

# Annual Report 2020

## Short Version

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Aargauische  
Kantonalbank

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This unaudited short version of the annual report is not a complete annual report. It is a translation of select segments of the original German annual and the pillar 3 report for information purposes only. In the event of variances, the German version shall take precedence over the English translation. You can find the full German annual and pillar 3 report at [www.akb.ch](http://www.akb.ch) for additional information.

# At a glance

in CHF million	2019	2020	Change in %
<b>Income statement</b>			
Operating income	396.0	408.7	3.2
Operating expenses	-203.6	-203.3	-0.2
Operating result	182.3	192.9	5.8
Profit	147.5	138.2	-6.3
<b>Appropriation of profit</b>			
Allocation to statutory retained earnings reserve	48.5	34.2	-29.5
Allocation to voluntary retained earnings reserves	33.0	37.0	12.1
Distribution to the canton	66.0	67.0	1.5
in CHF million	31.12.2019	31.12.2020	Change in %
<b>Balance sheet</b>			
Total assets	30 242.8	31 777.5	5.1
Loans to customers	23 366.5	23 598.2	1.0
Funds due to customers (inclusive cash bonds)	18 800.7	20 287.6	7.9
Net equity before distribution of net profit	2 467.1	2 586.0	4.8
<b>Customer volumes</b>			
Customer assets <sup>1)</sup>	28 649.3	30 112.7	5.1
Net new money	1 469.0	2 530.3	72.2
Business volume <sup>2)</sup>	54 721.7	56 873.4	3.9
<b>Key figures in %</b>			
Return on equity (ROE) <sup>3)</sup>	7.8	7.8	7-8
Total capital ratio excl. voluntary retained earnings reserves <sup>4)</sup>	17.4	17.8	16.8-17.2
Total capital ratio according to Pillar 3	17.9	18.6	
Leverage ratio <sup>5)</sup>	7.7	8.5	
Cost-income ratio	51.4	49.7	50-55
<b>Personnel <sup>6)</sup></b>			
FTE (full-time equivalent)	707.8	726.2	2.6
of which apprentices/trainees	42.6	44.0	3.3
<b>Rating</b>			
Standard & Poor's	AA	AA	

<sup>1)</sup> Basis: Deposits and assets under management (exclusive corporate assets).

<sup>2)</sup> Basis: Client assets, corporate assets and loans to customers.

<sup>3)</sup> Calculation return on equity: Operating result / average net equity.

<sup>4)</sup> To cushion the economic consequences caused by the Covid-19 pandemic, the national countercyclical buffer has been deactivated in pursuance of the resolution of the Swiss Federal Council as per 27.03.2021. The disclosure is without the national countercyclical buffer also retrospectively.

<sup>5)</sup> Calculation per 31.12.2020 in consideration of the granted temporary financial reliefs according to the FINMA-announcement as part of the Covid-19 pandemic.

<sup>6)</sup> FTE (full-time equivalent) is shown as part-time adjusted, apprentices, trainees and employees in the trainee pool are counted as 50%.

# Business performance

Aargauische Kantonalbank (AKB) unveiled a good operating result for 2020. At CHF 192.9 million, it was the third highest ever. Another highlight was the pleasing growth of CHF 1.5 billion in customer assets, which amounted to CHF 30.1 billion (+5.1 per cent) as at the end of the year. AKB strengthened its net equity in 2020 by a very significant CHF 118 million, and its net equity after distribution of net profit amounted to CHF 2.5 billion. The Board of Directors has proposed in consultation with the Executive Council a profit distribution to the canton of Aargau of CHF 67.0 million. Besides the CHF 11.1 million to pay the state guarantee, the canton of Aargau received total compensation of CHF 78.1 million for the reporting year.

## Growth in quality of loans to customers

There was a moderate increase in loans to customers of around CHF 230 million or 1.0 per cent as at the reporting date. With a total volume of CHF 23.6 billion of customer loans, the cantonal bank made a sustainable contribution to the economy in its business area.

Mortgage loans – the most important area of lending with a 70 per cent share of total assets – posted a net gain of CHF 158.2 million or 0.7 per cent to a total of CHF 22.2 billion. At the same time, AKB maintained its current prudential approach to lending. In addition, AKB further consolidated its leading position in mortgage lending to individuals in its market area.

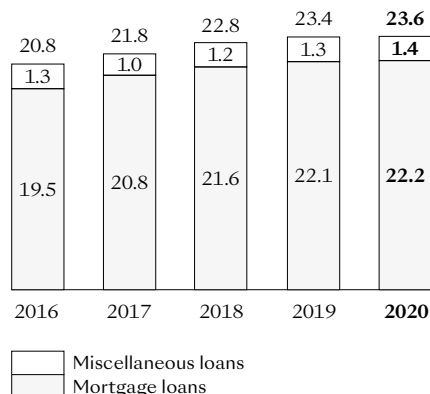
As a responsible bank of the canton Aargau, AKB accompanied its SMEs through the turbulent year in a spirit of partnership. AKB provided quick and straightforward bridging assistance in the form of amortisation suspensions and liquidity injections to companies that had liquidity problems through no fault of their own due to the coronavirus and intact business models. Under the federal and cantonal Covid-19 credit programmes, more than 2,100 loans totalling around CHF 300 million were granted, around CHF 160 million of which had been utilised by the end of the year.

## Confidence in the bank of the people of Aargau remains undiminished

The balance sheet item “Amounts due in respect of customer deposits” increased by the net amount of CHF 1.5 billion or 8.0 per cent to CHF 20.3 billion during the reporting year. As a result, its share of total assets as at the end of 2020 was 63.8 per cent. AKB considers the high net new money of CHF 2.5 billion to be a strong vote of confidence in the quality of its services and consultancy.

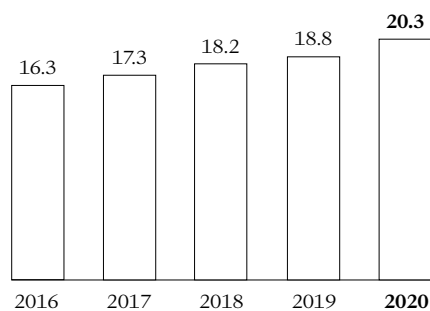
# 23.6 bn

Customer loans in CHF bn



# 20.3 bn

Customer funds in CHF bn



## Growth in business volumes

The Bank had just under CHF 32 billion in total assets as at the end of 2020. This was an increase of CHF 1.5 billion or 5.1 per cent. Customer assets and business volume – the latter consisting of customer deposits and loans to customers – expanded by CHF 1.5 billion and CHF 2.2 billion respectively, reaching a new record high of CHF 30.1 billion and CHF 56.9 billion.

## Operating income significantly exceeds previous year's all-time high

Earnings at AKB continued to grow, with operating income touching a new high of CHF 408.7 million (CHF +12.7 million; +3.2 per cent). Interest operations contributed 74.3 per cent to the record high operating income, making it a key earnings pillar.

At CHF 303.6 million, net income from interest operations was well above the previous year's level with an increase of CHF 10.2 million or 3.5 per cent despite continued high pressure on margins. The opportunities taken advantage of in liquidity management contributed significantly to the improved performance.

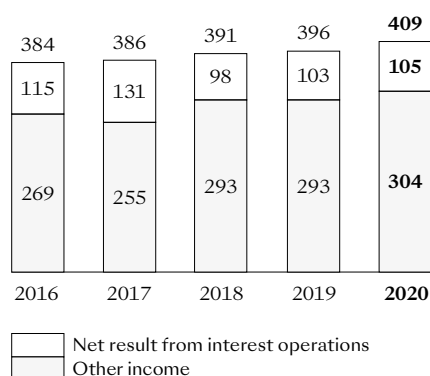
The “Changes in value adjustments for default risks and losses from interest operations” produced a net creating surplus of CHF 1.1 million in the reporting year. Towards the end of the reporting year, increased impairments had to be booked for SMEs and corporate customers affected by the economic consequences of the coronavirus pandemic. In the previous year, a net release surplus of CHF 8.0 million was recorded.

