans continued to rise significantly, despite large scheduled and unscheduled repayments in the Non-core Business segment, increasing from 490 (end of 2013) to 514 ERP loans (including 398 small ERP loans). In the first six months of the year, a total of 48 ERP loans (including 40 small ERP loans) with a volume of around euro 8 million were added in part or in full.

The Volksbank Group ranked sixth in the first half-year as regards approvals for small ERP loans (excluding ÖHT loans), once again making it one of the top performers out of the 25 ERP trustee banks.

Exposure to OeKB short-term financing together with the Kontrollbank refinancing facility rose slightly to around euro 16.9 million.

The volume of financing for SME customers in the Volksbank sector under the Austrian export fund was around euro 38million across 125 loans at the end of the first six months of 2014, slightly lower than the 2013 figure.

The volume of OeKB long-term financing for corporate customers as at 30 June 2014 fell from around euro 185 million (35 loans) at the end of 2013 to euro 130 million (27 loans) as planned, since a large number of these loans are attributable to the bank's Non-core Business and were wound down further in the past year.

Soft loan exposure remained unchanged compared to 2013 at approximately euro 54 million, aside from scheduled repayments.

In the case of trade finance, the bank primarily concentrates on documentary business, involving letters of credit and guarantees for the Volksbank sector's customers.

VB Leasing Finanzierungsgesellschaft m.b.H. (VBLF)

VB Leasing Finanzierungsgesellschaft's result for the first half of 2014 was pleasing. Despite the continued increase in refinancing costs, it came in slightly above the previous year's result. The volume of new business stood at approximately euro 162 million in the reporting period, which equates to more than 8,900 contracts. VB Leasing is currently ranked fifth among Austria's moveable goods/vehicle leasing providers.

VB Factoring Bank AG

At the end of the first half of the year, the factoring volume was down 1% on the comparable period of the previous year at euro 731.7 million, but was 12% higher than expected on account of sales growth for existing customers.

Outlook for the Financing segment

We expect syndicate credit volumes to move sideways in the second half of the year, but we believe that intensive collaboration with Volksbanks in the area of SMEs could yield significant potential both in terms of existing customers and attracting new customers. We will continue to hold joint working groups with regional Volksbanks in order to discuss this issue in the second half of the year.

We anticipate continued growth in the second half of 2014, particularly for small ERP loans and other subsidies for SMEs. Large-volume export finance from Non-core Business will continue to decline as planned up to the end of the year. The winding down of Non-core Business will bring the volumes of subsidised financing and export finance down to a level where subsidised SME finance can start to be built up once again in accordance with the needs of the target group by no later than 2015. One key priority in this regard will be workshops scheduled to take place in the second half of the year, with the aim of working with Austrian SMEs to deliver the resultant benefits during the new funding period.

VB Leasing Finanzierungsgesellschaft m.b.H. will continue to pursue its systematic risk policy in terms of creditworthiness, asset security and risk diversification, with a particular focus on ensuring a risk-adequate pricing policy.

Several large-scale factoring commitments are coming to an end, meaning that the business volume for 2014 as a whole is expected to contract.

FINANCIAL MARKETS SEGMENT

The Financial Markets segment is the competence centre for all financial market services. Its mission is to serve, advise and support association banks and VBAG's institutional customers. The key areas of the Financial Markets segment are Financial Markets & Group Treasury and Capital Markets Products & Sales.

Segment results

The result before taxes as of 30 June 2014 was euro –9 million in the Financial Markets segment. The increase in the net trading income on the comparable period is related to the restructuring of hedging transactions. Income from financial investments also improved compared to the first half of the previous year when a valuation result of euro –22 million for guarantees of capital-guaranteed funds was reported.

Financial Markets & Group Treasury

Financial Markets Execution

Alongside the customer-induced management of the trading book, key projects were driven forward in the first half of 2014, for example derivative volumes were reduced by means of netting transactions. Other work focused on ensuring optimal implementation of hedge accounting requirements along with the related restructuring of interest rate derivatives, or on expanding the Murex front-office system. Furthermore, cross-divisional projects were supported – such as the implementation of the European Market Infrastructure Regulation (EMIR) and associated reporting and clearing obligations.

In the first half year total transaction numbers and volumes in order management were up on the comparable period as a result of an increase in existing customer's transaction volumes. Products in demand still comprised fixed-income, step-up and MinMax bonds from various issuers, also including housing finance providers. In the area of funds, the focus was on real estate funds, equity funds with dividend-bearing stocks and sustainable mixed funds.

ALM Liquidity Management

In the first half of 2014, Liquidity Management focused on revising existing rules and procedures for the Association. VBAG's liquidity buffer was as expected, and totalled roughly euro 4 billion as at 30 June 2014, taking the cash reserve into account. The downgrade of VBAG's senior unsecured rating from Baa3 to Ba1 by rating agency Moody's at the end of March 2014 had no notable impact on liquidity at VBAG or the Association of Volksbanks.

ALM Investment Book

Work continued in the first half of 2014 on bringing the investment book into line with regulatory requirements governing the liquidity coverage ratio which will take effect from 2015. To this end, top-quality bonds were acquired on the primary market in the segments of covered bonds, supranational issuers and state-guaranteed companies. In terms of managing the Association of Volksbanks, governance in the areas of liquidity, interest rate book management and bank book investments was further improved by establishing an Association Asset-Liability Committee and an Association Investment Committee. Further measures were taken to optimise the balance sheet structure as part of interest rate book management, the focus here was on implementing asset-liability strategies which aim at positive contributions from the interest rate book.

Banks & Credit Markets

The winding down of unsecured bank and company risk positions while taking risk/return aspects into consideration and preserving equity continued in the first half year, with the positive development of spreads throughout the market helping sales efforts. Additionally, an investment universe comprising roughly 50 companies and banks (around 160 bond issues) was established for the own investments of local Volksbanks. Selections were made after in-depth individual checks in consultation with Operational Risk Control.

Capital Markets Products & Sales

Assets under management

Investment markets were again affected in the first half of 2014 by low interest rates and geopolitical uncertainties. As in the previous period, Capital Markets Products & Sales focused on investment products that have a strong safety bias but also ensure that investments are as attractive as possible, despite the challenging interest rate climate.

The volume of assets under management in terms of products contained under the "Volksbank Investments" brand (funds, certificates, wealth management and foreign assets) fell slightly to just over euro 6 billion as at 30 June 2014 (2013 year-end: euro 6.2 billion). Certificate volumes continued to decline while the development of funds was stable on the whole and wealth management mandates improved markedly.

Funds

The volume of Capital Markets Products & Sales funds increased modestly compared to the end of 2013, totalling roughly euro 2.9 billion as at 30 June 2014. In line with the overall market trend, special funds gained a significant 8%. Retail funds also performed in line with the market. A slight contraction was registered for mixed funds on the whole, but both of the classic pension products VB Rent and VB Mündel-Rent performed extremely well.

With a net volume gain of euro 93.7 million, immofonds 1 also developed positively in the first half of 2014. The total volume of immofonds 1 as at 30 June 2014 was euro 382.9 million.

Certificates and bonds

The market volume (open interest) of certificates issued by the five members of Zertifikate Forum Austria fell from euro 5.2 billion at year-end 2013 to euro 5.1 billion as at 30 June 2014. Volksbank Investments' certificates also contracted; as at 30 June 2014 the Volksbank Investments' open interest amounted to roughly euro 1.1 billion (31 December 2013: approximately euro 1.4 billion). Its share of the certificate market is about 21.1%, and just under 26% in the case of guarantee certificates.

A pool of third-party issuers ("Emittentenplattform") which provides the possibility of diversification in the area of certificates is also available for investors, in addition to VBAG a number of reputed international issuers are offered.

Bonds with a volume of euro 122 million were sold in the first half of 2014. Demand was particularly high for step-up bonds.

Wealth management

The volume of wealth management mandates rose by 5.6% in the first half of 2014 to just under euro 2 billion as at 30 June 2014. Based on Volksbank Investments' long-standing expertise in institutional wealth management, efforts were stepped up to acquire new customers in cooperation with the regional Volksbanks.

Outlook for the Financial Markets segment

Currently two primary banks remain that are not yet being fully serviced by VBAG regarding securities. The Financial Markets & Group Treasury division will focus on the switch of those two banks to full service status in the second half of the year. As a result, the entire securities business of every Volksbank including trading, order routing and settlement will be handled by VBAG and VB Services by the end of 2014. Moreover, in the area of third-party funds it is planned to optimise trading and settlement so as to leverage the income and cost optimisation potential of full servicing within the Association.

In view of current interest rate levels and the investor risk aversion resulting from geopolitical uncertainties, Capital Markets Products & Sales will concentrate on the issuance of fixed-term funds in the second half of the year, while also focusing on immofonds 1. The pool of third-party issuers was well received by the market and will continue to play a key role in terms of diversification possibilities. Additionally, the themes of pensions and fund saving will be in the spotlight, and should be of interest to investors not least because of the pension account newly established in Austria.

NON-CORE BUSINESS SEGMENT

Non-core Business is subdivided into four segments:
- Non-core Corporates segment
- Non-core Real Estate segment
- Non-core Retail segment
- Non-core Investment Book/Other operations segment

Non-core Corporates segment

This segment covers Corporate Customers, International Project Finance, Renewable Energy, and a portfolio in the Private Equity – Fund Investments business area. The portfolios are concentrated primarily on Austria and Western Europe.

In line with the strategy and objective of winding down the Non-core segments in a structured manner the segment's total assets declined by 40%.

Segment results

In the Non-core Corporates segment, the result before taxes was euro −26 million. This result primarily reflects higher risk provisions and a fall in net interest income due to reduction of the portfolio.

Corporate Customers

In the Corporate Customers segment, around 10 transactions were repaid early, amounting to approximately euro 37 million. These included the winding down of a commitment from the Renewable Energy business area totalling approximately euro 18 million.

Private Equity – Fund Investments

Further measures were taken in the Private Equity business area to reduce volumes and free up capital in the first half of 2014. This included the sale of another sub-portfolio as part of a structured sales process. The transaction involving the rest of the portfolio is expected to be completed in the second half of 2014.

