

B. GROUP MANAGEMENT REPORT

B.1 ORGANISATION



A. INTRODUCTION

B. GROUP MANAGEMENT
REPORTC. CONSOLIDATED
FINANCIAL STATEMENTSD. CORPORATE
GOVERNANCE

E. OTHER INFORMATION

We are a leading nationwide residential real estate developer in Germany¹. We develop modern, urban, multifamily residential properties and redevelop existing buildings for residential use. As of 31 December 2017, our project portfolio comprised 45 development projects with an aggregate expected sales volume for fully developed projects of more than €3.4 billion. As of that date, approximately 91% of our portfolio (by expected sales volume for fully developed projects) were located in Germany's key metropolitan regions (Berlin, Bonn, Cologne, Düsseldorf, Frankfurt am Main, Hamburg, Leipzig, Munich and Stuttgart) and 9% in other prospering medium-sized cities. Our purchaser groups are owner-occupiers, retail buy-to-let investors and institutional investors.

We are one of only a few pure play residential real estate developers in Germany with operations spanning the entire development value chain other than actual construction. We operate through a fully integrated nationwide platform covering the acquisition of land, land development, concept design, construction management, as well as marketing and sales. Headquartered in Essen, we also operate through seven branches in Berlin, Cologne, Frankfurt am Main, Hamburg, Leipzig, Munich and Stuttgart. Each branch has its own local teams for acquisition, planning, construction management and marketing and sales activities, while strategic decisions are coordinated

and managed together with our headquarters. We have strong risk management processes in place and apply sophisticated reporting and planning tools to mitigate development risks. The German Real Estate Agent and Commercial Contractor Regulation (Makler- und Bauträgerverordnung (MaBV)) enables us to contractually agree on significant fixed down payments based on construction milestones for residential units sold to owner-occupiers and retail buy-to-let investors which substantially reduces our development risk.

The strong backlog of current projects reflects the high level of investment activities from 2015 to 2017, in which land plots and properties were acquired with an aggregate expected sales volume for fully developed projects of €506 million, €974 million (including €48 million attributable to the acquisition of GRK-Holding GmbH (today Instone Real Estate Leipzig GmbH)) in 2016 and €879 million in 2015, respectively. This high level of investment activity followed a less active acquisition phase in 2014, while Instone Real Estate Development GmbH was still under the control of Hochtief Solutions AG, in which land plots or properties were acquired with an aggregate expected sales volume for fully developed projects of €223 million.

Our core business originates from Hochtief Solutions AG's real estate development division. In 2013, Hochtief

¹ | Selected residential property developers in so-called A-category cities, in 2017

Solutions AG contributed its development division into a separate entity, formart GmbH & Co. KG. In 2014, formart GmbH & Co. KG, which has since been renamed and converted into Instone Real Estate Development GmbH, was acquired by the Company. In 2015, the Company acquired the former GRK-Holding GmbH, which has since been renamed into Instone Real Estate Leipzig GmbH, a real estate developer specialised in the redevelopment of listed buildings for residential use. In June 2017, Instone Real Estate Development GmbH and Instone Real Estate Leipzig GmbH were integrated within Instone Real Estate Group N.V., which serves as holding company of the Group.

The Management Board of Instone Real Estate Group N.V.:

Kruno Crepulja (CEO, 46)

Kruno Crepulja is Chairman of the Management Board/ CEO of Instone Real Estate Group N.V. At the same time, he is CEO of Instone Real Estate Development GmbH. As its Chief Executive Officer, he is in charge of strategy, project service, purchasing, corporate communications and business development.

Oliver Schmitt (CFO, 53)

Oliver Schmitt is Member of the Management Board/ CFO of Instone Real Estate Group N.V. At the same time, he is CFO of Instone Real Estate Development GmbH. In his position as the Chief Financial Officer he is tasked with commercial project management, human resources, financing, finance and accounting, taxation, law, IT and corporate control.

Andreas Gräf (CDO, 51)

Andreas Gräf is member of the Management Board/CDO of Instone Real Estate Group N.V. At the same time, he is COO of Instone Real Estate Development GmbH for the branches Northrhine-Westphalia and Rhine-Main. He has been working in the construction and real estate sector for 30 years.

Manfred Torsten Kracht (CSO, 50)

Manfred Torsten Kracht is member of the Management Board/CSO of Instone Real Estate Group N.V. At the same time, he is Managing Director of Instone Real Estate Leipzig GmbH. As a member of the Management Board of Instone Real Estate's predecessor, GRK-Holding GmbH, Leipzig, he had been in charge of sales and project development since 2006 and assumed the management of Instone Real Estate Leipzig GmbH in 2016.

Former members of the Management Board:

Robert Victor van Beemen, trust lawyer, Managing Director of Instone Real Estate Group N.V. (from April 2014 to June 2017)

Stefan Mohr, Head of Corporate Real Estate at ActivumSG Advisory GmbH, Managing Director of Instone Real Estate Group N.V. (from April 2015 to June 2017) and member of the supervisory board of the Company (from February 2018 to date).

We are aware of the fact that women are underrepresented on the Management Board of Instone Real Estate Group N.V. and have been over the past years. The Management Board of Instone Real Estate Group N.V. was newly formed in 2017 with members of the Management Board from the two subsidiaries.

We will take this into account when appointing individuals to chief managerial positions in the future. Instone Real Estate will make a serious effort to achieve the goals as prescribed by Dutch law regarding equality for men and women on the Management Board in the years to come. The same applies to the composition of the Supervisory Board of Instone Real Estate Group N.V., which was established in February 2018.

Instone Real Estate specifically promotes female employees through training and further education and through special working time models for equal opportunities in order to accommodate more women on management levels.