## Strong commission business and declining trading activities

The success story in the commission business continues. Earnings from the commission business and services rose once again to an impressive CHF 75.3 million, an increase of CHF 4.5 million (+6.4 per cent). The main drivers for this business line were higher income

# 409 m

Operating income in CHF m



from the good performance of the AKB funds, asset management and stock exchange fees, which go up especially when markets are jittery.

AKB continued to focus its trading activities on the customer business. The global pandemic left its mark on earnings from the trading activities and AKB recorded a fall of 11.8 per cent to CHF 21.3 million in this area of the business. The decline in currencies, foreign notes and coins and precious metals trading largely led to the sharp drop here.

Other results from ordinary activities rose by 10.4 per cent to CHF 8.5 million. The sale of a financial investment had a significant influence on the positive performance in the reporting period.

## Operating expenses slightly below previous year

Operating expenses contracted slightly by CHF 0.4 million to CHF 203.3 million in the financial year just ended. However, personnel expenses increased by 2.8 per cent or CHF 3.3 million. This was due in particular to the higher number of well-trained specialists. On the other hand, general and administrative expenses decreased by CHF 3.6 million (-4.2 per cent). Improvements to IT – despite additional expenses during the pandemic – and property maintenance led to significant cost reductions. Despite the cancellation of customer events, marketing and

sponsoring costs increased. Through the “AKB Impuls” programme, AKB supports with project financing the coexistence of people with each other in our region. The voucher campaign with Aargau Tourismus brightened the mood of the people of Aargau by distributing various leisure and tourism offers to over 25,000 people through the municipalities.

## Cost-income ratio below 50 per cent

The increase in operating income and decrease in operating expenses reduced the cost-income ratio to a very satisfactory 49.7 per cent and demonstrates AKB’s high economic efficiency. Compared with the 2019 financial year, the strategic ratio improved by 1.7 percentage points.

## Operating result higher

The value adjustments on participations and depreciation and amortisation of tangible fixed assets stood at CHF 9.4 million, which is CHF 1.9 million below the previous year.

In the reporting year, a net creating surplus of CHF 3.1 million was booked to changes to provisions and other impairments, and losses. In the previous year, a net release of CHF 1.2 million was applied to provisions.

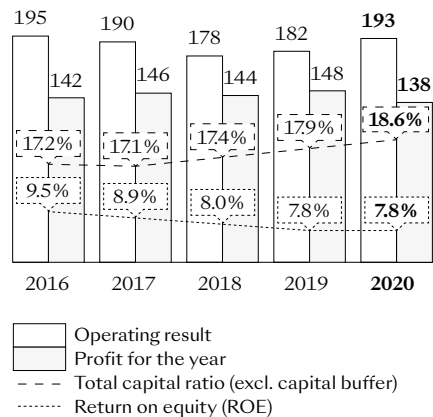
The operating result, which is the profit from operating activities, was an excellent CHF 192.9 million, an increase of CHF 10.6 million or 5.8 per cent on the figure for the comparable period. AKB thus recorded the third highest operating result in its long history.

Return on equity calculated on the basis of the operating result was 7.8 per cent (previous year: 7.8 per cent as well), which is within the strategic range of 7.0-8.0 per cent.

## Annual profit lower than previous year due to higher risk provisioning

Due to the probable increase in credit risks in connection with the economic downturn triggered by the Covid-19 pandemic, the risk pro-

Operating result, profit for the year, total capital ratio and return on equity (ROE) in CHF m



vision in the reserves for general banking risks is being increased with a view to the future. At the end of the year, the allocation to the reserves for general banking risks amounted to CHF 46.7 million or +72.3 per cent, compared with CHF 27.1 million in the previous year.

The tax expenses of CHF 8.0 million included CHF 7.2 million (previous year: CHF 7.1 million) of income taxes in favour of the local communities of AKB in the canton of Aargau. These taxes are attributable to the profit distribution to the canton of Aargau.

Due to the additional allocation to the reserves for general banking risks, AKB’s profit of CHF 138.2 million was CHF 9.3 million or 6.3 per cent lower than in the previous year (CHF 147.5 million).

The company’s profit before changes in reserves for general banking risks was CHF 184.9 million compared with CHF 174.6 million in the previous year, which was an excellent CHF 10.3 million or 5.9 per cent more.

## Appropriation of profit – AKB continues strengthening its capital base

The Board of Directors proposed in consultation with the Executive Council a profit distribution to the canton of Aargau of CHF 67.0 million and an allocation to the statutory retained earnings reserve of CHF 34.2 million as well as an allocation to the voluntary

retained earnings reserves of CHF 37.0 million. The voluntary retained earnings reserves are to be definitively and proactively formed in view of the increasing requirements of the regulator and the own funds requirements in connection with Basel III. This will enable AKB to further expand its very solid equity capitalisation and ensure that it can continue its operating activities successfully as usual even under more acute conditions in the future.

The additional capital is built up by allocating it to a voluntary retained earnings reserve. These reserves will be increased over the coming years and transparently reported every year. AKB is thus safeguarding its financial power in the long term and acting proactively and from a strong starting position.

Along with the allocation to reserves for general banking risks of CHF 46.7 million, there was an increase in equity of a very high CHF 117.9 million, resulting in an increase in the total capital ratio from 17.9 per cent to 18.6 per cent. Excluding the voluntary retained earnings reserves, the total capital ratio was 17.8 per cent (previous year: 17.4 per cent).

# Balance sheet

before appropriation of profit

in CHF 1000	31.12.2019	31.12.2020	Change in %
<b>Assets</b>			
Liquid assets	4 360 146	5 609 449	28.7
Amounts due from banks	571 725	414 290	-27.5
Amounts due from customers	1 313 489	1 386 968	5.6
Mortgage loans	22 053 016	22 211 185	0.7
Trading portfolio assets	113 361	108 951	-3.9
Positive replacement values of derivative financial instruments	107 192	115 410	7.7
Financial investments	1 605 036	1 823 184	13.6
Accrued income and prepaid expenses	22 424	24 413	8.9
Participations	15 705	15 705	-
Tangible fixed assets	59 327	54 584	-8.0
Other assets	21 344	13 342	-37.5
<b>Total assets</b>	<b>30 242 765</b>	<b>31 777 481</b>	<b>5.1</b>
Total subordinated claims	5 326	7 594	42.6
of which subject to mandatory conversion and / or debt waiver	-	-	n. a.
<b>Liabilities</b>			
Amounts due to banks	3 434 925	2 927 287	-14.8
Liabilities from securities financing transactions	200 000	383 583	91.8
Amounts due in respect of customer deposits	18 774 209	20 267 905	8.0
Negative replacement values of derivative financial instruments	138 910	115 776	-16.7
Liabilities from other financial instruments at fair value	107 053	101 801	-4.9
Cash bonds	26 486	19 713	-25.6
Bond issues and central mortgage institution loans	4 936 533	5 204 220	5.4
Accrued expenses and deferred income	88 337	96 785	9.6
Other liabilities	41 748	41 446	-0.7
Provisions	27 506	32 991	19.9
Reserves for general banking risks	1 329 500	1 376 200	3.5
Bank's capital	200 000	200 000	-
Statutory retained earnings reserve	750 780	799 280	6.5
Voluntary retained earnings reserves	39 000	72 000	84.6
Profit carried forward	264	278	5.3
Profit	147 514	138 216	-6.3
<b>Total liabilities</b>	<b>30 242 765</b>	<b>31 777 481</b>	<b>5.1</b>
Total subordinated liabilities	-	-	n. a.
of which subject to mandatory conversion and / or debt waiver	-	-	n. a.
<b>Off-balance-sheet transactions</b>			
Contingent liabilities	268 280	253 371	-5.6
Irrevocable commitments	828 694	1 178 132	42.2
Obligations to pay up shares and make further contributions	48 458	48 458	-
Credit commitments	-	-	n. a.