Non-core Real Estate segment

This segment covers commercial real estate project financing, associated work-out activities, own property asset management operations and VB Real Estate Services GmbH's real estate lease financing. The portfolios are concentrated primarily on Austria, CEE and SEE.

The winding down of the Non-core Real Estate segment in a structured manner could be continued in the first half year with 24 transactions in the amount of euro 650 million. The segment's total assets declined by euro 700 million, risk weighted assets by more than 30%.

Segment results

The result before taxes in the Non-Core Real Estate segment amounts to euro −25 million. This further decline compared to the prior-year comparable period is mainly attributable to a fall in net interest income, reflecting the winding down of the non-core portfolio that has already been implemented. The previous year's result for discontinued operations includes the purchase price adjustment agreed for the sale of Selini GmbH.

Real estate loan financing and work-out

Loans totalling around euro 598 million were redeemed early in the first half of 2014 thanks to active wind-down activities. This resulted in a reduction in RWAs of around euro 527 million. These wind-down projects included the sale of a loan portfolio concentrated on Austria, Romania and Poland with a total volume of approximately euro 408 million and a Bulgarian loan of around euro 55 million. Four loan commitments were also successfully wound down in the work-out department.

Real estate leasing and asset management

In addition to natural maturities, the real estate lease portfolio was reduced by around euro 35 million on the basis of 10 transactions, which corresponds to a reduction in RWAs of approximately euro 9 million. This includes the transfer of a Polish events hall to the current operator with a volume of approximately euro 12 million. A smaller Austrian project in the Group's real estate holdings and a non-controlling interest in a Czech real estate company were also sold in the second quarter of 2014. Several assets were held for sale; that's why in the second half of the year further significant volume reductions can be expected in this segment.

Non-core Retail segment

The Non-core Retail segment encompasses VB-Leasing International Group's moveable goods leasing operations in Central and Eastern Europe, as well as Volksbank Romania S.A.'s business activities.

Segment results

The result before taxes of euro −105 million primarily reflects a euro −128 million charge for the planned measures to strengthen VB Romania S.A's own funds. In the previous year, the income from companies measured at equity included a write-down of euro 60 million applied to the capital increase at VB Romania. The result of euro −14 million from the measurement of assets held for sale is offset by euro 15 million compensation of VAT arising from litigation that has now been concluded. Both items are included in the other operating result.

VB-Leasing International Holding GmbH (VBLI)

VB-Leasing International reported new business of euro 540.7 million in the reporting period, which represents a moderate increase compared to the first half of 2013. Apart from Bosnia-Herzegovina, which registered a slight decline, all of the other seven VBLI countries recorded growth. Some 19,700 new contracts were concluded overall.

The national offices in Poland and Romania were sold to Getin Holding S.A. based in Poland in the first half of 2014. These transactions are expected be completed by the end of the year at the latest, provided the local authorities submit their approval. The sales process launched in 2013 will continue for the VB Leasing Group's six remaining national offices.

Volksbank Romania S.A. (VB RO)

The restructuring process is well underway and the results of the transformation measures are in line with expectations. As of 30 June 2014, the Loan/Deposit ratio of the bank dropped to 240 % from 253 % in December 2013. The ongoing replacement of shareholder funding through locally originated deposits is a building block of the new business strategy and going according to plan. Overall the operational business targets are fulfilled according to budget. However, upcoming extraordinary events like the AQR and the sales process might impact the financial figures of the bank.

At 30 June 2014, the bank's capital ratio stood at 18.4 % which is considerably above the minimum required value of 10 % as well as the banking system's average level of 15 %.

Noteworthy is the sale of a non-performing loans portfolio (NPLs) in an aggregate volume of euro 498 million which has been finalized at the end of July 2014. With this transaction, Volksbank Romania has reduced its NPL ratio to a comfortable level of below 8 %, well below the average of Romania's banking system.

Non-core Investment Book/Other Operations segment

This segment includes all parts of the investment book which are to be wound down or sold in accordance with their repayment profile. VB Malta Ltd and holding companies with participations in the Non-core area were also assigned to the Non-core Investment Book/Other Operations segment.

Segment results

The result before taxes in this segment was euro −19 million. The result was burdened mainly by the measurement as per IFRS 5 of assets held for sale in an amount of euro −20 million. The positive result in the previous year reflects the first-time reporting of the asset guarantee issued by the Republic of Austria.

Outlook for the Non-core Business segment

The winding down the Non-core corporates segment and in the Non-core real estate segment will be continued in a structured manner.

The sales process launched in 2013 will continue for the VB Leasing Group's six remaining national offices.

An investment bank was engaged in April 2014 to support the sales process of Volksbank Romania S.A. According to the restructuring agreement of 26 April 2012, the sale of Volksbank Romania S.A. should be completed by 31 December 2015.

In the first half-year, the sale process was launched of a portfolio of non-performing loans with a nominal value of roughly euro 460 million, predominantly from the Real Estate segment. The transactions should be completed in the 2014 business year.

Condensed Statement of Comprehensive Income - 1 January to 30 June 2014

Income Statement

	1-6/2014 Euro thousand	restated 1-6/2013 Euro thousand	Changes Euro thousand	%
Interest receivable and similar income	296,195	404,028	–107,833	–26.69%
Interest payable and similar expense	–191,984	–271,304	79,319	–29.24%
Net interest income	104,211	132,725	–28,514	–21.48%
Risk provisions	–23,638	–27,349	3,710	–13.57%
Fee and commission income	32,588	37,239	–4,652	–12.49%
Fee and commission expenses	–22,282	–18,377	–3,905	21.25%
Net fee and commission income	10,306	18,862	–8,556	–45.36%
Net trading income	4,758	–26,755	31,513	–117.79%
General administrative expenses	–126,579	–126,209	–370	0.29%
Other operating result	–23,774	65,952	–89,726	–136.05%
Income from financial investments	–7,030	–21,212	14,182	–66.86%
Income from companies measured at equity	–127,934	–59,900	–68,034	113.58%
Income from discontinued operation	0	15,308	–15,308	–100.00%
Result for the period before taxes	**–189,680**	**–28,577**	**–161,103**	**>200.00%**
Income taxes	3,851	–27,186	31,037	–114.17%
Result for the period after taxes	**–185,828**	**–55,762**	**–130,066**	**>200.00%**
Result attributable to shareholders of the parent company (Consolidated net result)	**–203,013**	**–68,308**	**–134,705**	**197.20%**
thereof from continued operation	–203,013	–83,616	–119,397	142.79%
thereof from discontinued operation	0	15,308	–15,308	–100.00%
Result attributable to non-controlling interest	17,185	12,545	4,639	36.98%
thereof from continued operation	17,185	12,545	4,639	36.98%
thereof from discontinued operation	0	0	0	0.00%

Comprehensive income	1-6/2014 Euro thousand	restated 1-6/2013 Euro thousand	Changes Euro thousand	%
Result for the period after taxes	**–185,828**	**–55,762**	**–130,066**	**>200.00%**
Other comprehensive income				
Items that will not be reclassified to result				
Revaluation obligation of defined benefit plans (IAS 19)	0	–9,526	9,526	–100.00%
Deferred taxes of revaluation IAS 19	0	2,381	–2,381	–100.00%
Total items that will not be reclassified to result	**0**	**–7,144**	**7,144**	**–100.00%**
Items that may be reclassified to result				
Currency reserve	670	–6,384	7,054	–110.49%
Available for sale reserve (including deferred taxes)				
Change in fair value	20,529	83,618	–63,089	–75.45%
Net amount transferred to profit or loss	–3,290	–8,641	5,351	–61.92%
Hedging reserve (including deferred taxes)				
Change in fair value (effective hedge)	–522	–1,435	913	–63.62%
Net amount transferred to profit or loss	306	583	–277	–47.46%
Change in deferred taxes of untaxed reserves	818	20	798	200.00%
Change from companies measured at equity	–12,597	0	–12,597	100.00%
Total items that may be reclassified to result	**5,914**	**67,761**	**–61,847**	**–91.27%**
Other comprehensive income total	**5,914**	**60,616**	**–54,702**	**–90.24%**
Comprehensive income	**–179,914**	**4,854**	**–184,768**	**<–200.00%**
Comprehensive income attributable to shareholders of the parent company	**–197,443**	**–4,833**	**–192,609**	**>200.00%**
thereof from continued operation	–197,443	–20,141	–177,301	>200.00%
thereof from discontinued operation	0	15,308	–15,308	–100.00%
Comprehensive income attributable to non-controlling interest	17,529	9,687	7,841	80.94%
thereof from continued operation	17,529	9,687	7,841	80.94%
thereof from discontinued operation	0	0	0	0.00%

Condensed Statement of Financial Position

	30 Jun 2014 Euro thousand	31 Dec 2013 Euro thousand	Changes Euro thousand	%
Assets				
Liquid funds	446,773	1,762,453	–1,315,679	–74.65%
Loans and advances to credit institutions (gross)	5,981,989	5,798,139	183,850	3.17%
Loans and advances to customers (gross)	5,904,923	7,081,347	–1,176,424	–16.61%
Risk provisions (–)	–609,925	–773,009	163,084	–21.10%
Trading assets	1,563,509	1,627,392	–63,883	–3.93%
Financial investments	2,979,661	3,422,739	–443,078	–12.95%
Investment property	186,170	252,410	–66,240	–26.24%
Companies measured at equity	49,095	5,626	43,470	>200.00%
Participations	366,192	359,531	6,661	1.85%
Intangible assets	12,063	13,672	–1,609	–11.77%
Tangible fixed assets	116,018	131,503	–15,484	–11.78%
Tax assets	51,574	52,905	–1,331	–2.52%
Current taxes	31,338	19,974	11,365	56.90%
Deferred taxes	20,236	32,932	–12,696	–38.55%
Other assets	661,335	614,744	46,591	7.58%
Assets held for sale	1,072,230	554,657	517,573	93.31%
TOTAL ASSETS	**18,781,608**	**20,904,109**	**–2,122,500**	**–10.15%**