B.2 STRATEGY

The strategy of Instone is to create additional value for its project portfolio and to keep and further strengthen the Company's competitive position in the German residential real estate development market. To achieve this, the Company will leverage its strong platform and deep market knowledge and expand its competitive position in the German residential development sector. Also, Instone aims to fuel further growth through the realisation of growth opportunities, among others in Germany's key metropolitan regions, for which Instone expects further growth potential. Instone intends to achieve this as follows:

B.2.1 MAINTAIN AND EXPAND ITS COMPETITIVE POSITION IN THE GERMAN RESIDENTIAL DEVELOPMENT SECTOR WITH A CONTINUED FOCUS ON GERMANY'S KEY METROPOLITAN REGIONS.

Instone Real Estate's exclusive focus on modern urban mid-rise residential properties and their location in Germany's key metropolitan regions and other prospering medium-sized cities in Germany has been a key contributing factor to Instone Real Estate's success in the past. Its regional approach is driven by Germany's attractive growth markets (North Rhine-Westphalia and Rhine Main, Baden-Wuerttemberg and Bavaria, Saxony, as well as Northern and Eastern Germany) with four regional heads and seven branches.

Instone aims to continue to focus on, and seeks to strengthen its presence in, metropolitan growth regions in Germany (Berlin, Bonn, Cologne, Dusseldorf, Frankfurt am Main, Hamburg, Leipzig, Munich and Stuttgart) as well as on other prospering medium-sized cities such as Darmstadt, Dresden, Freiburg, Hanover, Heidelberg, Heilbronn, Karlsruhe, Mainz, Mannheim, Potsdam, Ulm and Wiesbaden. These metropolitan regions and prospering medium-sized cities present strong demographic growth, reinforced by the urbanisation trend, sustainable household formation and supportive regionally diversified economic backgrounds.

In addition, Instone is also aiming to invest with an opportunistic approach in particularly attractive areas that are

likely to benefit from incidental demand, such as Aachen, Augsburg, Baden-Baden, Erfurt, Ingolstadt, Halle, Kiel, Nuremberg, the Rhine-Main region around Frankfurt am Main, Regensburg, the Western Ruhr area, and Wurzburg.

B.2.2 FOCUS ON LAND PLOTS OR PROPERTIES WITHOUT ZONING OR PLANNING PERMISSION FOR RESIDENTIAL DEVELOPMENT PURPOSES AT THE TIME OF ACQUISITION.

The acquisition strategy of Instone Real Estate is driven by the aim to achieve attractive margins from project developments without taking undue risks. To this end, Instone Real Estate land acquisition strategy focuses primarily on land plots or properties without zoning or planning permission for residential development purposes at the time of acquisition, as it believes that such plots or properties typically offer a higher potential for value creation and less competition than land plots or properties with full zoning and planning permission. To manage regulatory development risk, Instone relies on its know-how and expertise to ensure it has a thorough understanding of remaining planning issues and only acquires land plots or properties that it considers highly likely to be granted the required planning permission in the near future, generally following pre-discussions with local building authorities. Accordingly, Instone does not invest in land if it does not believe it will be able to obtain zoning or planning permission within this time frame (no speculative land banking). Instone also seeks to avoid acquiring land to the extent it believes the purchase price already includes a step-up in value for future building permission.

Instone Real Estate has an excellent track record in developing land plots or properties without zoning or planning permission for residential development purposes at the time of acquisition, having successfully obtained zoning and planning permission for 100% of the land plots or properties for which it has submitted an application in the period from 1 January 2015 through 31 December 2017.

In accordance with its acquisition criteria, Instone constantly aims to identify opportunities to acquire land plots

or properties in Germany's key metropolitan regions by remaining close to the local markets through its seven branches. It focuses on the key German metropolitan residential markets while likewise reviewing other large and liquid markets that are also of interest for private and institutional investors.

KEY PERFORMANCE INDICATORS OF INSTONE REAL ESTATE

Volume of sales contracts

The volume of sales contracts covers all sales-related transactions such as notarised sales contracts and individual orders from customers, supplemented by rental income.

Operating performance

Revenue and changes in inventories make up the operating performance of Instone Real Estate.

Earnings before tax (EBT)

Instone Real Estate establishes the earnings before tax in accordance with the International Financial Reporting Standards as adopted in the EU (IFRS).

Volume of new internal acquisition permits

The volume of new internal acquisition permits for Instone Real Estate is seen as an indicator for the trend of the future business volume – expressed in revenue.

B.3 SUSTAINABILITY

Sustainable properties create long-term added value for investors, owners, users as well as developers. Sustainable action implies the consideration of ecological, social and economic aspects during the development of a property. The creation, erection, use and management of a building cause greenhouse gas emissions. Sustainable properties are economically efficient as well as environmentally-friendly as they preserve resources in the long run. It is our goal to create an optimal living environment which provides comfortable, healthy surroundings to our customers.

Instone Real Estate develops, builds, revitalises and markets residential real estate and city districts in Germany's growth regions. The properties and city districts on the one hand meet the needs of residents while on the other they are fulfilling complex technical requirements. Thanks to new technologies and digital progress, Instone Real Estate properties provide an attractive infrastructure and a high quality of use. This helps to accomplish a long-term acceptance of new and revitalised properties in inner-city locations.

In line with the core values of sustainability which include the re-use, secondary use and extension of the life cycle within a suitable time frame, we develop and restore listed buildings. We revitalise Gründerzeit architecture and repurpose special real estate.

For us as equal public-sector partner, this sustainable real estate development includes the conceptualisation of building rights for complex properties. This comprises the realisation of modern city residences, the construction of complete residential areas or residential complexes with a high share of barrier-free residential units plus the consideration of subsidised and low-rent residences.