# Income statement

in CHF 1000	2019	2020	Change in %
<b>Result from interest operations</b>			
Interest and discount income	275 021	276 144	0.4
Interest and dividend income from financial investments	7 552	6 741	-10.7
Interest expense	2 829	21 828	671.6
<b>Gross result from interest operations</b>	<b>285 402</b>	<b>304 713</b>	<b>6.8</b>
Changes in value adjustments for default risks and losses from interest operations	7 989	-1 114	-113.9
<b>Subtotal net result from interest operations</b>	<b>293 391</b>	<b>303 599</b>	<b>3.5</b>
<b>Result from commission business and services</b>			
Commission income from securities trading and investment activities	53 858	59 286	10.1
Commission income from lending activities	3 941	5 048	28.1
Commission income from other services	17 461	17 327	-0.8
Commission expense	-4 481	-6 343	41.6
<b>Subtotal result from commission business and services</b>	<b>70 779</b>	<b>75 318</b>	<b>6.4</b>
<b>Result from trading activities and the fair value option</b>	<b>24 129</b>	<b>21 283</b>	<b>-11.8</b>
<b>Other result from ordinary activities</b>			
Result from the disposal of financial investments	1 520	4 142	172.5
Income from participations	2 834	2 461	-13.2
Result from real estate	2 312	2 263	-2.1
Other ordinary income	1 045	511	-51.1
Other ordinary expenses	-1	-869	n. a.
<b>Subtotal other result from ordinary activities</b>	<b>7 710</b>	<b>8 508</b>	<b>10.4</b>
<b>Operating income</b>	<b>396 009</b>	<b>408 708</b>	<b>3.2</b>
<b>Operating expenses</b>			
Personnel expenses	-118 333	-121 592	2.8
General and administrative expenses	-85 302	-81 684	-4.2
of which compensation for the state guarantee	-11 853	-11 112	-6.3
<b>Subtotal operating expenses</b>	<b>-203 635</b>	<b>-203 276</b>	<b>-0.2</b>
Value adjustments on participations and depreciation and amortisation of tangible fixed assets and intangible assets	-11 303	-9 395	-16.9
Changes to provisions and other value adjustments, and losses	1 245	-3 094	-348.5
<b>Operating result</b>	<b>182 316</b>	<b>192 943</b>	<b>5.8</b>
Extraordinary income	431	4	-99.1
Extraordinary expenses	-	-	n. a.
Changes in reserves for general banking risks	-27 100	-46 700	72.3
Taxes	-8 133	-8 031	-1.3
<b>Profit</b>	<b>147 514</b>	<b>138 216</b>	<b>-6.3</b>

# Appropriation of profit

in CHF 1000	2019	2020	Change in %
<b>Appropriation of profit</b>			
Profit	147 514	138 216	-6.3
Profit carried forward	264	278	5.3
<b>Distributable profit</b>	<b>147 778</b>	<b>138 494</b>	<b>-6.3</b>
Allocation to statutory retained earnings reserve	48 500	34 200	-29.5
Allocation to voluntary retained earnings reserves	33 000	37 000	12.1
Distribution to the canton	66 000	67 000	1.5
<b>Profit carried forward</b>	<b>278</b>	<b>294</b>	<b>5.8</b>

# Risk management

In connection with its business model and its strategic orientation, AKB is largely exposed to credit risks, market risks, liquidity risks, operational risks (including IT risks) as well as compliance risks. For AKB, risk management is a process in which all relevant risks with a potential negative impact on the Bank are systematically identified, analysed, assessed, managed and monitored. This process is supported by appropriate organisational structures as well as methods, tools, and guidelines.

## I. Risk governance structure

The Bank's risk governance is based on the concept of the Three Lines of Defence.

Ultimate responsibility for risk management rests with the Board of Directors. It is responsible for the regulation, establishment and monitoring of effective risk management and overall risk management. To this end, it establishes the framework for institution-wide risk management.

The Audit and Risk Committee of the Board of Directors assists the Board of Directors in assessing and monitoring the functionality and appropriateness of internal control and/or the internal control system, bank-wide risk management and compliance.

The Executive Management is required to implement the operational business in accordance with the framework concept for bank-wide risk management. It must specify, set up and implement appropriate processes for identifying, assessing, managing and monitoring the risks taken by the Bank.

The overall company's risk management builds on three independent lines of defence under corporate governance:

### *First line of defence: risk responsibility, risk assumption and management*

The specific risk assumption is delegated by the Executive Management to the operational units by means of guidelines and instructions subject to clearly defined specifications and risk limits.

In some significant types of risk, risk assumption is also delegated to defined internal committees.

As Risk Officers, these operational bodies or committees are responsible for the assessment, management, control and handling of risks.

### *Second line of defence: risk monitoring and control*

The independent Risk/CRO sector, under the direction of the Chief Risk Officer (CRO), is responsible for the comprehensive and systematic monitoring and reporting of both individual and aggregated exposures to all material types of risk. The Risk/CRO sector is part of the Finance & Risk division and has direct access to the operational management, the Audit and Risk Committee and the Board of Directors. The Risk/CRO sector encompasses the functions of risk control and IT security and, together with the Compliance department, forms the Bank's "second line of defence".

The Risk/CRO sector issues various specific reports on the risk exposures and development of the risk situation for each major type of risk. In addition, it prepares a quarterly comprehensive and consolidated risk report covering all material risk categories for the attention of the Executive Management, the Audit and Risk Committee and the Board of Directors. In addition, the CRO immediately triggers the defined escalation and emergency procedures for significant risk-relevant developments. In any case, this includes violations of prescribed risk tolerances, risk limits and/or thresholds.

### *Third line of defence: independent "assurance"*

The internal auditing department, which is independent of the Executive Management, assists the Board of Directors in the performance of its senior management function. In this role, it assesses the Bank's risk management, control and governance processes.

## II. Framework for bank-wide risk management

The Bank has a framework for bank-wide risk management specified by the Board of Directors. This consists of the internal regulations on risk policy, the risk tolerance guidelines and the risk limits as well as the specific internal regulations and guidelines issued for the main types of risk.

The risk policy is limited to the definition of principles for the individual risk types, the delegation of authority, methodological and organisational standards as well as reporting and financial reporting.

The main risk types are limited by the Board of Directors through the risk tolerance guidelines. Based on the risk profile and risk-bearing capacity of the Bank, these limits define the risk tolerance of the Bank as a whole and the main types of risk to be complied with. The risk tolerance guidelines are reviewed annually and are continuously monitored. The defined risk tolerances are set up so that even in the case of a cumulative exhaustion they do not compromise the continued existence of the Bank.

The specific implementation rules regarding the tasks, competencies and responsibilities as well as the principles of identification and evaluation, limitation and control, monitoring and reporting are ultimately contained in the specific internal regulations on the main types of risk.

The annual reassessment of the risk policy as well as the final assessment and approval of the systematic analysis took place for the last time at the meeting of the Board of Directors on 29 October 2020.

In addition, the Board of Directors approved the “Risk Tolerance of the Board of Directors” at its meeting on 10 December 2020 and the Executive Management agreed the “Risk Limits of the Executive Management”, at its meeting on 18 November 2020. The updated “Risk Appetite Framework”, consisting of risk tolerance and risk limits, came into effect on 1 January 2021.

### **A. Credit risks**

An integral part of the framework for bank-wide risk management are the credit regulations, which establish the regulatory framework for all banking transactions that generate credit risks for the Bank. At the implementation level, the credit regulations are supplemented by credit guidelines as well as by directives and process descriptions. The credit guidelines, depending on the current risk assessment of the market and economic environments, specify the regulatory principles and guidelines in lending.

Credit risks are restricted by limits, quality requirements, fixed cover margins and guidelines for risk diversification. When granting loans and other exposures with default risks, creditworthiness and solvency are assessed using uniform criteria. There is a multi-level, risk-based allocation of responsibilities, which

regulates both ordinary credit competencies and special and tolerance competencies.

The units responsible for acquiring and servicing customers are completely separate from the loan processing and credit administration.

The credit risk monitoring at the portfolio level is carried out by the Risk/CRO sector, which is independent of the sales organisation and monitors the development of the credit portfolio in various ways. Appropriate methods and models are used to assess credit risks periodically and/or on an ad hoc basis.

The objective of credit monitoring at the portfolio level is to identify at an early stage existing and/or potential credit risks due to concentrations, interdependencies or influences of significant market developments and to assess and demonstrate their impact on the risk tolerance, risk limits and/or thresholds of the Bank as a whole.