	30 Jun 2014 Euro thousand	31 Dec 2013 Euro thousand	Changes Euro thousand	%
Liabilities and Equity				
Amounts owed to credit institutions	7,344,215	7,707,002	–362,788	–4.71%
Amounts owed to customers	1,935,544	2,148,440	–212,896	–9.91%
Debts evidenced by certificates	5,202,456	7,084,825	–1,882,368	–26.57%
Trading liabilities	1,420,686	1,377,709	42,977	3.12%
Provisions	162,476	188,703	–26,228	–13.90%
Tax liabilities	54,008	66,511	–12,504	–18.80%
Current taxes	7,748	14,112	–6,364	–45.10%
Deferred taxes	46,260	52,399	–6,140	–11.72%
Other liabilities	675,887	554,549	121,338	21.88%
Liabilities held for sale	426,501	0	426,501	100.00%
Subordinated liabilities	537,320	554,957	–17,637	–3.18%
Equity	1,022,516	1,221,412	–198,444	–16.28%
Shareholders' equity	870,110	1,067,553	–197,444	–18.49%
Non-controlling interest	152,407	153,859	–1,452	–0.94%
TOTAL LIABILITIES AND EQUITY	**18,781,608**	**20,904,109**	**–2,122,500**	**–10.15%**

Condensed Changes in the Group's Equity

Euro thousand	Subscribed capital [1]	Capital reserve	Retained earnings	Currency reserve	IAS 39 [2] valuation reserves: Available for sale reserve	Hedging reserve	Shareholders' equity	Non-controlling interest	Equity
As at 1 Jan 2013	**885,632**	**0**	**206,754**	**7,209**	**–1,327**	**735**	**1,099,003**	**193,675**	**1,292,677**
Consolidated net income [3]			–68,308				–68,308	12,545	–55,762
Change in deferred taxes arising from untaxed reserve			20				20		20
Revaluation obligation of defined benefit plans (IAS 19 including deferred taxes)			–7,144				–7,144		–7,144
Currency reserve				–3,293			–3,293	–3,091	–6,384
Available for sale reserve (including deferred taxes)					74,977		74,977		74,977
Hedging reserve (including deferred taxes)						–1,084	–1,084	233	–852
Change from companies measured at equity				–66	431	–365	0		0
Comprehensive income	0	0	–75,432	–3,359	75,408	–1,450	–4,833	9,687	4,854
Dividends paid							0	–4,957	–4,957
Change due to reclassifications shown under non-controlling interest and deconsolidation			2,408		2,198		4,606	–5,653	–1,047
As at 30 Jun 2013	**885,632**	**0**	**133,730**	**3,849**	**76,279**	**–715**	**1,098,775**	**192,752**	**1,291,527**
As at 1 Jan 2014	**885,632**	**0**	**109,511**	**221**	**69,333**	**2,856**	**1,067,553**	**153,859**	**1,221,412**
Consolidated net income [3]			–203,013				–203,013	17,185	–185,828
Change in deferred taxes arising from untaxed reserve			818				818		818
Currency reserve				227			227	443	670
Available for sale reserve (including deferred taxes)					17,238		17,238		17,238
Hedging reserve (including deferred taxes)						–117	–117	–99	–216
Change from companies measured at equity				–4,049	697	–9,245	–12,597		–12,957
Comprehensive income	0	0	–202,194	–3,822	17,935	–9,362	–197,443	17,529	–179,914
Dividends paid							0	–1,140	–1,140
Change due to reclassifications shown under non-controlling interest and deconsolidation			–1				–1	–17,841	–17,842
As at 30 Jun 2014	**885,632**	**0**	**–92,684**	**–3,601**	**87,269**	**–6,506**	**870,110**	**152,407**	**1,022,516**

[1] Subscribed capital corresponds to the figures reported in the financial statements of Österreichische Volksbanken-Aktiengesellschaft.
[2] As at 30 June 2014, the available for sale reserve included deferred taxes of euro –18,394 thousand (30 June 2013: euro –14,125 thousand). The hedging reserve contains deferred taxes in the amount of euro 119 thousand at the balance sheet date (30 June 2013: euro 150 thousand).
[3] Currency translation differences amounting to euro 231 thousand (1-6/2013: euro –197 thousand) for shareholders' equity and euro 271 thousand (1-6/2013: euro –304 thousand) for non-controlling interest resulted from the application of average rates of exchange in the income statement.

Condensed Cash flow Statement

Euro thousand	1-6/2014	1-6/2013
Cash and cash equivalents at the end of the previous period (= liquid funds)	**1,762,453**	**851,262**
Cash flow from operating activities	**–1,563,777**	–460,978
Cash flow from investing activities	**288,989**	210,546
Cash flow from financing activities	**–40,501**	–12,803
Cash and cash equivalents at the end of period (= liquid funds)	**447,165**	**588,026**

Condensed Notes to the Financial Statements for the period from 1 January to 30 June 2014

1) General information and accounting principles

The interim report as at 30 June 2014 of Österreichische Volksbanken-Aktiengesellschaft (VBAG) has been prepared in accordance with all IFRS/IAS published by the International Accounting Standards Board (IASB) as well as all interpretations (IFRIC/SIC) issued by the International Financial Reporting Interpretations Committee and the Standing Interpretations Committee respectively as adopted for use in the European Union. These interim financial statements comply with IAS 34 Interim financial reporting.

The interim financial statements do not include all of the information required for full annual financial statements, and should be read in conjunction with the consolidated financial statements of the Group as at 31 December 2013. In preparing this interim report the accounting principles, the estimates and assumptions were the same as those applied to the consolidated financial statements as at 31 December 2013.

There were no events or changes in circumstances for the remaining goodwill that would indicate an impairment, therefore no impairment test was carried out.

These condensed consolidated interim financial statements were reviewed by the auditor.

The interim consolidated financial statements have been drawn up in euro as this is the Group's functional currency. All figures are indicated in thousands of euros, unless specified otherwise. The following tables may contain rounding differences.

a) Going concern

The Managing Board of VBAG has launched a range of measures over the past two years to strengthen VBAG's capital base at individual bank and Group level, and hence that of the Association of Volksbanks by virtue of VBAG's role as the central organisation of the Association of Volksbanks in accordance with the banking association agreement as per section 30a of the Austrian Banking Act (BWG). They include in particular:

- conversion or repurchase of supplementary, hybrid and subordinated capital, following approval from the regulator and the European Commission, with an effect on CET1,
- introduction of a 95% base amount for cooperative capital, which prevented its phasing out, and consequently secured CET1 of more than euro 110 million for the banking association,
- adjustments to the issue conditions of various Tier 1 and Tier 2 instruments in order to meet Basel III requirements, and consequently retain them as own funds of more than euro 100 million in the banking association,
- various RWA reduction measures,
- implementation of substantial wind-down measures that markedly improved VBAG's risk position (at individual bank and Group level), and thus indirectly that of the banking association, which is clearly reflected in the steady rise in the equity ratio,
- substantial improvement in the quality and effectiveness of risk management.

RWAs within the Group and the Association of Volksbanks were reduced further by cutting risks arising from the Non-core area on an ongoing basis. Total risk (risk-weighted amounts pursuant to CRR, to be applied from 1 January 2014) stood at euro 26.5 billion for the association as of 30 June 2014. As a result of the aforementioned measures, the Tier 1 capital ratio and the core capital ratio of the Association of Volksbanks amount to 11.2%. The equity ratio stands at 15.3%.

Following the FMA's JRAD decision issued in May 2014 for VBAG in its function as the central organisation for the Association of Volksbanks as per the association agreement pursuant to section 30a of the Austrian Banking Act (BWG), a 13.6% equity ratio was prescribed for the Association of Volksbanks on the basis of Basel III, which was to be complied with for the first time as of the 30 June 2014 reporting date.

This figure was decided on the basis of the lending portfolio and the risk regime as of the 31 December 2012 reporting date. It is impossible to gauge the extent to which the scheduled 2014 JRAD, based on the 30 June 2014 reporting date, will acknowledge the association's wind-down achievements – which are far ahead of schedule – and its handling of section 70 audit findings – which have largely been resolved – in terms of reducing the capital requirement in the coming years. It is also impossible to say at present how the results of the current AQR process and the subsequent stress test will affect the prescribed equity ratio for the banking association.

Based on current planning by VBAG and the Volksbanks, a banking association equity ratio of 13.6% can be expected by the end of 2014 in accordance with Basel III.

These forecasts, and consequently the fulfilment of these requirements, could be jeopardised if potential charges arising from the AQR/stress test or winding-down of VBAG's Non-core portfolio, for example, prove higher than expected, although such a scenario is not anticipated at present.

However, the current medium-term forecast anticipates a marked decline in equity ratios within the banking association from 2015 onwards. This is primarily due to equity reductions resulting from:

- agreements with the Republic of Austria and the European Commission (government participation capital of euro 300 million no longer eligible, non-controlling interest and capital differences of almost euro 500 million no longer eligible following the sale of VBLI and VB Romania in 2014 and 2015),

- various Basel III effects (phasing out of members' uncalled liabilities [Haftsummenzuschlag] totalling more than euro 300 million, and of private participation capital within the banking association totalling euro 180 million),
- foreseeable charges arising from the continued wind-down of VBAG's Non-core portfolio.

Current forecasts indicate a shortfall in equity funding in the banking association in 2017 on the basis of the 13.6% equity ratio based on the JRAD decision. As far as the Managing Board can see, regulatory authorities in Europe currently vary in their approach to the legal status of an SREP ratio under a JRAD process. Hence it is currently difficult to predict the extent of measures and sanctions which would be required or imposed by the regulatory authorities in the event of non-compliance.

As a precaution, a number of further initiatives have already been set in motion. Various programmes introduced in the past to relieve the burden of RWAs within the banking association have already reduced these at primary banks. VBAG's Managing Board believes that these initiatives should also be continued over the next two years to achieve a decrease in RWAs that exceeds the level currently planned. A feasibility study has been commissioned to determine whether switching to the IRB approach could result in a significant fall in RWAs. Other opportunities and requirements are also being assessed with a view to issuing new Basel III-compliant bonds (even though the ability to issue bonds seems limited at present). Finally, discussions will be held with shareholders and owners of participation capital regarding measures to optimise further the existing capital structure.