The early commitment between Instone Real Estate and municipalities and organisations to the sustainable development of zoning and land use plans as well as to the shaping of urban development contracts guarantees optimal results.

As a matter of fact, in developing our old and new properties we comply with current energy-saving regulations, as

we are striving to keep the consumption of energy both low during the construction and the later operation of the buildings. This results in low operating expenses.

Instone Real Estate is a member of relevant associations of the real estate industry, including the Zentraler Immobilien Ausschuss (ZIA) and the Bundesverband Freier Immobilien- und Wohnungsunternehmen (bfw). Furthermore, Instone Real Estate is involved in different committees that aim to positively influence shared regulations in Germany, including those regarding sustainable property. We also regularly participate in market analyses and conduct customer surveys to adapt our residential properties to the needs of potential owners and users.

In intensive meetings, we advise our customers on decoration options and technical solutions. Our aim is to create flexible living space that encompasses all target groups. This is why the residential units and living forms developed by Instone Real Estate in both new and restored pre-war buildings are always at least low-barrier solutions, if not barrier-free solutions.

B.4 STAFF

As at 31 December 2017, Instone Real Estate employed a total of 301 staff compared to 292 in the previous year, including the team members of its foreign subsidiaries.

The international locations employed two employees in Luxembourg and one in Vienna (as at 31 December 2017). The number of staff remained unchanged as expected, respectively with two withdrawals in Austria. During the previous years 2014 and 2015, restructuring activities at both locations had preceded, which led to a noticeable reduction of personnel.

B.5 NET ASSETS, FINANCIAL POSITION AND RESULTS OF OPERATIONS

The consolidated financial statements of Instone Real Estate Group N.V. for the year 2017 were influenced by effects resulting from the expansion of the scope of consolidation in prior years. The Group division formart GmbH & Co KG, Essen, Germany, which operates today as Instone Real Estate Development GmbH, was consolidated for the first time on 1 October 2014. This consolidation led to the formation of Instone Real Estate Group N.V. as a group. The Group division GRK-Holding GmbH, Leipzig, Germany, which operates today as Instone Real Estate Leipzig GmbH, was included in the consolidated financial statements for the first time on 31 December 2015.

B.5.1 NET ASSETS

The **total assets** of Instone Real Estate rose to €789.1 million (31 December 2016: €685.2 million). This was primarily due to the increase of **inventories** to €659.4 million (84%) from €542.7 million (79%) as at 31 December 2016. Inventories essentially include unfinished products from ongoing project developments, the share of which grew to €659.4 million in 2017 compared to €537.6 million in the previous year. Finished products were valued at €0.1 million (31 December 2016: €5.1 million). The decrease is due to the sale and subsequent handover of finished condominiums. Existing **trade receivables** for the year under review were down to €4.2 million (31 December 2016: €19.6 million) as the projects accounted for using the percentage of completion (PoC method) were almost totally handed over to the customer in 2017.

Due to the first-time consolidation of Instone Real Estate Development GmbH in 2014 and Instone Real Estate Leipzig GmbH in 2015, inventories as of 31 December 2017 still included €50.5 million (31 December 2016: €71.9 million) step-ups from the purchase price allocations. Based on our current assumptions, we assume that these effects will expire in 2022.

Total inventories minus received upfront payments increased from €381.2 million to €429.0 million during the year under review. This was primarily due to a higher increase in inventories by €116.8 million compared to the €68.8 million increase of received upfront payments.

The capitalised work done to the inventories was partially higher than the received upfront payments. This was due to the restrictions of German law which does not allow to receive the customer payments earlier than the construction is in line. Accordingly, the financing of inventories by upfront payments received deteriorated slightly.

The **equity-method investments**, which include shareholdings in project companies, dropped from €1.4 million to €0.4 million in the financial year 2017. The decrease was due to the dividend pay-out by Projektentwicklungsgesellschaft Holbeinviertel mbH & Co. KG, Frankfurt am Main, in 2017.

The **non-current financial receivables** included a loan from the Group company west.side gmbH, Bonn, to the co-shareholder Dresdner Handel und Beratungsgesellschaft mbH, Dresden, valued at €0.7 million (31 December 2016: €0.7 million).

The **current financial receivables** of €32.4 million (prior year: €0.2 million) resulted in receivables to associated companies. These included €32.3 million receivables to the majority shareholders for the indemnity of other operating expenses and personnel costs relating to the planned private placement and the Company's listing on the Frankfurt Stock Exchange. These receivables were based on a cost-sharing and indemnity agreement and an indemnification agreement.

Other receivables and other assets (current) rose from €5.6 million to €15.5 million in 2017. In the year under review, other receivables were accounted relating to a tax indemnification of €2.8 million by Hochtief Solutions AG, Essen, Germany, capitalised transaction costs of €2.5 million, €1.7 million receivables from a sale of voting rights of a subsidiary in amount and bails as contract performance guarantee of €1.0 million. The comprised contingent items grew from €0.8 million to €2.3 million for upfront payments on land where the transfer of use and encumbrances occurred after the individual balance sheet date. Moreover, changes to already paid arrangement fees which were spread over the term of the €2.5 million loans in the financial year 2017 (31 December 2016: €0.5 million) contributed to the volatility of other receivables and other assets. Also, the

rise of tax receivables from €2.8 million to €3.2 million in 2017 was essentially the result of refund claims in connection with the German Value Added Tax Act (Section 13b) (Umsatzsteuergesetz). These items were largely responsible for the fluctuations over the financial years.

Cash and cash equivalents declined from €112.5 million in 2016 to €73.6 million in the financial year 2017, which was mainly the result of a cash outflow for the investment in new land for project development. We refer to the consolidated statement of cash flows.