Monthly reports are sent to the senior credit approval department regarding the development of the credit portfolio. The Executive Management, the Audit and Risk Committee and the Board of Directors are each informed about the specific credit risk analyses. In addition, the risk assessment of the entire loan portfolio is reported in detail quarterly.

To measure and manage default risk, the Bank classifies its loans according to a rating system. The system is used to ensure the uniform assessment of default risks and to determine the expected losses which the Bank will incur in lending. This component is used for the risk-based definition of credit conditions and thereby directly influences the conclusion of credit transactions.

#### *Methods used to identify default risks and to determine impairment requirements*

Besides a comprehensive rating system, credit monitoring is based on defined early warning indicators (overruns, interest arrears, impairments, etc.), which point to a deterioration in credit quality as early as possible and ensure the timely performance of a new assessment and, if necessary, corrective measures.

The Bank attaches great importance to the consistent management of problem exposures and loss positions. The Special Financing department in the credit management sector

monitors in particular the “watch list” positions and provides support for positions that are impaired or non-performing, either on its own or together with the client advisor of the sales organisation. The sector, along with the Real Estate Management department is also responsible for the management and the rapid resale of properties foreclosed on by the Bank.

Receivables for which the Bank considers it unlikely that the borrower will be able to fully comply with its future obligations are considered at risk. Client commitments are classified as at risk at the latest when the contractual payments (principal, interest and/or commission) are 90 days or more overdue and there is evidence at the same time that the borrower cannot comply at all or in full with its future obligations.

Loans at risk are valued individually and the impairment is covered by specific valuation allowances. The impairment is the difference between the receivable’s carrying amount and the estimated recoverable amount, taking into account the counterparty risk and the net proceeds from the sale of any collateral. In determining the net proceeds of collateral, all holding costs such as interest, maintenance and sales costs, etc. up until the estimated time of sale, as well as any applicable taxes and fees, are deducted.

To cover inherent default risks in the customer portfolio existing on the valuation date, AKB estimates the future expected and unexpected loss at overall portfolio level. This serves as the basis for the calculation of capital allocation to reserves for general banking risks in the lending business in accordance with the concept of “risk provisioning”.

The concept of “risk provisioning” is used for risk prevention and anticipation of future expected and unexpected losses from the loans to customers. Depending on the provision situation, the aim of “risk provisioning” is to create additional, voluntary reserves for future loan defaults or to use these reserves to cover losses in the case of special events.

The calculation is based on internal stress scenarios, which assume a severe general economic recession. The aim of the scenarios is to show the effects of a real estate price collapse or a macroeconomic recession on the loan portfolio. The allocation to the account “risk

provisioning” accounted for separately under the balance sheet heading “reserves for general banking risks” is performed according to the “high water-mark method”, i.e. an allocation is performed only if the unexpected losses of the CVaR (Credit Value at Risk) calculated in the stress scenario are greater than the amount of risk provisions. The addition or release is made via the income statement item “Changes in reserves for general banking risks”.

To take into account the increased default risks in connection with the current coronavirus pandemic, risk provisions were increased by CHF 28.2 million in the reporting year based on the calculated scenarios. As a result, the holdings at the end of the year amounted to CHF 250.2 million.

In capital planning, the effects of the losses based on the stress scenarios on the capital situation are shown. The results show that when entering a series of very high credit losses which affect the entire banking industry equally, the Bank itself would still have an intact equity ceiling, so the ordinary course of business could be guaranteed in compliance with the capital adequacy requirements.

#### 1. Customer loans

The core business of AKB is the granting of mortgages and other mortgage-backed loans. To determine the maximum amount of property financing, the following factors are decisive: collateral values internally defined by the Bank for each property type and the financial viability of the borrower and the observance of amortisation principles. The criteria to be applied in each case are set out in the credit guidelines and also take into account the assessment of the property market.

For loans with securities as collateral, the credit guidelines define the assets accepted as collateral and their collateral values. The guidelines are further restricted using risk-based criteria by currency, issuer domicile, stock exchange, tradability and diversification and are reviewed periodically.

Alongside the mortgage business and securities collateral-secured loans for private clients, the Bank’s operations include commercial lending, primarily to companies based in the market territory.

### *Valuation of collateral*

To value property, AKB employs experts to support the client advisor and the approval entities in technical matters, decisions and judgements. The guidelines for valuing all kinds of property are subject to binding regulations. The client advisors can make decisions on standard transactions under their own authority using a set of estimation tools. Properties which do not meet the defined parameters for standard transactions are assessed exclusively by real estate experts. The real estate experts are based in a central unit independent from the front office. For the majority of standard transactions, either a hedonic model for owner-occupied homes and single-family homes, or a capitalised earnings method for multi-family homes and simple residential and commercial buildings is used. Both estimation tools are integrated into the lending process, which guarantee an efficient and consistent evaluation. In the case of poor creditworthiness an additional liquidation value is calculated.

The value of securities collateral is monitored daily. If the collateral values fall below the loan exposure amount, the outstanding amount needs to be reduced or additional collateral put up. In exceptional market conditions or in the case of increasing cover deficit, the collateral is realised and the loan closed out.

For commercial loans, the relevant evaluation criteria are mainly future earnings outlook, market position, the assessment by management and financial ability to repay the loan on schedule. Unsecured major exposures are restricted by limits at individual and total exposure level. Additionally, guidelines and benchmarks exist at the overall portfolio level.

### 2. Credit risks from trading

Responsibilities and technical tasks related to credit risks from trading, including the internal standards for the application of risk mitigation techniques, are set out in the loan regulations, in the credit guidelines and at the instruction level. The counterparty risks in the interbank business as well as in positions towards central counterparties are limited by a limit system. Limits must be approved by the competent approval entities at the request of the operational units in the trading department in accordance

with the allocation of authority. The approval entities are completely separate from the units making the request. The adequacy of the limits is checked at least once per year or if particular events occur. To reduce wrong-way risks, care is taken to ensure appropriate diversification.

Compliance with limits is monitored daily by the Risk/CRO sector and is reported on a monthly basis. Furthermore, each quarter the Audit and Risk Committee and the Board of Directors are informed about limit compliance, risk assessment and particular findings.

AKB conducts interbank business primarily for liquidity management and handling of client orders (international payments). This involves short-term money market deposits and transfers from domestic and foreign banks.

### 3. Country risk

Country risks are limited by the Board of Directors through predetermined thresholds based on rating category. Within these thresholds, the competent credit committee places additional limits in the form of individual limits per country. The Risk/CRO sector monitors compliance with country limits. Exposures in risk countries are assessed at least twice a year for traceability and impairments made if necessary.

## **B. Market risk**

Market risks describe the risk of losses arising due to changes in market prices (equities, exchange rates, interest, commodities and property) and factors influenced by market prices (e.g. volatility and correlations). We differentiate between three sub-risk categories:

- Market risk in the trading book
- Interest rate risk
- Other market risks

### 1. Market risk in the trading book

Financial instruments that are held for the Bank's own account for resale in order to exploit short-term price and interest rate fluctuations are assigned to the trading book and measured on a fair value basis using daily market prices. These positions are actively managed within the defined risk tolerance and risk limits exclusively by the trading desks "Forex", "Equity" and "Interest". The Bank also

acts as an issuer of certificates. The underlying assets or securities of the certificates are held in the trading portfolio as a hedged item.

The concrete tasks, competencies and responsibilities as well as the principles of identification and evaluation, limitation and control, monitoring and reporting of the Bank's trading activities are regulated in the internal trading regulations. Entering into risks from proprietary trading is specified in detail in and regulated by the internal trading guidelines and dealer-specific instructions. With the exception of self-issued certificates, AKB does not engage in any market-making activities.

Derivative financial instruments may be used in currency, interest and securities trading for the Bank's own or a third-party account. Both standardised and OTC instruments are used.

Risk is limited by Value at Risk limits (VaR), position and daily loss limits.