Following the government support provided in 2012, the European Commission and the Republic of Austria required VBAG to undertake an ambitious downsizing programme. This wind-down programme is legally binding on VBAG and is to be implemented by VBAG's governing bodies. As a result, the winding-down, in particular the associated compulsory sale of equity investments within the narrow timeframe prescribed by the European Commission, cannot be halted, even to prevent the loss of non-controlling interest.

A comprehensive strategy project was launched for the Association of Volksbanks in 2013 to improve its current medium-term planning. The aim is to leverage all earning potentials and cost synergies within the banking association in the short to medium term. Under the Managing Board's current plans, 55 Volksbanks and specialist institutions are to be merged into nine provincial Volksbanks and three specialist institutions. Based on harmonised structures and workflows, with their regional focus and market dominance, these Volksbanks should benefit from a group-like divisional structure. This programme is expected to make an additional and significant contribution to earnings by 2018. These extra earnings will however be offset by implementation costs, particularly in the years 2014-2016.

In the long run, these measures are expected to improve the banking association's equity ratios. Whether the medium-term improvement this will bring about in the banking association's earning power will create a basis for attracting capital from outside depends on whether potential investors consider the new approach to be sustainable.

Conversely it is possible, though unlikely on a present view, that the costs of the ongoing wind-down of the Non-core portfolio may turn out higher than anticipated in the medium-term planning, thereby countering any positive effects.

Following the JRAD assessment, the regulatory authorities raised the equity ratio for the Association of Volksbanks well above the statutory minimum capital requirements and also the capital requirements adopted for the purposes of state aid legislation – at least in the short term. It will be possible to comply with this equity ratio for the time being. Over the medium term, however, it will only be possible to adhere to the equity ratio of 13.6% imposed on the Association of Volksbanks as part of the scheduled JRAD process, which not only exceeds statutory minimum capital requirement but is also higher than the capital requirements adopted for the purposes of state aid legislation, if:
- sufficient opportunities and satisfactory conditions can be created to improve the association's ability to issue bonds, and/or
- the equity ratio that was increased very sharply and at short notice as part of the scheduled JRAD process can be reduced again in acknowledgement of the wind-down measures that have been successfully implemented in line with the requirements set out in the European Commission's decision on state aid rules, and/or
- suitable measures can be implemented in order to optimise VBAG's existing equity structure, or increase equity on the part of the owners.

Based on requirements set out in the restructuring agreement with the Republic of Austria dated 26 April 2012 and the European Commission's decision of 19 September 2012 based upon this, VBAG is required to dispose of key business areas and holdings in Austria and abroad over the coming years.

Previous experience in Austria and abroad has shown that these wind-down processes often involve higher costs than were previously foreseeable. VBAG's Non-core segment is also exposed to this uncertainty.

VBAG has a substantial real estate portfolio in Austria, and Central and Eastern Europe. In addition to credit risks, valuation haircuts may also be imposed as a result of spread risks when selling parts of this portfolio.

VBAG holds a 51% interest in Volksbank Romania S.A. (the company is measured at equity in the consolidated financial statements due to its being controlled jointly with non-Group third parties). Volksbank Romania S.A. plans various measures in 2014 in connection with this restructuring of its lending portfolio and the continuing build-up of primary deposits. In the equity planning, this results in a significantly higher equity requirement. The measures planned to strengthen the equity of VB Romania S.A. in the second half of 2014 resulted in a charge to earnings of euro 128 million as of 30 June 2014 arising from at equity accounted participating interests within the VBAG Group.

As at 30 June 2014, refinancing of euro 0.6 billion (31 December 2013: euro 0.8 billion) provided by VBAG to VB Romania was still outstanding. VBAG currently assumes, based on the measures planned under the sales process and the expected build-up of primary deposits at VB Romania, that repayments will be made on schedule. However, it is conceivable – though currently unlikely – that the difficult and volatile macroeconomic environment could give rise to stress scenarios that might impact the carrying amount of refinancing provided by VBAG to Volksbank Romania S.A.

The risk profile will also become clearer once Volksbank Romania's forecasts for the years 2015 and beyond have been presented, and a better estimate is available for the market environment in relation to the sale of Volksbank Romania S.A., which is to be concluded by 31 December 2015 at the latest.

The continuing economic malaise, particularly in the banking sector, poses a risk of lower incomes and distributions from equity participations. This may lead to lower market values in the future.

Regulators at European and national level are demanding that institutions comply, both now and in the future, with ever more extensive requirements. This constitutes a huge drain on Group resources in terms of personnel, as well as project and IT costs, but also has an impact due to potentially higher capital requirements that far exceed the minimum regulatory requirement under Basel II and Basel III. In this context, please refer to the detailed information provided in connection with the joint risk assessment and decision (JRAD), the asset quality review (AQR) and the 2014 bank stress test.

If capital regulations were to be infringed due to additional risk provisioning arising from the AQR or the stress test basis scenario, such infringements would need to be remedied within six months. If shortfalls in capital were to be identified on the basis of adverse stress tests, such shortfalls would need to be covered within nine months. When implementing recapitalisation measures to cover capital shortfalls, capital instruments of the highest quality are to be utilised to the extent that the shortfalls cannot be reduced with other funding sources. The results of the AQR and the stress test are not yet available. It is currently difficult to predict the scope of measures and sanctions that the regulatory authorities might apply in the event of non-compliance.

Entirely independently of the AQR and the stress test, reference has been made in the last two years to a further requirement for capital that might arise as a result of the necessary winding-down of business areas and participating interests. In particular, in order to avoid further charges, an extensive strategy project was launched across the banking association in summer 2013 with the ultimate objective of improving its internal financing power and the access to the capital markets.

2) Changes in the Group structure

One company from the Real Estate segment was sold in the first half of 2014. The deconsolidation result from VB Real Estate Leasing VOGEVA GmbH came to euro 106 thousand and is recorded under other operating income.

Calculation of deconsolidation result of Non-core Real Estate segment

Euro thousand	
Assets proportional	3,664
Liabilities proportional	2,974
Disposal of net assets proportional	**–691**
Revenues proportional	797
Deconsolidation result	**106**

Furthermore in the first half of 2014 several Holding companies have been merged. These mergers had no effect on the consolidated financial statements.

In the result of discontinued operation a purchase price adjustment which was agreed in the contract for the sale of Selini Holding GmbH is recorded in the first half of 2013. Detailed informations and breakdowns are shown in the consolidated financial statements as at 31 December 2013.

3) Subsequent events

After the balance sheet date further sales of project companies, loans and advances and real estate property were finalised. Due to the uncertainty of the outcome of the negotiations or due to the fact that the sale was initiated after the balance sheet date, these investments were not classified as assets held for sale.

Moody's issued new rating information in early August, downgrading VBAG by two notches from Ba1 to Ba3. This downgrade reflects Moody's belief that the Republic of Austria is now less prepared to support VBAG, and banks in general. At the same time, Moody's confirmed VBAG's Standalone Bank Financial Strength Rating. Moody's acknowledges the "substantial progress" made in the winding-down of the non-core portfolio.

As in March, Moody's rating downgrade had no significant negative effects on the Group's liquidity situation.

Shortly after Moody's announcement, Fitch also published new rating information relating to the Association of Volksbanks and VBAG, in which express reference is also made to the progress achieved in winding down VBAG's non-core portfolio both last year and this year. In contrast to Moody's, Fitch confirmed its A rating for the association, for all association banks and for VBAG. This signifies "safe investment, unless unforeseen events should occur". The outlook at Fitch remains "negative" – both for the association and VBAG. Fitch justifies confirmation of its A rating by referring to the fact that the Association of Volksbanks commands a significant market share of 7%. Hence it is regarded as systemically relevant by the Austrian authorities, as the Volksbank network covers rural areas where few alternatives exist.

Fitch now justifies the confirmation of its "negative outlook" by referring to the fact that "a clear intention exists in the EU to reduce state support for banks. This is demonstrated by a number of statutory, regulatory and political initiatives. Given also the ad hoc legislation for Hypo Alpe Adria, it is further expected that the Republic of Austria's willingness to support VBAG, and banks in general, will diminish." Unless this changes by the next credit review, it must be anticipated that Fitch will reduce the support uplift in the medium term (rating improvement through potential state support), which would negatively affect the rating for the Association of Volksbanks. The potential extent of such a reduction is currently unclear.