Non-current provisions for pensions and similar obligations increased slightly by €0.1 million to €4.2 million in 2017. The values for provisions resulted from offsetting the plan assets of €5.6 million (31 December 2016: €5.4 million). Plan assets of €5.0 million (31 December 2016: €4.9 million) were placed in a trustee deposit with Helaba Pension Trust e. V., Frankfurt am Main, and €0.6 million (31 December 2016: €0.6 million) in a trustee deposit with the European Bank for Financial Services GmbH (ebase®), Aschheim.

The **remaining other non-current provisions** for the year under review decreased from €12.4 million to €1.3 million in 2017. This was a result of personnel-related provisions which went down from €11.7 million in 2016 to €0.7 million in 2017. The reason for this was essentially the transition of maturity of the liabilities for special payments in connection with a long-term incentive scheme to the current provisions.

Other current provisions for the year under review increased by €22.6 million – from €25.6 million at 31 December 2016 to €49.2 million. This was primarily due to the transition of maturity of the liabilities for payments in connection with a long-term incentive scheme from the €11.1 million non-current provisions, the increase in current personnel-related provisions by €17.0 million and a decrease by €5.5 million in other current provisions mainly due to project-related provisions for warranty risks and litigation risks.

Non-current financial liabilities for the financial year 2017 were reduced to €241.0 million (31 December 2016:

€300.9 million). €48.0 million of the liabilities towards the shareholders of Instone Real Estate Group N.V. were converted into equity in 2017. During the year 2017, interests were capitalised, so that at the end of 2017, the liabilities to shareholders still amounted to €57.8 million (31 December 2016: €96.6 million). Instone Real Estate Development GmbH was able to sustainably improve its liquidity by first-time placement of a promissory note loan worth €66.9 million. The non-current financial liabilities to banks for project related financing decreased during the reporting year.

The non-current financial liabilities as at 31 December 2016 had included a €52.4 million financial liability relating to a mezzanine financing. This facility was fully repaid to the lender in the year under review, and Instone Real Estate was able to sustainably lower its interest burden through its early repayment.

The **current financial liabilities** grew to €134.7 million (31 December 2016: €81.6 million). The increase of the current financial liabilities by €53.1 million was mainly due to two effects: Within an amount of €88.9 million new project-related loans from banks were taken over and €21.5 million liabilities for the call and put option for the shares in Instone Real Estate Development GmbH at 31 December 2016 were fully redeemed in the year under review.

The financing of a special project constituted a crucial component of other current financial liabilities, which were valued €12.5 million at 31 December 2016 and were fully redeemed in the year under review.

Trade payables increased to €275.7 million in the financial year 2017 (31 December 2016: €215.2 million). This was primarily due to the capitalisation of the upfront payments. These amounted to €230.4 million received for new sales of condominiums or further instalments according to the ongoing construction of sold condominiums that were attributed as inventories.

The first-time consolidation of Instone Real Estate Development GmbH in the financial year 2014 and the first-time consolidation of Instone Real Estate Leipzig GmbH in the financial year 2015 had essentially generated

deferred tax liabilities on newly-valued inventories.

Mainly due to this effect the deferred tax liabilities as at 31 December 2017 fell to €7.7 million from €23.4 million in the previous year. They included deferred tax liabilities generated by the development of step-up effects on inventories of €17.0 million (31 December 2016: €23.9 million).

The Income tax liabilities increased to €13.8 million (31 December 2016: 6.2 million) due to the income taxes on increased profits of the German group entities.

The **equity ratio** as at 31 December 2017 was 6.6% (31 December 2016: 0.4%). The clear increase in 2017 was at first due to the €48.0 million shareholder loan conversion into equity from 28 December 2017. Second, it was owed to the contribution from shareholders in equity of €32.3 million by the cost-sharing and indemnification agreements from shareholders in favour of Instone Real Estate Group N.V. These were entered for the indemnity of other operating expenses and personnel costs relating to the planned private placement and the Company's listing on the Frankfurt Stock Exchange. Third, neutral changes in equity were the result of the actuarial gains and losses from defined benefit plans in the amount of €0.9 million (31 December 2016: €-1.2 million). In contrast to these positive effects equity was influenced by the negative overall result of €31.0 million in the year under review. The shareholdings of other shareholders decreased by €0.5 million compared to the previous year. The decrease was connected to the dividend pay-out of GRK REVION Hamburg GmbH, Leipzig, Germany which had already been fully consolidated in the previous year.

B.5.2 FINANCIAL POSITION

The cash flow of Instone Real Estate in the financial year 2017 was essentially affected by cash outflow for investments in new project developments, which were opposed by inflows after entering into new financing contracts. As in previous years, outgoing payments for the acquisition of the two Group divisions had impact on the cash flow, combined with the realignment of the financing structure of Instone Real Estate.

In 2017, Instone Real Estate continued to expand its project development business by investing in new land plots and simultaneously, the scope of financing for bank loans increased to €664.6 million (31 December 2016: €334.7 million). This new project financing and the €66.9 million first-time placement of a promissory note by Instone Real Estate Development GmbH increased liabilities to €317.4 million (31 December 2016: €197.2 million).

The capital structure of Instone Real Estate as at 31 December 2017 was defined by a 6.6% equity ratio (31 December 2016: 0.4%). However, the non-current financial liabilities contained liabilities towards shareholders valued at €57.8 million (31 December 2016: €96.6 million). This corresponded to a 13.9% share (31 December 2016: 14.5%) in the balance sheet total.

As part of the placement of the promissory note by Instone Real Estate Development GmbH, we were able to raise various loan tranches of credit institutions. The maturity structure of the individual tranches was as follows:

in € million	2017
Due to 31.12.2020	47.0
Due to 31.12.2022	19.9

Debt financing drawn from financial institutions to finance projects increased to €250.5 million (31 December 2016: €209.7 million (including mezzanine financing)). The ongoing cash inflow from our project developments reduced this item constantly, providing sufficient flexibility to procure additional debt capital – for example, for the acquisition of land.