The risk tolerance for the entire trading book (forex, equity and interest) is determined as VaR limits by the Board of Directors and its adequacy is verified at least annually. At Executive Management level, the risk tolerance is allocated to the individual trading desks "Forex", "Equity" and "Interest" as VaR risk limits. Daily monitoring of the VaR limit is carried out by the Risk/CRO sector which is an independent unit of the trading department. Daily reports on the utilisation of the VaR limit are sent to the competent department manager and managers of each trading desk, on a monthly basis to the Executive Management and on a quarterly basis to the Audit and Risk Committee and the Board of Directors.

For the monitoring and reporting of market risks in the trading book, the Risk/CRO sector has a dedicated IT system that derives the trading book positions directly from the core banking system, evaluates them independently and calculates the limit utilisation.

The position and daily loss limits are allocated by the relevant department managers per trading desk or per trader and monitored by the respective manager of the corresponding trading desk. The position limits restrict the exposure for each dealer and are designed to protect to the Bank from excessive exposure. The daily loss limits are intended to restrict short-term losses due to large market fluctua-

tions and prevent the Bank from exceeding its risk tolerance and/or VaR risk limits through an accumulation of realised and unrealised losses.

## 2. Interest rate risk

It is the aim of interest rate risk management to reduce any margin pressure from changes in market prices and client behaviour, strengthen the solvency of the Bank and thus safeguard the stability of the equity through optimal balance sheet structure management. Asset and liability management (ALM) is based on the internal regulations for ALM and the corresponding guidelines. The regulations define the principles, responsibilities and competencies, while the LBSM guidelines lay down specific requirements in connection with balance sheet structure management.

The "Liquidity & ALM Board" (LAB) is the strategic decision-making committee for monitoring and managing interest rate risks, within the framework of the competencies and limits set by the Board of Directors. The LAB meets monthly and delegates certain well-defined tasks, competencies and responsibilities to the "Liquidity & ALM Committee" (LAC). The LAB comprises the members of the Executive Management and the advisory members of the LAC. The operational unit "Treasury" implements the strategic decisions of the LAB. Risk/CRO conducts the supervision/monitoring of the implementation of strategic decisions by the LAB and its compliance with the limits, independently from the operational units. It is also responsible for the monthly risk reporting to the LAC and LAB and quarterly reporting to the Audit and Risk Committee and the Board of Directors.

The management of interest rate risks is based on the present value method and focuses on limiting the negative impact in the net present value of equity and the income effect.

To calculate the present value of equity, fixed interest rate products are divided according to their maturity and variable interest rate products are replicated. Replication is based on the need to reproduce, as accurately as possible, changes in client interest rates using changes in market interest rates, i.e. to achieve an optimum ratio between risk (interest rate risk) and income (margin). The optimum ratio is calculated with the aid of the efficient fron-

tier method, which originates from portfolio theory. The entire equity complex is treated as non-interest sensitive and is not replicated. Replication is reviewed annually for its effectiveness.

Interest rate risks are monitored on the basis of static (sensitivity, market value of equity and VaR) and dynamic calculations (simulations of possible market scenarios). The Bank manages the interest rate risks through on-balance sheet measures. Hedging is conducted depending on the assessment of interest rate risk.

Interest rate risks are limited by the risk tolerance specified by the Board of Directors by limiting the maximum present value loss in the equity. At Executive Management level, a further limit is applied by means of VaR limits. Simulations are carried out periodically to determine future trends in the Bank's earnings from interest operations. Both the value effect and income effect are measured here.

The market value of equity is stressed monthly by means of six different changes in the yield curve. The LAB is informed monthly of the scenarios used and the resulting changes in value.

Future potential changes in the interest balance (income effect) are stressed at regular intervals using various scenarios. These include both different changes in the yield curve and client behaviour, which can, depending on the interest rate environment, lead to massive shifts in capital. The interest balance calculated is based on a dynamic change in interest-bearing positions and the market environment. The results are discussed in the LAB and brought to the attention of the Audit and Risk Committee as part of the quarterly reporting.

For the monitoring and reporting of interest rate risks as well as for the calculation of key figures and the implementation of stress scenarios, the Risk/CRO sector has a dedicated IT system that derives the balance sheet data directly from the core banking system.

#### *Business policy on the use of derivative financial instruments*

The instruments used for balance sheet management serve mainly to hedge interest rate and foreign currency risks in the banking book. Interest rate swaps and cross-currency swaps

are also primarily used. Credit derivatives are not used.

Micro-hedges are predominantly used for hedging. Selected and clearly identified, interest rate-sensitive client receivables or liabilities are hedged (either individually or grouped together) over the entire remaining period as underlying assets here. Macro-hedges are also occasionally used alongside to hedge sensitivity in a specific time bucket.

The objectives and strategies of hedges between the hedging instrument and the hedged item are documented in each case upon conclusion of the derivative hedging transactions.

The effectiveness of the hedging relationship is reviewed periodically by the independent Risk/CRO sector. It monitors whether the sensitivity of the hedging transactions exceeds the sensitivity of the allocated underlying assets by more than 20 per cent. The hedging transaction must always reduce the sensitivity of the underlying assets overall.

Hedges where the criteria of effectiveness are no longer met are compared with the non-effective portion of a commercial transaction and the effect from the ineffective portion is booked under income from trading activities. In the reporting year there were no hedges that were not effective or not fully effective.

### 3. Other market risks

A VaR limit is in place to limit other market risks, which consist in particular of position risks from equity securities and from foreign currency positions.

#### **C. Liquidity risk**

The primary objective of liquidity management is to ensure the ongoing solvency of the Bank at all times, particularly during bank-specific and/or market-wide periods of stress.

The principles, responsibilities and competencies for managing liquidity risks are defined in the regulations and in the liquidity and balance sheet structure management guidelines. The LAC is responsible for the management of tactical liquidity. The LAC reports directly to the LAB committee. The LAC meets twice monthly and, among other duties, is responsible for developing and fleshing out strategies



for managing liquidity risk and the liquidity reserves.

The central operational unit Treasury implements the tactical decisions of the LAC and safeguards and manages intraday or short-term liquidity. The Risk/CRO sector conducts the supervision and monitoring of the implementation of tactical decisions by the LAC and its compliance with the limits, independently from the operational units. It is also responsible for daily liquidity reporting to Treasury and monthly risk reporting to the LAC and the LAB. The Audit and Risk Committee and the Board of Directors is updated quarterly on the changes in liquidity risk.

Operational measurement and management of liquidity risks is based on a daily liquidity schedule, which compares the expected cash inflows and outflows in a normal market phase. The liquidity schedule therefore shows the time horizon over which the Bank is still liquid or viable.

Liquidity risks are monitored on the basis of both static and dynamic calculations (including simulations of possible stress scenarios). Liquidity risks are limited by rules governing the maintenance of liquidity reserves (e.g. on quality and diversification) and guidelines on the financing structure (e.g. on counterparties, maturity bands and currencies). In addition, the Board of Directors limits liquidity risk by setting the liquidity risk tolerance.

The liquidity risk tolerance defines the minimum time horizon which must be continually maintained in a given stress scenario. Both institution-specific events and the effects of a global economic crisis are considered as stress scenarios.

In order to promptly detect risks in a liquidity position and potential funding options for the Bank, it has defined appropriate early warning indicators and set out potential emergency procedures with potential response measures. The defined early warning indicators are continuously monitored.

#### **D. Operational risk**

Operational Risk Management (OpRisk) is part of the independent risk control function within the Risk/CRO sector under the supervision of the Chief Risk Officer (CRO). The risk control

function is responsible for the design, implementation and maintenance of an effective and efficient operational risk framework and ensures the full and systematic monitoring and reporting of operational risk.

AKB defines operational risks as the risk of losses arising as a result of inadequate or failed internal procedures, people or systems or as a result of external events. Included are all legal risks, including fines from regulators and settlements. Strategic risks and reputational risks as secondary risks have an indirect effect on operational risks. These are an integral part of the operational risk management.

AKB defines operational risk management as a comprehensive process.

The focus is on the risk-oriented protection of persons, services, information and assets of the individual departments as well as the maintenance and restoration of critical business processes in an operational emergency.

The principles, responsibilities and competencies for the management of operational risks and designing the internal control system are defined in a specific set of internal regulations. This also defines an escalation process for results that exceed the expected scope.