4) Notes to the income statement

Net interest income

Euro thousand	1-6/2014	1-6/2013
Interest and similar income	296,195	404,028
Interest and similar income from	272,333	380,611
liquid funds	255	681
credit and money market transactions with credit institutions	36,058	28,964
credit and money market transactions with customers	126,145	167,981
debt securities	49,650	69,440
derivatives in the investment book	60,226	113,544
Current income from	15,546	12,530
equities and other variable-yield securities	491	1,020
other affiliates	668	1,493
investments in other companies	14,387	10,017
Income from operating lease and investment property	8,316	10,888
rental income investment property	6,216	7,642
income from operating lease contracts	2,100	3,246
rental income	10,194	12,277
depreciation	–8,094	–9,030
Interest and similar expenses of	–191,984	–271,304
deposits from credit institutions (including central banks)	–49,765	–67,964
deposits from customers	–30,385	–37,122
debts evidenced by certificates	–95,041	–154,444
subordinated liabilities	–14,819	–8,267
derivatives in the investment book	–1,975	–3,507
Net interest income	104,211	**132,725**

Net interest income according to IAS 39 categories

Euro thousand	1-6/2014	1-6/2013
Interest and similar income	296,195	404,028
Interest and similar income from	272,333	380,611
financial investments at fair value through profit or loss	606	1,953
derivatives in the investment book	60,226	113,544
financial investments not at fair value through profit or loss	211,501	265,114
financial investments available for sale	37,945	47,202
financial investments at amortised cost	163,797	203,240
of which financial lease	75,638	82,003
of which unwinding of risk provisions	1,313	1,007
financial investments held to maturity	9,759	14,672
Current income from	15,546	12,530
financial investments at fair value through profit or loss	262	568
financial investments available for sale	15,285	11,961
Income from operating lease and investment property	8,316	10,888
Interest and similar expenses of	–191,984	–271,304
derivatives in the investment book	–1,975	–3,507
financial liabilities at amortised cost	–190,010	–267,797
Net interest income	104,211	**132,725**

Risk provisions

Euro thousand	1-6/2014	1-6/2013
Allocation to risk provisions	–57,038	–86,947
Release of risk provisions	62,381	80,739
Allocation to provisions for risks	–3,053	–2,602
Release of provisions for risks	1,472	694
Direct write-offs of loans and advances	–28,673	–20,885
Income from loans and advances previously written off	1,273	1,653
Risk provisions	**–23,638**	**–27,349**

Net fee and commission income

Euro thousand	1-6/2014	1-6/2013
Fee and commission income from	32,588	37,239
lending operations	5,195	9,171
securities businesses	21,358	21,993
payment transactions	2,195	2,448
foreign exchange, precious metals	0	15
other banking services	3,839	3,612
Fee and commission expenses from	–22,282	–18,377
lending operations	–9,310	–9,588
securities businesses	–11,954	–7,988
payment transactions	–624	–482
other banking services	–394	–319
Net fee and commission income	**10,306**	**18,862**

Net fee comission income does not include any income or expenses from financial investments designated at fair value through profit or loss.

Net trading income

Euro thousand	1-6/2014	1-6/2013
Equity related transactions	-1,056	2,650
Exchange rate related transactions	889	1,684
Interest rate related transactions	4,925	–31,089
Net trading income	**4,758**	**–26,755**

General administrative expenses

Euro thousand	1-6/2014	1-6/2013
Staff expenses	–68,174	–69,358
Other administrative expenses	–54,166	–51,377
Depreciation of fixed tangible and intangible assets	–4,239	–5,473
General administrative expenses	**–126,579**	**–126,209**

Other operating result

Euro thousand	1-6/2014	1-6/2013
Other operating income and expenses	–4,754	87,486
Proceeds from deconsolidation of subsidiaries	106	2,523
Other taxes	–19,127	–24,057
Other operating result	**–23,774**	**65,952**

Other operating income and expenses are added up in the table above.

In the first half of 2014 an amount of euro -34,604 thousand is recorded in other operating expenses according to the measurement regulations for disposal groups of IFRS 5. Furthermore an amount of euro 14,720 thousand is recognised in other operating income concerning a repayment of value added tax in VB Leasing Poland from a now closed legal procedure.

In the comparative period, an amount of euro 65 million was recorded in other operating result from the asset guarantee provided by the Republic of Austria. Detailed information is shown in the consolidated financial statements as at 31 December 2013.

Deconsolidation result of euro 106 thousand for VB Real Estate Leasing VOGEVA GmbH is recognised in the deconsolidation result. In the same period last year the results of euro 54 thousand from the sale of VB Real Estate Leasing Bonus GmbH and euro 2,469 thousand for Immokik s.r.l. are included.

Other taxes comprises the banking tax.

Income from financial investments

Euro thousand	1-6/2014	1-6/2013
Result from financial investments at fair value through profit or loss	–2,892	**4,816**
Result from financial investments at fair value through profit or loss	–2,892	4,816
Debt securities	–285	3,981
Equity and other variable-yield securities	–2,607	835
Result from fair value hedges	332	**3,688**
Result from revaluation of underlying instruments	–25,596	51,662
Loans and advances to credit institutions and customers	3,702	–22,427
Debt securities	68,480	–72,459
Amounts owed to credit institutions and customers	–28,370	65,653
Debts evidenced by certificates	–69,408	80,895
Result from revaluation of derivatives	25,928	–47,974
Result from valuation of other derivatives in the investment book	–7,233	**–22,800**
Exchange rate related transactions	1,542	3,381
Interest rate related transactions	-7,783	–2,758
Credit related transactions	220	–1,816
Other transactions	–1,212	–21,607
Result from available for sale financial investments (including participations)	-1,917	**4,178**
Realised gains/losses	3,571	9,478
Income from revaluation	0	1,276
Impairments	–5,487	–6,576
Result from loans & receivables financial investments	–375	**2,983**
Realised gains/losses	–375	3,367
Income from revaluation	0	13
Impairments	0	–397
Result from held to maturity financial investments	11,335	**1,425**
Realised gains/losses	11,335	1,425
Result from assets for operating lease and investment property assets as well as other financial investments	–6,280	**–15,502**
Realised gains/losses	–187	2,049
Change in value investment properties	–6,093	–17,551
Result from financial investments	–7,030	**–21,212**

In the first half of 2014, an amount of euro 3,290 thousand (1-6/2013: euro 8,641 thousand) previously recognised in the available for sale reserve was reclassified and shown in income statement.

Euro thousand	1-6/2014	1-6/2013
Result from financial investments, which are measured at fair value through profit and loss	**–15,886**	**–31,847**
Financial instruments at fair value through profit or loss	–2,892	4,816
Fair value hedges	332	3,688
Other derivatives in investment book	–7,233	–22,800
Investment property assets	–6,093	–17,551
Result from financial investments, which are not measured at fair value through profit and loss	**8,856**	**10,635**
Realised gains/losses	14,344	16,319
Available for sale financial investments	3,571	9,478
Loans & receivables financial investments	–375	3,367
Held to maturity financial investments	11,335	1,425
Operating lease assets and other financial investments	–187	2,049
Income from revaluation	0	1,289
Available for sale financial investments	0	1,276
Loans & receivables financial investments	0	13
Impairments	–5,487	–6,973
Available for sale financial investments	–5,487	–6,576
Loans & receivables financial investments	0	–397
Income from financial investments	**–7,030**	**–21,212**

Income from companies measured at equity

The result from at equity accounted companies during the first half of 2014 reflected charges of euro 128 million arising from the planned measures to strengthen the own funds of VB Romania S.A.

In the comparative period the income from companies measured at equity displays the impairment of the capital increase in VB RO as at October 2013 amounting of euro 60 million.

Income Taxes

No deferred tax assets were recognised on the loss in VBAG in the first half of 2014 since they cannot be used over the next four years. Deferred tax income on differences derived from the valuation of derivatives and securities was recognised to the extent that deferred tax liabilities were incurred from other valuation differences.

5) Notes to the consolidated statement of financial position

Loans and advances to credit institutions and customers

Euro thousand	30 Jun 2014	31 Dec 2013
Loans and advances to credit institutions	5,981,989	5,798,139
Loans and advances to customers	5,904,923	7,081,347
Loans and advances to credit institutions and customers	**11,886,912**	**12,879,486**

Loans and advances to credit institutions and customers are measured at amortised cost.

Risk provisions Euro thousand	Individual impairment credit institutions	Individual impairment customers	Portfolio based allowance	Total
As at 1 Jan 2013	703	882,950	183,392	1,067,045
Changes in the scope of consolidation	0	0	0	0
Currency translation	0	–6,872	–141	–7,013
Reclassification	0	3,115	0	3,115
Unwinding	0	–1,007	0	–1,007
Utilisation	0	–142,509	0	–142,509
Release	0	–45,438	–35,301	–80,739
Addition	0	86,947	0	86,947
As at 30 Jun 2013	703	777,188	147,950	925,841
As at 1 Jan 2014	**703**	**708,993**	**63,313**	**773,009**
Currency translation	0	220	11	231
Reclassification	0	–7,369	–3,626	–10,995
Unwinding	0	–1,313	0	–1,313
Utilisation	0	–145,664	0	–145,664
Release	0	–44,459	–17,922	–62,381
Addition	0	56,994	44	57,038
As at 30 Jun 2014	703	567,401	41,821	609,925

The additions include an amount of euro 4,892 thousand (1-6/2013 euro 225 thousand), which is caused by allocation due to interest past-due. Loans and advances to credit institutions and customers include non-interest-bearing receivables amounting to euro 440,307 thousand (31 Dec 2013: euro 406,930 thousand). In 2014, the line reclassification includes the reclassification to the position assets held for sale for the most part.

Trading assets

Euro thousand	30 Jun 2014	31 Dec 2013
Debt securities	106,428	109,947
Equity and other variable-yield securities	17,565	26,655
Positive fair value from derivatives	1,439,517	1,490,790
equity related transactions	33,983	39,401
exchange rate related transactions	1,991	2,337
interest rate related transactions	1,403,543	1,449,052
Trading assets	**1,563,509**	**1,627,392**

Financial investments

Euro thousand	30 Jun 2014	31 Dec 2013
Financial investments at fair value through profit or loss	20,765	51,976
Debt securities	11,481	42,897
Equity and other variable-yield securities	9,284	9,080
Financial investments available for sale	2,219,089	2,283,393
Debt securities	2,157,849	2,216,571
Equity and other variable-yield securities	61,240	66,822
Financial investments loans & receivables	210,826	255,945
Financial investments held to maturity	528,981	831,425
Financial investments	**2,979,661**	**3,422,739**

Reclassification from available for sale to loans & receivables

In accordance with the amendments to IAS 39 and IFRS 7, available for sale financial investments were reclassified to the loans & receivables category in 2008. On initial recognition, these securities met the definition for the loans & receivables category but were instead designated as available for sale. The reclassification to the loans & receivables category was performed with retrospective effect from 1 July 2008. The fair value at the reclassification date was applied as the new carrying amount of these securities.

Euro thousand	30 Jun 2014	31 Dec 2013	1 Jul 2008
Carrying amount	93,288	106,754	1,140,363
Fair value	94,763	108,218	1,140,363
Available for sale reserve with reclassification	–4,152	–4,724	–79,177
Available for sale reserve without reclassification	–4,815	–6,009	–79,177

The amounts of the available for sale reserve take into account deferred taxes. The reclassification did not have any material effect on the income statement.