Cash flow from financing activities rose to €18.2 million in the financial year 2017 (2016: €8.5 million), which was primarily due to inpayments relating to new borrowings. These exceeded the outpayments from repayments and the outpayments for interest.

Payments due for project-related financing are shown in the following table:

in € million	2017	2016
Due to 31.12.2018 (2016: due to 31.12.2017)	134.2	57.8
Due to 31.12.2019 (2016: due to 31.12.2018)	61.7	109.3
Due to 31.12.2020 (2016: due to 31.12.2019)	10.3	42.6

The individual project-related financing of Instone Real Estate was negotiated with multiple financial institutions and was subject to varying terms and conditions. For a draw-down of funds under fixed-rate loans or term loans, different amounts and frequencies have been agreed. The 2017 interest rate conditions were at the level of the previous year.

Funds required at short notice can be procured using overdraft facilities that have been agreed with the individual banks. To compensate for interest, any payments already received go to these overdraft facilities which the purchasers of our properties pay into separately managed omnibus accounts dedicated to purchase price payments. If required, these overdraft facilities can be converted into fixed-rate loans or term loans.

The **cash flow from investing activities** in the financial year 2017 sank slightly to a cash outflow of €22.7 million (2016: cash outflow of €21.8 million). It was in principle defined by the exercise of the third tranche of the call and put option by the former controlling shareholder of Instone Real Estate Development GmbH, Hochtief Solutions AG. It led to a cash outflow of €22.5 million.

During the year under review, we invested €0.5 million (2016: €0.4 million) in property, plant and equipment. The key investments were technical and other office equipment.

The **net cash flow from operating activities** of Instone Real Estate of €-34.5 million in the financial year 2017

(2016: €87.7 million) was characterised by the increase in cash outflow from new investing in land for project developments: The increase in inventories of unfinished products as well as the decrease in the volume of receivables resulted in an aggregate cash outflow of €106.5 million in the year under review (2016: €41.5 million). This resulted from investments in land as well as project-related activities in 2017 and in previous years.

The inflow of upfront payments of €68.8 million had a positive effect on the cash flow from operating activities in the financial year 2017.

The depreciation of fixed assets of €0.4 million (2016: €0.4 million), the increase of provisions by €12.5 million from €15.0 million in 2016, the decrease of deferred tax liabilities and increase of deferred tax assets by €15.7 million from €12.9 million in 2016 and the increase of revaluations of interest held at equity by €1.0 million (2016: €-1.3 million) in the financial year 2017 were cash neutral. Non-cash expenditures in connection with the consolidation of the subsidiaries increased cash flow from operating activities in the financial year 2017 by €31.2 million (2016: €23.5 million).

As at 31 December 2017, financial resources had decreased to €73.6 million (2016: €112.5 million). This included resources that were not related to the ongoing financing (free cash) in the total amount of €58.7 million (2016: €91.1 million).

Following the successful extension of certain guarantee facility agreements with renowned credit insurers, financing for Instone Real Estate was further secured and diversified.

As at 31 December 2017, a €185.2 million surety line of insurances was available (2016: €185.0 million). An amount of €99.4 million was drawn under such a surety line (2016: €102.7 million). This provided flexibility for further investments in the financial year 2018. Project-related financing agreements supplied further €16.7 million surety volumes (2016: €137.8 million), of which €1.4 million (2016: €2.3 million) was being used as at 31 December 2017.

B.5.3 RESULTS OF OPERATIONS

For the financial year 2017, the operating performance of Instone Real Estate decreased to €319.9 million (2016: €362.5 million). Due to a decline in construction work for project developments, the cost of materials went down to €244.8 million (2016: €293.7 million). This corresponded to 76.5% of the operating performance (2016: 81.0%). In the year under review, changes in inventories were lower than in the previous year due to deliveries of products to customers. The production costs of projects under construction have only partially compensated for this reduction as fewer projects are under construction. The operating performance in 2017 was negatively affected by the amortisation of the step-up of the purchase price allocation of Instone Real Estate Development GmbH and Instone Real Estate Leipzig GmbH in the amount of €23.1 million (2016: €49.9 million).

The decrease of cost of materials in 2017 by €48.9 million to €244.8 million (2016: €293.7 million) corresponded mainly to the decrease of the consolidated operating performance. This decrease was due to a decline in construction work for multi-annual project developments compared to the previous year.

Staff costs increased by €14.3 million to €49.5 million in 2017 (2016: €35.2 million). This increase was primarily due to expenses for payments in connection with a long-term incentive scheme in the financial year 2017.

Other operating income of €5.4 million (2016: €8.3 million) essentially included the one-off refund for the sale of voting rights and for a better fortunes clause – in total €2.7 million (2016: €0.0 million) – as well as €0.9 million income from the reduction of impairment and the reversal of provisions (2016: €1.4 million).

Other operating expenses of €41.5 million (2016: €42.4 million) decreased slightly by €0.9 million. The reduction of commission fees and other distribution costs by €5.7 million was primarily the result of the lower volume of sales contracts in 2017. This effect was partially offset both by the €4.0 million rise in business consulting, attorneys' and notaries' fees mainly relating to the planned private

placement and the Company's listing on the Frankfurt Stock Exchange and other overhead costs.

In 2017, the result from €0.2 million equity-method investments (2016: €1.3 million) included the €0.9 million decrease in value of Projektentwicklungsgesellschaft Holbeinviertel mbH & Co. KG, Frankfurt am Main (2016: increase of €1.4 million).