The risk tolerance for operational risks is limited by means of suitable early warning indicators, which are further restricted, specified and monitored using appropriate thresholds and limits.

Any violations of the limits are remedied promptly with targeted measures.

The basis for the management of operational risks is the inventory of inherent operational risks at the level of the Bank as a whole. For the identification and assessment of operational risks, AKB uses numerous instruments (including periodic risk and control assessments [RCA], continuous recording of loss events, approval process for the introduction of new or major adjustments to existing products, services, processes or systems). Within the framework of RCA, for example, the operational risks of each business unit are assessed on a bottom-up basis on the basis of a defined methodology. The operational risks identified are systematically categorised and prioritised.

Both internal and external operational risk events are systematically recorded, assessed

and analysed in order to identify the reasons for their occurrence and to close potential gaps in the internal control system.

Operational risks are reduced by an effective and suitable internal control system. Internal control is designed so that processes run as intended and in compliance with applicable regulations. The starting point for designing the internal control system is a systematic risk analysis. This is the result of a comprehensive and systematic process to assess the overall risks to which the Bank is exposed. By conducting systematic risk analysis, the Board of Directors ensures that all significant risks in the Bank are recorded, limited and monitored. It is also used as a basis for the regular review of the adequacy and effectiveness of the internal controls.

The Bank uses an ICS tool for documenting, monitoring and evaluating the adequacy and effectiveness of the internal control system.

The adequacy and effectiveness of the internal controls are assessed once a year by the department managers and documented in a report. Another essential criterion of the assessment is the up-to-dateness of the internal control system. The assessment is also the basis for defining and carrying out any necessary corrective actions. To reduce risk, specific insurance policies are also used. The entire insurance portfolio of AKB is reviewed annually by an external insurance broker, discussed with the Bank or approved by the Executive Management.

Potential information security risks are managed on the basis of regular threat assessments. It provides adequate and effective security measures to protect information and infrastructures in terms of confidentiality, integrity, availability and traceability.

For business-critical processes, precautions have been taken in the context of Business Continuity Management (BCM). In this context AKB takes recognised standards into account. The relevant principles, responsibilities and procedures for BCM are defined in a specific set of internal regulations.

The Audit and Risk Committee and the Board of Directors are updated quarterly on changes in early warning indicators, the assessment of the operational risks and changes in the operational risk profile (including the

information security risks). Reporting includes the results of significant internal and relevant external operational risk events.

In addition, the CRO produces an annual report for the Board of Directors, the Audit and Risk Committee and the Executive Management on the assessment of the internal control system of the Bank. This report also includes the findings and developments of the risk situation in the areas of operational risk, information security and Business Continuity Management (BCM).

### **E. Compliance risk**

Compliance risk refers to any legal, reputational and loss risks which may arise from the violation of legal or professional standards or ethical principles. The principles, responsibilities and competencies for the compliance risks are defined in a specific set of internal regulations. Compliance with legal, regulatory, professional or internal regulations is monitored by the independent compliance function within the General Counsel – Legal & Compliance sector.

Compliance activities relate in particular to combating money laundering, preventing insider dealing, complying with banking and stock exchange law, observing product distribution rules, monitoring the risks from cross-border client transactions, avoiding conflicts of interest and ensuring the tax transparency of the client funds deposited with AKB.

Compliance annually reviews the compliance risk inventory, which it uses to draw up a plan of action. Compliance risks identified are managed and limited through the issue of directives, tailored operational systems and processes, employee training and downstream, independent monitoring and controls. The Compliance unit also advises the Executive Management and employees on compliance-related issues.

### **Significant events after the reporting date**

No significant events occurred after the reporting date that have a significant influence on the financial position and financial performance of the Bank as at 31 December 2020.

# Key prudential metrics (KM1)

in CHF 1000		e	d	c	b	a
		31.12.2019	31.03.2020	30.06.2020	30.09.2020	31.12.2020
<b>Eligible Capital</b>						
1	Common equity tier 1 (CET1)	2 401 058		2 401 058		2 518 974
2	Tier 1 capital	2 401 058		2 401 058		2 518 974
3	Total capital	2 401 058		2 401 058		2 518 974
<b>Risk-weighted assets (amounts)</b>						
4	RWA	13 393 901		13 515 296		13 533 490
<b>4a</b>	<b>Minimum capital requirement</b>	<b>1 071 512</b>		<b>1 081 224</b>		<b>1 082 679</b>
<b>Risk-based capital ratios as a percentage of RWA</b>						
5	Common equity tier 1 ratio	17.9%		17.8%		18.6%
6	Tier 1 capital ratio	17.9%		17.8%		18.6%
7	Total capital ratio	17.9%		17.8%		18.6%
<b>Additional CET1 buffer requirements as a percentage of RWA</b>						
8	Capital conservation buffer as per the Basel minimum standards (2.5% from 2019)	2.5%		2.5%		2.5%
9	Countercyclical capital buffer (Art. 44a CAO) in accordance with the Basel minimum standards					
10	Additional capital buffer due to international or national system relevance					
11	Total of bank CET 1 specific buffer requirements	2.5%		2.5%		2.5%
12	CET 1 available after meeting the bank's minimum capital requirements	9.9%		9.8%		10.6%
<b>Capital target ratios in accordance with Annex 8 of the CAO (in % of risk-weighted assets)</b>						
12a	Capital conservation buffer in accordance with Annex 8 of the CAO	4.0%		4.0%		4.0%
12b	Countercyclical buffer in accordance with Art. 44 and 44a of the CAO	1.0%		0.0%		0.0%
12c	CET 1 target ratio in accordance with Annex 8 of the CAO plus the countercyclical buffer in accordance with Art. 44 and 44a of the CAO	8.8%		7.8%		7.8%
12d	T1 target ratio in accordance with Annex 8 of the CAO plus the countercyclical buffer in accordance with Art. 44 and 44a of the CAO	10.6%		9.6%		9.6%
12e	Total capital target ratio in accordance with Annex 8 of the CAO plus the countercyclical buffer in accordance with Art. 44 and 44a of the CAO	13.0%		12.0%		12.0%
<b>Basel III Leverage Ratio</b>						
13	Total Basel III leverage ratio exposure measure	31 054 874		29 368 581		29 486 134
14	Basel III leverage ratio (tier 1 capital in % of total exposures)	7.7%		8.2%		8.5%
14a	Basel III leverage ratio under the fully loaded ECL (expected credit loss) accounting model (tier 1 capital in % of total exposures)	7.7%		8.2%		8.5%
<b>Liquidity coverage ratio</b>						
15	LCR Numerator: total high quality liquid assets	5 696 790	6 661 518	7 278 466	8 197 893	7 731 198
16	LCR Denominator: net cash outflows	3 719 379	4 084 861	4 743 232	4 928 525	4 496 122
17	Liquidity coverage ratio (LCR) %	153.2%	163.1%	153.4%	166.3%	172.0%

# Sustainability report

Am  
richtigen  
Ort.ch



Aargauische  
Kantonalbank

# Foreword

Dear Reader,

For the strategy period 2021-2024, we have made sustainability a central pillar and are therefore focusing even more on our responsibilities in all three areas. Ecological and social considerations are a key component of corporate decisions. We have set ourselves the goal of being considered the most sustainable financial services provider in our area of the market.

Sustainability is a multifaceted concept. Besides ecological issues, people and most especially the business aspects play a critical role. But sustainability is also about durability and viability. These two qualities are an excellent fit for AKB. For 107 years, AKB has been the bank of the people of Aargau, the point of contact for financial matters, provides over 800 jobs and is committed to resource-saving corporate management.

Compared with previous years, this sustainability report has a slightly different structure. This report now has articles and stories about how AKB is better protecting the climate, why it is a good employer and how much it is living up to its social responsibilities. AKB is still providing separate information on its sustainability commitment using the applicable standards of the Global Reporting Initiative (GRI). You can find this report at [www.akb.ch/sustainability](http://www.akb.ch/sustainability).

We look forward to being a reliable partner for you as a bank and will focus even more on offering you an attractive range of sustainable financial services.