Investment property

Euro thousand	30 Jun 2014	31 Dec 2013
Investment properties	**186,170**	**252,410**

Participations

Euro thousand	30 Jun 2014	31 Dec 2013
Investments in unconsolidated affiliates	37,790	27,660
Participating interests	73,000	76,276
Investments in other companies	255,403	255,596
Participations	**366,192**	**359,531**

Shares and participations in companies whose fair value cannot be reliably determined are carried at cost net of any impairment. Shares and participations with a carrying amount of euro 322,594 thousand (31 Dec 2013: euro 310,322 thousand)were measured at fair value.

Other assets

Euro thousand	30 Jun 2014	31 Dec 2013
Deferred items	7,267	12,110
Other receivables and assets	238,760	208,200
Positive fair value from derivatives in the investment book	415,308	394,434
Other assets	**661,335**	**614,744**

Assets held for sale

This position includes assets which have been classified as assets held for sale according to IFRS 5. The displayed amount is composed as follows.

Euro thousand	30 Jun 2014	31 Dec 2013
Liquid funds	391	0
Loans and advances to credit institutions (gross)	29,534	0
Loans and advances to customers (gross)	950,843	397,706
Risk provisions (–)	–53,844	–42,732
Financial investments	32,051	36,442
Investment property	60,200	0
Participations	3,854	31,781
Intangible assets	302	0
Tangible fixed assets	11,123	0
Tax assets	15,940	0
Other assets	21,836	142,722
Other liabilities	0	–11,261
Assets held for sale	**1,072,230**	**554,657**

Amounts owed to credit institutions

Euro thousand	30 Jun 2014	31 Dec 2013
Central banks	209,898	152,100
Other credit institutions	7,134,317	7,554,902
Amounts owed to credit institutions	**7,344,215**	**7,707,002**

The amounts owed to credit institutions are measured at amortised cost.

Amounts owed to customers

Euro thousand	30 Jun 2014	31 Dec 2013
Savings deposits	201	201
Other deposits	1,935,343	2,148,239
Amounts owed to customers	**1,935,544**	**2,148,440**

The amounts owed to customers are measured at amortised cost.

Debts evidenced by certificates

Euro thousand	30 Jun 2014	31 Dec 2013
Bond issues	5,202,456	7,084,825
Debts evidenced by certificates	**5,202,456**	**7,084,825**

Debts evidenced by certificates are all measured at amortised cost.

Trading liabilities

Euro thousand	30 Jun 2014	31 Dec 2013
Negative fair value from derivatives		
equity related transactions	42,943	58,755
exchange rate related transactions	14,007	13,044
interest rate related transactions	1,363,736	1,305,910
Trading liabilities	**1,420,686**	**1,377,709**

Other liabilities

Euro thousand	30 Jun 2014	31 Dec 2013
Deferred items	13,847	14,113
Other liabilities	377,670	224,801
Negative fair value from derivatives in the investment book	284,371	315,635
Other liabilities	**675,887**	**554,549**

Liabilities held for sale

This position includes liabilities which have been classified as liabilities held for sale according to IFRS 5. The displayed amount is composed as follows.

Euro thousand	30 Jun 2014	31 Dec 2013
Amounts owed to credit institutions	339,619	0
Amounts owed to customers	12,403	0
Provisions	3,857	0
Tax liabilities	4,530	0
Other liabilities	66,093	0
Liabilities held for sale	**426,501**	**0**

Subordinated liabilities

Euro thousand	30 Jun 2014	31 Dec 2013
Subordinated liabilities	424,559	442,585
Supplementary capital	112,761	112,372
Subordinated liabilities	**537,320**	**554,957**

Subordinated liabilities are measured at amortised cost. Book value of supplementary capital was calculated by discounting the estimated future cash flows with the original effective interest rate in order to get the net present value according to IAS 39 AG 8.

6) Own funds

The own funds of the Association of Volksbanks which were calculated pursuant to the Capital Requirement Regulations (CRR) can be broken down as follows:

Euro thousand	30 Jun 2014
Paid-up capital instruments (less own CET 1 instruments)	405,205
Reserves	1,842,266
Transitional adjustments due to grandfathered CET 1 capital instruments	521,207
Minority interest	184,853
Deduction and adjustments	–161,749
Transitional adjustments to CET 1 capital	163,197
Common equity tier 1 capital (CET 1)	2,954,979
AT 1 capital and qualifying AT 1 instruments issued by subsidiaries	48,692
Deduction and adjustments	133,835
Transitional adjustments to AT 1 capital	–182,527
Additional tier 1 capital (AT 1)	0
Tier 1 capital (T1 = CET 1 + AT 1)	2,954,979
T2 capital and qualifying AT 1 instruments issued by subsidiaries	1,103,134
Tier 2 capital (T2)	1,103,134
Own funds	4,058,113

Common equity tier 1 capital ratio (tier 1)[1)]	11.16%
Tier 1 capital ratio[1)]	11.16%
Equity ratio[1)]	15.33%

1) in relation to total risk exposure amount

The risk-weighted assessment amounts as defined in CRR can be broken down as follows:

Euro thousand	30 Jun 2014
Risk weighted exposure amount - credit risk	22,655,762
Total risk exposure amount for position, foreign exchange and commodities risks	782,039
Total risk exposure amount for operational risk (OpR)	2,345,136
Total risk for credit valuation adjustment (CVA)	689,669
Total risk exposure amount	26,472,606

Starting with 1 January 2014, the reporting of own funds and of the risk exposure amounts was adapted to the new regulations of CRR. The reported figures are based on the Association of Volksbanks. The Association of Volksbanks is an association according to section 30a of the Austrian Banking Act and includes the Volksbank primary banks, VBAG as well as their subordinated institutes. Before the figures were based on Basel II regulations and computed for the VBAG Group of credit institutions. As a comparison would be of limited information, no comparative figures were displayed.

In accordance with IFRS reporting, the scope of consolidation differs from the scope of consolidation under CRR as the IFRS provides for the inclusion of other entities not belonging to the financial sector. According to CRR, companies in the financial sector that are under the control of the parent or where the Group helds a majority of shares either direct or indirect, are fully consolidated. Therefore VB RO and VBI Bet GmbH are still included in the scope of consolidation under CRR and are fully consolidated for the purpose of calculation of own resources and capital requirements. The carrying amount of institutions, financial institutions and subsidiaries providing banking-related auxiliary services that are controlled by the parent but that are not significant for the presentation of the group of credit institutions according to section 19 (1) of CRR is deducted from own funds. Subsidiaries which are managed jointly with non-Group companies are proportionately consolidated. Investments in companies in the financial sector with a share of between 10% and 50% that are not jointly managed are also deducted from own funds unless they are voluntarily consolidated on a pro rata basis. Investments in companies in the financial sector of less than 10% are deducted from own funds considering the eligibility according to section 46 CRR. All other participating interests are included in the assessment base at their carrying amounts.

All credit institutions under control or where the Group helds a majority of shares either direct or indirect are considered in the scope of consolidation according to CRR.

In the first half year of 2014, no substantial, practical or legal obstacles existed which would have prevented the transfer of equity or the repayment of liabilities between the parent institution and institutions subordinated to the former.

7) Financial assets and liabilities

The table below shows financial assets and liabilities in accordance with their individual categories and their fair values.

Euro thousand	Held for trading	At fair value through profit or loss	Held to maturity	Available for sale	Amortised cost	Carrying amount – total	Fair value
30 Jun 2014							
Liquid funds	0	0	0	0	446,773	446,773	446,773
Loans and advances to credit institutions	0	0	0	0	5,981,989	5,981,989	
Individual impairment credit institutions	0	0	0	0	–703	–703	
Loans credit institutions less individual impairment	0	0	0	0	5,981,286	5,981,286	5,927,684
Loans and advances to customers	0	0	0	0	5,904,923	5,904,923	
Individual impairment customers	0	0	0	0	–567,401	–567,401	
Loans customers less individual impairment	0	0	0	0	5,337,522	5,337,522	5,300,765
Trading assets	1,563,509	0	0	0	0	1,563,509	1,563,509
Financial investments	0	20,765	528,981	2,219,089	210,826	2,979,661	2,982,090
Participations	0	0	0	366,192	0	366,192	366,192
Derivatives investment book	415,308	0	0	0	0	415,308	415,308
Assets held for sale less individual impairments	0	11,972	0	23,915	927,428	963,315	970,800
Financial assets total	**1,978,817**	**32,738**	**528,981**	**2,609,196**	**12,903,835**	**18,053,566**	**17,973,123**
Amounts owed to credit institutions	0	0	0	0	7,344,215	7,344,215	7,362,409
Amounts owed to customers	0	0	0	0	1,935,544	1,935,544	1,851,229
Debts evidenced by certificates	0	0	0	0	5,202,456	5,202,456	5,268,461
Trading liabilities	1,420,686	0	0	0	0	1,420,686	1,420,686
Derivatives – investment book	284,371	0	0	0	0	284,371	284,371
Subordinated liabilities	0	0	0	0	537,320	537,320	458,895
Liabilities held for sale	0	0	0	0	354,652	354,652	354,652
Financial liabilities total	**1,705,056**	**0**	**0**	**0**	**15,374,187**	**17,079,243**	**17,000,702**

Euro thousand	Held for trading	At fair value through profit or loss	Held to maturity	Available for sale	Amortised cost	Carrying amount – total	Fair value
31 Dec 2013							
Liquid funds	0	0	0	0	1,762,453	1,762,453	1,762,453
Loans and advances to credit institutions	0	0	0	0	5,798,139	5,798,139	
Individual impairment credit institutions	0	0	0	0	–703	–703	
Loans credit institutions less individual impairment	0	0	0	0	5,797,436	5,797,436	5,641,889
Loans and advances to customers	0	0	0	0	7,081,347	7,081,347	
Individual impairment customers	0	0	0	0	–708,993	–708,993	
Loans customers less individual impairment	0	0	0	0	6,372,354	6,372,354	6,280,427
Trading assets	1,627,392	0	0	0	0	1,627,392	1,627,392
Financial investments	0	51,976	831,425	2,283,393	255,945	3,422,739	3,426,480
Participations	0	0	0	359,531	0	359,531	359,531
Derivatives – investment book	394,434	0	0	0	0	394,434	394,434
Assets held for sale	0	34,850	0	33,373	354,974	423,196	419,181
Financial assets total	**2,021,826**	**86,826**	**831,425**	**2,676,297**	**14,543,161**	**20,159,535**	**19,911,787**
Amounts owed to credit institutions	0	0	0	0	7,707,002	7,707,002	7,613,995
Amounts owed to customers	0	0	0	0	2,148,440	2,148,440	2,043,646
Debts evidenced by certificates	0	0	0	0	7,084,825	7,084,825	7,172,449
Trading liabilities	1,377,709	0	0	0	0	1,377,709	1,377,709
Derivatives – investment book	315,635	0	0	0	0	315,635	315,635
Subordinated liabilities	0	0	0	0	554,957	554,957	483,160
Financial liabilities total	**1,693,344**	**0**	**0**	**0**	**17,495,224**	**19,188,568**	**19,006,594**

The table below shows all assets and liabilities which are measured at fair value classified according to their fair value hierarchy.