From the effects shown, essentially due to the higher staff costs, the consolidated result of operating activities (EBITDA) in the financial year 2017 declined significantly by €11.7 million and resulted in a loss of €10.4 million (2016: profit of €1.3 million).

The 2017 financial result improved to €-20.4 million (2016: €-24.8 million). A decisive contributing factor was the reduction of interest costs by €3.7 million. Further improvement in the financial result is attributable to an increase in interest income and reductions in interest components from the increase in provisions.

As at 31 December 2017, earnings before tax resulted in a loss of €31.2 million (2016: loss of 24.0 million). This higher loss compared to the previous year is mainly due to the higher staff costs for payments in connection with a long-term incentive scheme. The lower financing costs as well as the lower balance of operating performance and cost of materials could partly mitigate this effect.

In the financial year 2017, €0.2 million tax income (2016: €1.8 million) slightly improved the consolidated result. The release of deferred tax liabilities mainly due to the write-down of the revaluation of inventories from the first-time consolidation of Instone Real Estate Development GmbH and Instone Real Estate Leipzig GmbH resulted in a profit of €15.3 million (2016: €12.6 million). This was offset by €15.1 million expenses from corporate income taxes and trade taxes (2016: €10.8 million) due to the taxation of the higher positive results in the subsidiaries.

Earnings after tax of Instone Real Estate totalled €-31.0 million (2016: €-22.2 million); due to the effects shown, they were significantly lower than in the previous year mainly to the higher staff costs.

The impact on equity by the 2017 loss of €31.0 million was offset by the contribution from shareholders in equity with a profit of €32.3 million by the cost-sharing and indemnification agreements from shareholders in favour of Instone Real Estate Group N.V.

B.5.4 OTHER FINANCIAL PERFORMANCE INDICATORS

In 2017, volume of sales contracts decreased to €359.1 million (2016: €519.3 million), the number of sales contracts including residential units sank to 826 (2016: 1,129). This decrease was justified by a postponement of sales launches and of two block sales.

For the year under review, Instone Real Estate generated a total amount of revenue and changes in inventories worth €319.9 million (2016: €362.5 million) – including a €94.8 million share for land plot purchases (2016: €127.8 million); therefore €225.1 million (2016: €234.7 million) were attributed to project implementation.

The volume of newly internal acquisition permits reached €506.1 million in 2017 (2016: €878.9 million). This led to a project portfolio corresponding to an aggregate expected sales volume of €3.4 billion as at 31 December 2017.

B.6 RISK REPORT

The risk policy of Instone Real Estate has the aim of advancing the Group's successful development and profitability in the long term. Our sophisticated risk management system is key to achieving this goal. It employs proactive risk control to minimise potential impacts.

B.6.1 RISK MANAGEMENT SYSTEM

Instone Real Estate has installed a risk management system which identifies potential risks, assesses the risks identified and mitigates these. This particularly applies to risks whose effects could jeopardise the continued existence of Instone Real Estate as a going concern. We continued to apply our proven risk management system throughout the financial year 2017. Moreover, we extended the risk management system to include the Instone Real Estate Leipzig GmbH (formerly GRK-Holding GmbH). In general, the aim of the Group is to recognise risks and secure them at an early stage. However, some industry-standard risks (i.e. risks of delay in permission of building rights) must be taken that can not be secured. Their successful handling in the past has given the Group advantages over competitors.

Together with external partners we continue to work towards optimising this system. All applicable internal regulations, rules of procedure and arrangements that vouch for a Group-wide standard, structured approach to risks are regularly subjected to an internal review. In 2017, for example, we continued with the evaluation of all applicable internal regulations. This review and evaluation is an ongoing and continuous process. In 2017, we also completely revised some of the Company's guidelines. Moreover, based on the rules of procedure for the Management Board of Instone Real Estate – and taking into consideration current laws and relevant case law – we further developed the decision-making policy that applies to the entire Group. This essentially governs the material process flows and decision-making approvals within the entire Group that are subject to approval.

Central risk-controlling elements include internal approval processes for critical decisions, and the dual-control principle. The powers of the individual decision-making levels

are clearly defined by the policies on decision-making. For example, each new project, including the date of its sales start, must be approved by the Management Board. Beforehand, Instone Real Estate's acquisition projects must undergo an intensive selection process which always also involves the Management Board. Upon release of the project, requirements specific to the project are automatically issued to mitigate risks. Material changes or digressions of the projects from approved specifications or parameters must be laid out in detail and are discussed during the scheduled monthly forecast and results meetings with the Management Board.

We raise and evaluate opportunities and risks at project level monthly and summarise them in reports. This constitutes the foundation on which talks are held each month within the project team, as well as forecast and results discussions with the Management Board. All risks related to approved projects as well as tied to imminent acquisitions and the respective measures to mitigate risks are defined during these meetings.

During the financial year 2017, the Compliance System which was developed in 2015 and was specifically tailored to the needs of Instone Real Estate, was driven forward. It explicitly targets the Company's risk fields that are the direct result of developing residential property. It provides additional support to our employees in handling laws, regulations, decrees and other requirements. For the first time we used an eLearning system in 2017 to train our employees in compliance and data protection. This system enables us to provide our employees with current general and task-specific information.

The Compliance System was expanded in the beginning of 2018 in preparation for the private placement and the Listing on Frankfurt Stock Exchange. Among other things, an internal compliance hotline has been set up where employees can anonymously address any violations or grievances at Instone. Furthermore, an organisational structure for ad hoc announcements and other information requiring disclosure was implemented in order to meet the requirements of capital market compliance, in particular to fulfil the post-admission obligations which apply to the Company since the listing of its shares.

We believe that our overall risk management system (as discussed above and in chapters B.6.2, B.6.3 and C.2.4 of this report) also encompassed, and sufficiently safeguarded the integrity of, our financial reporting. However, during the fiscal year ended 31 December 2017, we did not have a specific formal risk management and control system relating to the process of financial reporting by the Company and our subsidiaries whose financial information is included in our consolidated financial statements.