Kind regards  
Dieter Widmer

# The future's green

**AKB issued a green bond in the summer of 2020. The Bank uses the funds to refinance a sustainable mortgage – the “green mortgage”. David Müller discusses the reasons for the product, and its take-up and future.**

## **What were the reasons behind the launch of the green mortgage?**

Switzerland's building stock is responsible for around 25 per cent of the country's CO<sub>2</sub> emissions. We want to raise awareness about energy efficiency among prospective and existing homeowners during our advisory sessions with them. At the same time, we are looking to provide a direct financial incentive so that projects to reduce emissions are carried out more quickly.

## **How have customers responded to the new product?**

Our customers greatly appreciate our commitment and the idea behind it, and the attractive conditions, of course. Building emissions are now an important component of our discussions with customers.

## **How has the green mortgage performed to date and is it in line with expectations?**

We are very satisfied with how it is doing. In the past, economic aspects were the deciding factor in the mortgage business. Our client advisors quickly recognised the sense of taking ecological considerations more on board.

However, it takes time for the importance of environmental issues and possible contributions by society to become established.

## **What goals AKB has set itself with the green mortgage?**

We want to make an effective contribution to meeting the targets defined by the Federal Council for reducing CO<sub>2</sub> emissions. The Swiss financial centre wants to be a leader in the area of sustainability so that it can become more competitive. We are a part of this and we take this duty seriously.

As a cantonal bank, we have a social responsibility. The AKB green mortgage is a demonstration of our inner conviction of the considerable importance of sustainability and the path we have chosen in this regard.

## **AKB's green mortgage supports and promotes all energy-efficient structural measures in properties. What was it most used for in the first few months?**

We supported a lot of new construction projects with climate-friendly energy systems and high efficiency requirements in terms of energy consumption. At the same time, we significantly stimulated demand among existing property owners to replace oil or gas heating systems and install a photovoltaic system.

## **Can you tell me what the impact of the green mortgage is on energy efficiency and resource conservation?**

An important concern for us right from the very start was measuring and transparently reporting the CO<sub>2</sub> savings made. So we have been working with external experts on this and will soon be publishing an impact report that will provide this information.

## **AKB is unshaken in its belief that sustainability is very important. Are there any plans to expand the sustainable product range in the lending sector?**

The topic of sustainability is a very important strategic consideration of ours and involves taking account of ESG criteria in their ecological, social and economic aspects. So as part of our huge and varied commitment in this area, we have a product range that meets this ambition.

We note that the conviction and the desire to make energy-efficient renovations are often there, but they're often not followed through because of cost considerations. So AKB sees itself not only as a “mortgage lender”, but also as an agent helping to realise energy-efficient projects. We will therefore continue to launch new services and products in the future.

# What is particularly important to us

## Attractive working models

AKB is a strong believer in the importance of attractive, modern and market-compliant employment conditions that are tailored to its employees' needs and stage of life. Where possible, it offers part-time work, job sharing or a "career arc" (a tailored transition for managers into retirement). With its "bandwidth model", there is also the option of taking extra holiday leave by reducing the annual salary. Loyal, motivated and performance-focused employees are an important factor in achieving ambitious corporate goals.

## Sustainable projects and sponsorships

Our sustainable commitment includes supporting promising projects which have social benefits. Besides financial contributions, the focus is also on transferring expertise and advisory functions. By taking part in the Liebegg agricultural centre's "Open Farming Hackdays", AKB made an important contribution, as the main sponsor, to solving upcoming challenges in agriculture. 70 attendees from all sectors of society and the economy worked in eleven interdisciplinary teams on new digital solutions for the future of Swiss agriculture. The first edition of Hackdays achieved impressive results with promising potential. Further information can be found at [www.opendata.ch/projects/open-farming-hackdays-2020](http://www.opendata.ch/projects/open-farming-hackdays-2020).

## Dialogue with our stakeholders

AKB takes its responsibilities in the area of sustainability seriously. But what does it see as particularly important and where does this commitment pay off? AKB clarifies these questions with its stakeholders every year so it can draw on a wider audience and build an opinion. In 2020, customers, all employees and the canton of Aargau, as owner, were able to voice an opinion. Achieving a good outcome from the survey is both a task and a challenge. The goal is to reconcile different opinions and interests and to ensure sustainable corporate development.

## Sustainability communication

Do you want to learn more about what AKB is doing in the area of sustainability to meet the expectations of a modern financial institution? You can find a comprehensive overview at [www.akb.ch/nachhaltigkeit](http://www.akb.ch/nachhaltigkeit). In its sustainability reporting, AKB has been following the guidelines of the Global Reporting Initiative (GRI) as a globally recognised standard since 2009 and providing information on the topics classified as relevant for reporting in accordance with the "Core" reporting option. AKB's GRI Content Index can be found at [www.akb.ch/sustainability/gri](http://www.akb.ch/sustainability/gri).

## Development-focused management

Demands on managers have changed. Development-focused leadership takes place on an equal footing and concentrates on motivating, individually encouraging and developing employees. Supervisors act as role models, seek common ways of achieving goals and lead through trust and taking personal responsibility. What Generation Y wants, according to their representatives, is regular feedback, appreciative communication, meaningful work and development opportunities. With development-focused management, AKB is equipped to provide the further development opportunities employees need.

# Sustainability profile of the Bank's properties

**Saving energy, optimising consumption and reducing CO<sub>2</sub> emissions are an important pillar of operational ecology at AKB. The focus here is on the Bank's own buildings and what reductions can be made. The centrepiece is the main building at Bankplatz 1 in Aarau, which also falls under the cantonal regulations for large consumers and therefore also has to meet specific requirements. Markus Dietwiler, Head of Operational Services, monitors the most important parameters at AKB's largest site and is responsible for optimising them.**

## Heating energy

By switching from gas to district heating, CO<sub>2</sub> emissions have been cut by around 100 tonnes per year over the past two years. A groundwater heat pump powered by natural electricity generates 90 per cent of the district heating, and a gas boiler is also available at peak times to cover energy needs.

## Electricity

Electricity consumption, 97 per cent of which is covered by green electricity, has also been in decline for years. The main reasons for this are the use of energy-saving motors for the ventilation systems and district cooling for the building. The annual reduction in electricity used by the ventilation systems corresponds to the average electricity consumption of 24 single-family homes. Total electricity consumption was also reduced by around 21 per cent compared with 2019. The building technology's share of total electrical energy consumption was reduced from 35 per cent to 24 per cent in 2020.

The energy measurement concept in use at the main building shows the major sources of consumption over time, as well as the points of interest both graphically and in different colours. In 2020, this electricity recording system was also extended to other AKB branches. This form of monitoring has now been introduced and is in operation at

one third of all sites. Integrating the measurement concept into the Bank's network also facilitates location-independent access and rapid intervention.

## Looking to the future

AKB will continue to work hard at realising savings and optimisations in building technology and is expanding the number of measuring points. Besides monitoring the systems, this also increases the informative value of the consumption data as fewer extrapolations are made.

However, there are also limits on making further significant savings. AKB is only a tenant in around 50 per cent of its offices and, for example, cannot influence the type of heat generation as this is determined by existing gas or oil heating systems. However, it can still achieve further improvements through reductions and savings or the use of an additional heat pump to reduce the share of fossil energy.

AKB will reduce its ecological footprint in stages as it implements its strategy to conserve resources.



# What does...

## **transparency in the investment business actually mean?**

For AKB, sustainability is a promise that it has been making for more than a decade. Trust, security, customer proximity, sustainable growth and the responsible use of natural resources are at the heart of this. The investment arena is another area where the Bank can make further progress. AKB applies ESG criteria when assessing and evaluating investments. The ESG criteria have become established as a standard and describe three sustainability-related areas of responsibility that a company has: The “E” stands for the environment. This includes topics such as climate risks, environmental pollution, scarcity of resources and ecological opportunities and risks. The “S” stands for “social” and covers social topics such as occupational safety, health protection or the social commitments of a company. The last letter “G” stands for “governance” and this deals with the topic of sustainable corporate governance.

When obtaining data, AKB relies on sound analysis by MSGI ESG, one of the world’s leading rating agencies in the area of sustainability. Over 200 analysts evaluate ESG indicators on the basis of a transparent model, helping to create clarity for investors. AKB therefore offers a contemporary investment philosophy in line with social expectations.