Euro thousand	Level 1	Level 2	Level 3	Total
30 Jun 2014				
Financial assets				
Trading assets	20,895	1,542,615	0	1,563,509
Financial investments	1,615,960	599,178	6,110	2,221,249
at fair value through profit or loss	5	14,650	6,110	20,765
available for sale	1,615,955	584,528	0	2,200,483
Participations	0	0	322,594	322,594
Derivatives – investment book	0	415,308	0	415,308
Assets held for sale	18,930	0	16,957	35,887
Total	**1,655,785**	**2,557,100**	**345,662**	**4,558,547**
Financial liabilities				
Trading liabilities	0	1,420,686	0	1,420,686
Derivatives – investment book	0	284,371	0	284,371
Total	**0**	**1,705,056**	**0**	**1,705,056**

Euro thousand	Level 1	Level 2	Level 3	Total
31 Dec 2013				
Financial assets				
Trading assets	41,507	1,585,885	0	1,627,392
Financial investments	1,921,850	393,366	132	2,315,348
at fair value through profit or loss	8,253	43,591	132	51,976
available for sale	1,913,596	349,775	0	2,263,372
Participations	0	0	310,322	310,322
Derivatives – investment book	0	394,434	0	394,434
Assets held for sale	0	0	68,222	68,222
Total	**1,963,357**	**2,373,685**	**378,677**	**4,715,719**
Financial liabilities				
Trading liabilities	0	1,377,709	0	1,377,709
Derivatives – investment book	0	315,635	0	315,635
Total	**0**	**1,693,344**	**0**	**1,693,344**

Available for sale financial investments totalling euro 18,605 thousand (31 Dec 2013: euro 20,021 thousand) and participations totalling euro 43,598 thousand (31 Dec 2013: euro 49,209 thousand) are measured at amortised cost because their fair value cannot be determined without unreasonable effort.

In the first half of 2014 financial instruments with a carrying amount of euro 67,091 thousand, which were still measured at Level 2 market value as at 31 December 2012, were reclassified as Level 1 financial instruments due to an increase in trading activity. On the other hand, Level 1 financial instruments with a carrying amount of euro 345,678 thousand were reclassified into Level 2 due to a decrease in market trading activity. The measurement methods outlined in the 2013 annual report remained unchanged.

Fair value hierarchy

Financial instruments recognised at fair value are assigned to the three IFRS fair value hierarchy categories.

Level 1 – Financial instruments measured at quoted prices in active markets, whose fair value can be derived directly from prices on active, liquid markets and where the financial instrument observed on the market is representative of the financial instrument owned by the Group that requires measurement.

Level 2 – Financial instruments measured using procedures based on observable market data, whose fair value can be determined using similar financial instruments traded on active markets or using procedures whose inputs are observable.

Level 3 – Financial instruments measured using procedures based on unobservable parameters, whose fair value cannot be determined using data observable on the market. Financial instruments in this category have a value component that is not observable and which has a significant influence on fair value.

Development of Level 3 fair values

Euro thousand	Financial investments at fair value through profit and loss	Participations	Available for sale	Assets held for sale	Total
As at 1 Jan 2013	66,725	312,409	0	0	379,134
Changes in the scope of consolidation	0	5,561	0	0	5,561
Reallocation in Level 3	2,645	67,651	1,592	0	71,887
Additions	1,408	9,100	0	0	10,509
Disposals	–20,115	–17,946	0	0	–38,061
Valuation					
through profit or loss	–15,682	–12,549	0	0	–28,230
through other comprehensive income	0	–22,123	0	0	–22,123
Reclassification	–34,850	–31,781	–1,592	68,222	0
As at 31 Dec 2013	132	310,322	0	68,222	378,677
Changes in the scope of consolidation	0	0	0	0	0
Reallocation in Level 3	0	0	0	0	0
Additions	0	22,640	0	0	22,640
Disposals	0	–5,177	0	–42,331	–47,508
Valuation					
through profit or loss	–89	–4,830	0	–5,271	–10,190
through other comprehensive income	0	–725	0	2,768	2,043
Reclassification	6,068	364	0	–6,431	0
As at 30 Jun 2014	**6,110**	**322,594**	**0**	**16,957**	**345,662**

Improved systems allowed more extensive valuation of holdings at fair value in 2013, which led to financial instruments being reclassified into Level 3 during the previous year.

The calculation of the fair values for private equity companies, included with an amount of euro 6,110 thousand in level 3 fair values of financial investments at fair value through profit or loss, with an amount of euro 4,780 thousand in level 3 fair values of particiaption and with an amount of euro 16,957 thousand in level 3 fair values of assets held for sale is done by fund managers on the basis of regularly provided reporting documents. These information is provided on a quarterly basis. The reporting contains a fair value calculation for the share of VBAG and is updated mostly quarterly. The fair value calculation of the fund manager is based on the fair value of the single portfolio entities and of other assets and liabilities. In the majority of cases the valuation is in line with the Reporting Guidelines of ECVA (European Private Equity and Venture Capital Association) which constitutes a market standard for valuation.

In terms of sensitivity analyses for level 3 market values concerning participations, factors that increase or decrease value are determined in alternative valuation scenarios by varying income estimates and income-based parameters within a range of 10% to 20%. In the event of a beneficial movement, market value changes by euro 31,105 thousand (31 Dec 2013: euro 34,961 thousand), while a detrimental movement leads to a change of euro –30,900 thousand (31 Dec 2013: euro –34,990 thousand). The private equity portfolio is not included in the sensitivity analyses as no significant deviations in value were noted in the past which would suggest major uncertainties in determining fair values.

8) Number of staff

Number of staff employed during the business year, including disposal groups

	Average number of staff		Number of staff at end of period	
	1-6/2014	**1-6/2013**	**30 Jun 2014**	**31 Dec 2013**
Domestic	**1,078**	1,124	**1,074**	1,101
Foreign	**742**	757	**736**	752
Number of staff - total	**1,820**	**1,881**	**1,810**	**1,853**

9) Branches

	30 Jun 2014	31 Dec 2013
Domestic	1	1
Foreign	1	1
Total	**2**	**2**

10) Related party disclosures

Euro thousand	Unconsolidated affiliates	Companies in which the Group has a participating interest	Associated companies	Companies which exercise a significant influence on the parent as shareholders
30 Jun 2014				
Loans and advances to credit institutions	0	628,642	556,707	0
Loans and advances to customers	33,845	138,987	0	0
Risk provisions (–)	–2,084	–42,007	0	0
Debt securities	0	80,661	0	805,744
Amounts owed to credit institutions	0	930,763	37,399	0
Amounts owed to customers	12,240	17,113	2,318	298
Liabilites arising from guarantees	0	0	0	0
31 Dec 2013				
Loans and advances to credit institutions	0	660,669	827,161	
Loans and advances to customers	43,872	164,904	0	0
Risk provisions (–)	–3,878	–44,275	0	0
Debt securities	0	69,104	0	778,595
Amounts owed to credit institutions	0	1,009,141	13,829	0
Amounts owed to customers	5,727	29,664	2,318	209
Liabilities arising from guarantees	0	2,088	0	0

Transfer prices between the VBAG Group and its associated companies are geared to usual market conditions. As in previous year, VBAG Group does not have any other liabiltities for unconsolidated affiliates or associated companies on balance sheet date.

The shareholders Volksbanken Holding eGen and Republic of Austria exercise a significant influence on Österreichische Volksbanken-AG.

As at 30 June 2014, loans and advances to credit institutions contain transactions with the Volksbank-Sector amounting to euro 3,287,854 thousand (31 Dec 2013: euro 4,064,671 thousand) and amounts owed to credit institutions include transactions with the Volksbank-Sector amounting to euro 5,166,924 thousand (31 Dec 2013: euro 5,359,206 thousand).