B.6.2 IN-CONTROL AND RESPONSIBILITY STATEMENTS

On the basis of reports and information provided to our Managing Directors, our Management Board is of the opinion that:

- a. this report provides sufficient insight into any failings in the effectiveness of the Company's risk management and control systems;
- b. the Company's risk management and control systems provide reasonable assurance that the Company's financial reporting does not contain material inaccuracies;
- c. based on the Company's state of affairs as at the date of this report, it is justified that the Company's financial reporting is prepared on a going concern basis; and
- d. this report states those material risks and uncertainties that are relevant to the expectation of the Company's continuity for a period of twelve months after the date of this report.

Furthermore, our Management Board confirms that:

- a. to the best of their knowledge, the statutory annual accounts included in this report give a true and fair view of the assets, liabilities, financial position and profit or loss of the Company and its consolidated subsidiaries taken as a whole; and
- b. this report includes a fair review concerning the financial position, on the balance sheet date, and the

development and performance of the business of the Company and its consolidated subsidiaries as a whole, together with a description of the principal risks and uncertainties that they face.

B.6.3 RISKS

Material threats from Instone Real Estate's operating activities result primarily from potential changes in the market situation:

- revenue risks due to a market-related reduction in demand and any potential-related decline in prices
- revenue risks due to changes in demand implying that the planning concept may no longer adequately cater to market requirements
- cost risks from higher purchase prices (price increases for the contract work)
- cost risks from unplanned costs in relation to the restoration of listed buildings
- interest and financing risks (for example, increase in the level of interest rates)
- performance delivery risks due to delays in applying building rights
- litigations

Additionally, there are potential risks that could be triggered internally:

- cash flow bottlenecks
- loss of knowledge/loss of qualified personnel
- loss of reputation following the integration of the formart and GRK trademarks, into the new umbrella trademark, Instone Real Estate

We deem the revenue risk as result of a decline in demand to be very low under current general market conditions.

Our risk management ensures that during the approval process and sales release procedure for projects, the planned sales proceeds and the speed of marketing activities are critically examined and questioned by the Management Board. By establishing a pre-sales rate, we can test the planned purchase prices and the project development concept on the market. Should this result in either the concept not being accepted by the market or the anticipated sales prices not being achievable, the project undergoes a readjustment and a renewed review. At the same time this allows us to identify and exploit opportunities for increasing the purchase price.

We lower cost risks by entering into long-term partnerships with our subcontractors and retaining contractors as early as possible for key contract work. Moreover, product standards undergo an ongoing development to achieve a very high cost certainty for the individual projects. The Project Service department is tasked with costing for all branches and in doing so can rely on experience gained from all projects throughout Germany. Likewise, we regularly prepare a costing analysis from figures based on experience gathered from projects already implemented, to test the cost approach recurrently. We deem the impact of cost risks at a medium level.

The restoration of listed buildings involves specific risks from unplanned costs. In acquiring the GRK Group in 2015 we gained specific know-how in relation to this on the one hand; on the other, these specific cost risks are included in the context of our project planning and calculation. The impact of this risk is deemed as low.

The projects are financed via bank loans and a proportionate share of equity. The current low level of interest rates makes it possible for us to finance the project's cost effectively. A significant rise in interest rates at short notice is currently not foreseeable. For longer-term projects, we calculate with higher interest rates based on the principle of prudence. To preferably ensure high certainty concerning interest rates for our projects, we ask that banks, at the time of enquiring about the financing of investments, in addition to their financing terms, also provide so-called term sheets, or request completely prepared and arranged financing contracts.

The resulting financing conditions, especially the rate of interest, are taken into consideration in the projects' profitability analyses. For further explanations on how we manage cash flow, interest and default risks, we refer to the explanations in the notes to the consolidated financial statements. As a result and in connection with current market invorimentes, Instone Real Estate assesses the risk as low.

To secure the Company's solvency, we continuously monitor our cash flow based on the individual projects. Even cash flow forecasts of relevant acquisition projects are taken into consideration in the cash flow planning at an early point in time following the prior approval by the Management Board. Instone Real Estate's business model greatly limits default risk. We can recognise potential cash flow bottlenecks at an early stage and avoid these by processing cash flow forecasts from the individual projects, organising the cash flow planning at a higher level and continually monitoring the relevant cash flows.

Other risks concerning our projects, for example vandalism or fire, are insured accordingly (liability insurance, contractor's all risk insurance, insurance against fire during the construction phase). Beyond this, we have taken out additional Group-wide insurance policies to avoid any potential damage for Instone Real Estate.

In order to mitigate performance delivery risks due to delays in applying building rights, Instone Real Estate relies on its strong regional network and expertise for a thorough analysis of remaining zoning or planning issues. The Company only acquires land plots and properties that it considers highly likely to be granted the required planning permission in the near future, generally following pre-discussions with local building authorities. This risk is rated medium.

Instone Real Estate mitigates litigation risks by using standard terms and conditions in the agreements with purchasers, architects, construction companies and using a standard sales contract with its customers. Additionally, potential litigation risks are identified and analysed in accordance with our Group-wide Compliance System. The impact of this risk is evaluated as low for the Group.

The loss of reputation and image following the merger of the formart and GRK trademarks into the new umbrella trademark, Instone Real Estate, has not had any significant impact on our operating activities (as originally assumed). Maintaining the good name was therefore the focus of our interest. The brand launch was therefore accompanied by a broad kick-off campaign. Our 'Gemeinsam geht mehr' (Achieving more together) motto highlights the values of our new umbrella brand. With our powerful new brand, we emphasise the aspects of experience, trust, and fairness.