11) Segment reporting

Segment reporting by business segments

Euro thousand	Financing	Financial Markets	Other Operations	Non-core Corporates	Non-core Real Estate	Non-core Retail	Non-core Investment Book/Other operations	Con-solidation	Total
Net interest income									
1-6/2014	17,438	15,766	1,746	2,895	11,461	42,294	14,137	–1,527	104,211
1-6/2013	16,548	21,468	2,748	11,080	27,421	45,476	10,468	–2,483	132,725
Risk provisions									
1-6/2014	–3,326	–1,217	–116	–12,890	-7,404	94	1,221	0	–23,638
1-6/2013	–3,539	–29	–3	–1,685	–16,640	–2,250	–3,203	0	–27,349
Net fee and commission income									
1-6/2014	2,297	9,037	2,116	–415	–63	3,043	–5,846	137	10,306
1-6/2013	3,078	13,727	3,029	517	168	2,441	–4,349	251	18,862
Net trading income									
1-6/2014	2	5,014	0	–9	681	–985	56	0	4,758
1-6/2013	8	–28,056	1	58	–280	1,486	30	0	–26,755
General administrative expenses									
1-6/2014	–23,410	–33,743	–13,422	–7,688	–21,403	–24,832	–8,169	6,088	–126,579
1-6/2013	–18,599	–31,093	–20,167	–10,731	–20,497	–24,904	–6,720	6,502	–126,209
Other operating result									
1-6/2014	2,926	2,570	7,461	–5,742	2,015	3,179	–31,485	–4,698	–23,774
1-6/2013	3,038	7,117	2,378	–739	–2,204	3,723	56,910	–4,270	65,952
Income from financial investments									
1-6/2014	243	–6,310	0	–2,287	–9,788	339	10,775	0	–7,030
1-6/2013	–27	–43,759	31,430	5,476	–16,950	601	2,017	0	–21,212
Income from companies measured at equity									
1-6/2014	0	0	120	0	0	–128,053	0	0	–127,934
1-6/2013	0	0	100	0	0	–60,000	0	0	–59,900
Income from discontinued operation									
1-6/2014	0	0	0	0	0	0	0	0	0
1-6/2013	0	0	0	0	15,308	0	0	0	15,308
Result for the period before taxes									
1-6/2014	–3,831	–8,882	–2,095	–26,137	–24,501	–104,922	–19,312	0	–189,680
1-6/2013	**506**	**–60,626**	**19,516**	**3,975**	**–13,674**	**–33,427**	**55,154**	**0**	**–28,577**
Income taxes including taxes of discontinued operation									
1-6/2014	–270	–694	9,881	–217	842	–5,657	–33	0	3,851
1-6/2013	–1,518	22,533	–18,555	–1,885	285	–5,416	–22,631	0	–27,186
Result for the period after taxes									
1-6/2014	–4,100	–9,577	7,786	–26,354	–23,659	–110,579	–19,346	0	–185,828
1-6/2013	**–1,011**	**–38,093**	**961**	**2,090**	**–13,389**	**–38,843**	**32,523**	**0**	**–55,762**
Total assets									
30 Jun 2014	2,422,757	16,187,056	759,288	367,039	1,345,940	1,968,911	1,980,235	–6,249,618	18,781,608
31 Dec 2013	2,535,110	16,595,061	912,994	621,779	2,057,020	2,028,063	2,379,189	–6,225,109	20,904,109
Loans and advances to customers									
30 Jun 2014	2,440,353	2,015,374	11	527,217	1,334,346	1,036,689	42,039	–1,491,106	5,904,923
31 Dec 2013	2,543,842	1,672,728	11	712,958	1,585,566	1,818,242	176,947	–1,428,948	7,081,347
Companies measured at equity									
30 Jun 2014	0	0	5,745	0	0	43,350	0	0	49,095
31 Dec 2013	0	0	5,626	0	0	0	0	0	5,626
Amounts owed to customers									
30 Jun 2014	41,091	2,116,344	13	18,995	60,208	2,144	0	–303,250	1,935,544
31 Dec 2013	45,592	2,413,756	13	46,304	59,262	4,068	10,590	–431,146	2,148,440
Debts evidenced by certificates including subordinated liabilities									
30 Jun 2014	336,202	5,647,559	0	72,236	221,175	0	513,904	–1,051,300	5,739,776
31 Dec 2013	356,969	7,003,748	0	114,503	367,618	0	605,457	–808,515	7,639,781

Segment reporting by regional markets

Euro thousand	Austria	Central and Eastern Europe	Other markets	Total
Net interest income				
1-6/2014	54,558	46,675	2,979	104,211
1-6/2013	80,775	51,540	410	132,725
Risk provisions				
1-6/2014	–30,447	1,516	5,292	–23,638
1-6/2013	–18,410	–5,155	–3,784	–27,349
Net fee and commission income				
1-6/2014	8,524	2,631	–850	10,306
1-6/2013	16,258	1,953	651	18,862
Net trading income				
1-6/2014	4,287	416	55	4,758
1-6/2013	–28,175	1,349	72	–26,755
General administrative expenses				
1-6/2014	–91,919	–26,215	–8,444	–126,579
1-6/2013	–93,017	–26,254	–6,938	–126,209
Other operating result				
1-6/2014	3,250	750	–27,774	–23,774
1-6/2013	57,442	8,410	100	65,952
Income from financial investments				
1-6/2014	–7,389	–7,362	7,720	–7,030
1-6/2013	–5,409	–19,133	3,330	–21,212
Income from companies measured at equity				
1-6/2014	120	–128,053	0	–127,934
1-6/2013	100	–60,000	0	–59,900
Income from discontinued operation				
1-6/2014	0	0	0	0
1-6/2013	15,308	0	0	15,308
Result for the period before taxes				
1-6/2014	–59,016	–109,641	–21,023	–189,680
1-6/2013	**–24,872**	**–47,290**	**–6,159**	**–28,577**

12) Quarterly financial data

Euro thousand	4-6/2014	1-3/2014	10-12/2013	7-9/2013	4-6/2013
Net interest income	53,967	50,244	37,601	18,260	82,681
Risk provisions	–12,634	–11,004	26,409	–22,522	9,758
Net fee and commission income	5,201	5,105	3,372	8,012	7,987
Net trading income	16,778	–12,019	10,327	24,861	–19,589
General administrative expenses	–62,196	–64,383	–56,961	–66,614	–64,740
Other operating result	–20,352	–3,422	91,884	–1,170	1,947
Income from financial investments	17,244	–24,274	–47,754	20,053	–29,912
Income from companies measured at equity	–127,863	–71	–65,209	–953	–60,075
Income from discontinued operation	0	0	0	0	15,308
Result for the period before taxes	–129,856	**–59,824**	**–332**	**–20,073**	**–56,636**
Income taxes	952	2,899	–25,119	27,902	–2,872
Result for the period after taxes	–128,903	**–56,925**	**–25,451**	**7,829**	**–59,508**
Result attributable to shareholders of the parent company	–142,487	**–60,526**	**–33,204**	**1,503**	**–66,142**
Result attributable to non-controlling interest	13,583	3,601	7,753	6,325	6,634

STATEMENT OF ALL LEGAL REPRESENTATIVES

We confirm to the best of our knowledge that the condensed half year financial statement gives a true and fair view of the assets, liabilities, financial position and profit or loss of the Group as required by the applicable accounting standards and that the Group management report gives a true and fair view of important events that have occurred during the first six months of the financial year and their impact on the condensed half year financial statements and of the principal risks and uncertainties for the remaining six months of the financial year.

Vienna, 26 August 2014

Stephan Koren
Chairman of the Managing Board
Corporate Planning & Finance, Steering,
Legal & Compliance, HR Management,
Marketing & Communication

Michael Mendel
Deputy Chairman of the Managing Board
Risk management

Rainer Borns
Member of the Managing Board
Association of Volksbanks
Organisation/ IT

Christoph Raninger
Member of the Managing Board
Market
Financial Markets & Group Treasury
Strategy & Capital Measures
Capital Markets, Product & Sales
Commercial Business

REPORT ON THE REVIEW

of the condensed Interim Consolidated Financial Statements

Introduction

We have reviewed the accompanying condensed Interim Consolidated Financial Statements of Österreichische Volksbanken-Aktiengesellschaft, Vienna, for the period from 1 January 2014 to 30 June 2014. These condensed Interim Consolidated Financial Statements comprise the condensed consolidated statement of financial position as of 30 June 2014 and the condensed consolidated statement of comprehensive income, the condensed consolidated statements of cash flow and condensed consolidated statement of changes in equity for the period from 1 January 2014 to 30 June 2014 and the condensed notes, summarizing the significant accounting policies and other explanatory notes.

Management is responsible for the preparation of the condensed Interim Consolidated Financial Statements in accordance with International Financial Reporting Standards (IFRS's) for Interim Reporting (IAS 34) as adopted by the EU.

Our responsibility is to express a conclusion on these condensed Interim Consolidated Financial Statements. Our liability towards the Company and towards third parties is limited in accordance with § 275 par 2 of the Austrian Commercial Code (UGB).

Scope of review

We conducted our review in accordance with Austrian Standards for Chartered Accountants, in particular in compliance with KFS/PG 11 "Principles of Engagements to Review Financial Statements", and with the International Standard on Review Engagements (ISRE 2410) "Review of Interim Financial Information Performed by the Independent Auditor of the Entity". A review of interim financial statements is limited primarily to making inquiries, primarily of Company personnel, responsible for financial and accounting matters as well as for risk management, and applying analytical and other review procedures. A review is substantially less in scope than an audit conducted in accordance with Austrian Standards on Auditing and/or International Standards on Auditing and consequently does not enable us to obtain assurance that we would become aware of all significant matters that might be identified in an audit. Accordingly, we do not express an audit opinion.

Conclusion

Based on our review, nothing came to our attention that causes us to believe that the accompanying condensed Interim Consolidated Financial Statements are not prepared in all material respects in accordance with International Financial Reporting Standards (IFRS's) for Interim Reporting (IAS 34) as adopted by the EU.

Without qualifying our conclusion of our review of the condensed Interim Consolidated Financial Statements, we refer to the disclosures made by the Management in the condensed notes relating to the Company's ability to continue as a going concern, in particular to the disclosures relating to meet the regulatory capital requirements as well as to the assessment of the existing refinancing facilities for Volksbank Romania S.A.

Statement on the consolidated interim management report for the 6 month period ended 30 June 2014 and on management's statement in accordance with § 87 Austrian Stock Exchange Act (BörseG)

We have read the consolidated interim management report and evaluated whether it does not contain any apparent inconsistencies with the condensed Interim Consolidated Financial Statements. Based on our evaluation, the consolidated interim management report does not contain any apparent inconsistencies with the condensed Interim Consolidated Financial Statements.

The interim financial information contains the statement by management in accordance with § 87 par 1 subsection 3 Austrian Stock Exchange Act.

Vienna, 26 August 2014

KPMG Austria GmbH
Wirtschaftsprüfungs- und Steuerberatungsgesellschaft

signed by:

Martin Wagner Austrian Chartered Accountant	Walter Reiffenstuhl Austrian Chartered Accountant

This report is a translation of the original report in German, which is solely valid.