Additionally, our employees are the flagship of the entire Group and form the link to customers and business partners. The specific targeting and development of qualified personnel helps us to ensure that we always place employees with outstanding training in positions that suit their profile. This is the best approach to developing the image of the Instone Real Estate trademark and to retain sufficiently qualified key personnel. We deem the impact of this risk at a low level.

In summary, this results in a risk sphere that is common for the business field. By reviewing risks early and dealing with them openly, we can act early to mitigate them. The residual risks are minor and do not have any major impact on Instone Real Estate's continued existence.

None of the risks described above influenced the financial position of the financial year 2017 significantly and therefore no remedial measures to the risk management system were necessary. It is not possible to estimate the possible consequences of significant risks that may materialise in the future and that may not be controlled by our risk management system.

B.7 OUTLOOK

Instone is one of the largest housing project developers in Germany (number 2 company in the residential segment according to the bulwiengesa AG project developer study 2017/2018). Its focus is on trading development – i.e. the development of properties intended for sale – as well as condominiums.

Instone has eight locations and realises projects throughout Germany. All target cities defined have a higher-than-average housing demand and a below-average risk in German-wide comparison.

Our current strategy of investing in inner-city and suburban locations of A-cities as well as in other target cities offers good long-term market opportunities. Therefore, we continue to invest in large-scale realisations combined with rental housing construction to develop attractive urban neighborhoods.

In addition to investing in new properties for the project business, we do not plan any significant investments in long-term assets for the year 2018. We also plan to expand our financing activities to include project-related financing. Changes to the company's finances are not planned.

As in previous years, we will not incur any significant expenses for research and development in 2018.

For 2018, we do not expect any significant changes in the number of personnel.

For the financial year 2018, we expect the volume of concluded sales contracts to increase to more than €500 million based on projects available for sale or ready for the start of the marketing phase.

Based on the planned handovers for 2018, we expect an operating performance of more than €500 million and an adjusted EBT between €25 million and €30 million. We expect better operating results for the future as the effects of PPA will not impact future results as much compared to previous years.

B.8 SUPPLEMENTARY REPORT

On 22 January 2018, Instone Real Estate published the press release about the planned listing of its shares on the regulated market of the Frankfurt Stock Exchange (Prime Standard) in 2018. As part of the planned previous private placement, both new and existing shares were planned to be offered. As a result of a capital increase, new shares were planned to be issued with gross proceeds to the Company, and existing shares were planned to be offered by the Company's shareholders, funds launched by ActivumSG Capital Management Limited.

On 13 February 2018, part of the Company's share premium was converted into share capital, thereby increasing the Company's share capital from €8,386.00 to €50,316.00 and, following the effectiveness of the conversion of the Company into a public limited liability company (naamloze vennootschap) and the change of its name which took place in this context, from €50,316.00 to 29,988,336.00. On the same day, a further capital increase took place according to which €7,000,000.00 new shares were issued with a par value of €1.00 each. These measures together resulted in an increase of the Company's share capital to €36,988,336.00.

On 13 February 2018, the Placement was completed, and on 15 February 2018 the Company's shares were listed on the regulated market (Prime Standard) of the Frankfurt Stock Exchange.

In the Placement, a total of 19,900,000 shares were placed with institutional investors. The placed shares consisted of 7,000,000 new shares from the capital increase and 12,900,000 existing shares held by the Company's shareholders Coöperatieve Activum SG Fund III Investments U.A., Coöperatieve Formart Investments U.A. and Coöperatieve Activum SG Fund V, including additional shares from an over-allotment option. The placement price for the shares of the Company was €21.50.

Around €56 million of the net proceeds from the capital increase were used to fully repay an existing shareholder loan. With the remaining approximately €86.0 million, the Company plans to finance the acquisition and development of new housing projects and other corporate

expenses. One portion of this remaining capital was also used to repay an intercompany loan.

The free float on 23 April 2018 was around 50.4%. The remaining shares were still held by Coöperatieve Activum SG Fund III Investments U.A., Coöperatieve Formart Investments U.A. and Coöperatieve Activum SG Fund V.

In addition, certain of the Company's organisational documents were revised (and additional internal rules were adopted) so that its internal organisation became suitable for a listed company; also, a Supervisory Board (the "Supervisory Board") and certain Supervisory Board committees were established.

The Supervisory Board is composed of the following five members:

Stefan Brendgen, born in 1964 in Mönchengladbach, Germany, as chairman of the Supervisory Board and chairman of the nomination committee.

Stefan Mohr, born in 1967 in Frankfurt am Main, Germany, as deputy chairman of the Supervisory Board.

Marija Korsch, born in 1948, in Zadar, Croatia, as member of the Supervisory Board.

Dr. Jochen Scharpe, born in 1959 in Werdohl, Germany, as member of the Supervisory Board and chairman of the audit committee.

Richard Wartenberg, born 1968 in Stuttgart, Germany, as member of the Supervisory Board and chairman of the remuneration committee.

Furthermore, as our business activities and properties are geographically concentrated in Germany, we have filed with the Dutch trade registry, on 9 February 2018, a proposal to convert the Company into a German stock corporation (Aktiengesellschaft), governed by the laws of the Federal Republic of Germany and having its registered seat in Essen, Germany (the "AG Conversion"). The resolution to convert the Company into a German stock corporation is expected to be proposed to the Company's general shareholders meeting (the "General Meeting") by the Management Board and the Supervisory Board, subject to certain conditions (as specified in the proposal) having been met.

On 29 March 2018, Instone Real Estate Leipzig GmbH repaid a €22.6 million bank loan for the corporate financing of the Company.

There are no other events which might influence the Company's outlook and which are not discussed in the statutory annual accounts included in this report.