## **Sustainable engagement in everyday banking life?**

AKB also addresses issues such as e-waste. Modern workplaces for over 800 employees need IT equipment to be replaced time and again. Simply disposing of discarded equipment is an option, but not a very sensible one and it is certainly regrettable. That is because a lot of the time the devices are not really old or no longer usable. AKB has therefore been on the lookout for two suitable partner companies to take care of the processing and reuse of the material. Gisler Systems AG has either professionally disposed of around 200 AKB printers or refurbished them so that they can be used as second-hand devices by private individuals or start-up companies. “AfB social & green IT” – a non-profit foundation to create work for

people with disabilities – acquires discarded computers, monitors and other hardware from AKB and also refurbishes them for further use. Through these two partnerships, AKB supports the social and ecological development of society.

## **Offsetting CO<sub>2</sub> emissions?**

Earth Overshoot Day took place on 22 August 2020, more than three weeks later than in the previous year due to Covid-19. From this day, the world’s population consumes and uses more resources than the Earth can replenish in the course of the year. One aspect under particular scrutiny because of its harmfulness to the climate is the CO<sub>2</sub> footprint. What would be ideal is to lead a climate-neutral lifestyle. However, that is effectively impossible, especially for the population of an industrialised country. Even with the best of efforts, it is impossible in this country to reduce emissions to a level that would be tolerable for the Earth. But there is also some good news: emissions can be offset. Unlike air pollution, it does not matter how and where CO<sub>2</sub> gets into the atmosphere and where it is later removed from it. Various companies make use of such offsetting options. AKB has supported the Aargau Foundation’s “Fair Recycling” climate protection programme since 2013 and offsets its annual CO<sub>2</sub> emissions against climate certificates from an environmentally friendly refrigerator recycler in Brazil. By funding this offsetting project, AKB is helping to combat climate change through its climate neutrality.

# How AKB's sustainability is perceived by the public

In the summer of 2020, AKB conducted an assessment in cooperation with Demoscope of how the Bank is perceived externally in terms of its sustainability. The survey focused on how the population in the market area views AKB, what demands are placed on the Bank in terms of sustainability issues and what the situation is with regard to specific stances on values and claims. To identify any changes in perception, the survey will be repeated at the end of the strategy period 2021-2024. This is especially true given AKB's new strategic goal of being considered the most sustainable bank in the canton by 2024.

90%

of respondents consider sustainability an important or quite important issue.

78%

of respondents consider sustainable behaviour by their bank to be important or quite important.

68%

of AKB customers consider their bank to be sustainable.

22%

of respondents have purchased sustainable financial products.

50%

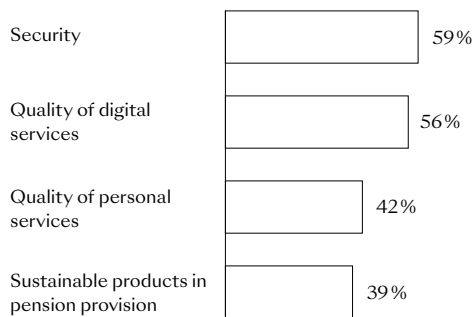
of the respondents consider AKB's range of sustainable financial products to be adequate or quite adequate.

47%

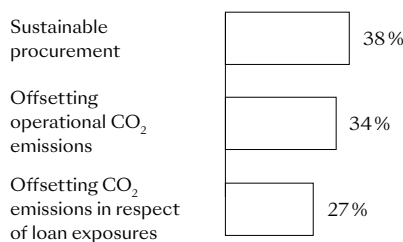
of respondents perceive AKB to be a sustainable bank.

## What are the most important aspects of sustainability?

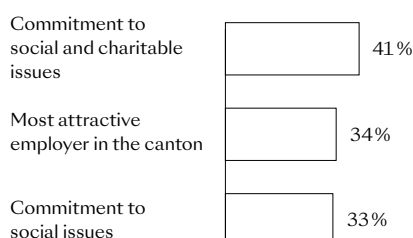
### Core business in percent



### Ecology in percent



### Social in percent



# Green Bonds

**In summer 2020, AKB became only the second Swiss bank to issue a green bond in CHF with a volume of CHF 100 million. Demand for these green bonds is high. The market is growing and private investors are also taking an interest. The green bond is a bond where AKB undertakes to use the funds exclusively to finance the AKB green mortgage. Sustainably focused investors can therefore team up with the projects of ecologically active developers. AKB launched both products – the green bond and green mortgage – as part of its conviction to also position sustainability in its core business and to further expand it in the future.**

## Fast placement

The green bond was placed very efficiently and successfully with a wide range of investors in the market, with demand far outstripping supply. What was behind this success? The main reason was that there is a still small but dynamic market in Switzerland which incorporates environmental topics and combines them with highly transparent reporting. This includes compliance with the Green Bond Process Guidelines of the International Capital Market Association (ICMA), which sets clear requirements for disclosing the funds received. The external auditors ISS ESG certified the allocation criteria for AKB. It also provided information about the green bond's ecological aspects or, more broadly, its sustainable creditworthiness.

## Market conditions play an important role

This creates transparency, which is extremely important in the context of sustainability. Besides the general trend towards more sustainability in finance, another reason for the successful placement was the yield being slightly positive and the AKB green bond's issue volume of CHF 100 million. The assessment of the state of the market was the only uncertain factor on launch day. However, this also turned out to be positive, both for the investors and for AKB. The timing for a placement of the green bond was therefore excellent.

## More on the horizon

In recent years, the market for green bonds has evolved from a small niche into a liquid and diversified segment in several different currencies. Green bonds are similar to conventional bonds in terms of pricing. In view of numerous new "green" initiatives and increasing environmental awareness in society, the market for green bonds is expected to continue growing rapidly. AKB's green product range will be added to in stages and the Bank will look at expanding it into other business areas. Those looking to achieve an environmental dividend and financial return have come to the right place.

# “The new strategy sets new standards.”

**AKB will revise its credit guidelines over the coming months and integrate the sustainability approach of the new 2021-2024 strategy into the financing area. Silvio Tedone, Head of the Credit Expertise Centre, casts light on why a revision is necessary, what the main components are and what is the most important focus for him personally.**

## **Why will AKB be revising its credit guidelines?**

We usually amend the credit guidelines once or twice a year to bring them into line with current market conditions. But the amendments this time round go further. AKB has set itself the goal of being the most sustainable bank in the canton by the end of 2024. This target is very ambitious, especially for our core business – lending. The credit guidelines are our most important set of rules in the lending business, guide our actions in practice and are binding on all employees. We are therefore anchoring the new sustainability principles in this set of rules.

## **What were the biggest challenges in this realignment?**

The new strategy sets completely new standards. The biggest challenge is to convince our employees and our clients to act. New principles and regulations, especially in the field of sustainability, should not simply be thought of as technical guidelines. They represent a change of direction in our way of thinking. Together with my colleagues from all areas of the Bank, we are working very hard to ensure that this realignment is understood and made a reality.

## **What are the main components of the revised credit guidelines?**

An important new tool of the sustainability principles in the credit sector are the exclusion criteria. They exclude “problematic” industries and business activities from lending altogether. Over the course of the year, ESG criteria will play an important role when deciding on a specific loan (Note: ESG refers to the consideration of environmental, social and governance criteria). We want to see how our SME customers deal with issues such as

environmental pollution, fair working conditions and diversity. Environmental and energy aspects will also be given greater consideration when appraising the value of real estate.

## **Have some measures already been implemented and when will the new credit guidelines be fully active?**

The first version is expected to come into force in the first quarter of 2021. It already includes important exclusion criteria. Refinements in this direction will gradually follow over the course of the year.

## **How will things change for AKB customers?**

That’s easy to answer: customers who think and act sustainably will be rewarded and gain access to attractive products and conditions.

## **Are there any other measures in the pipeline for the lending and financing business?**

Sustainability is also playing a very important role in product development. In 2020, we launched the AKB green mortgage for energy-related investments in the domestic sector and issued our first green bond at the same time. By the end of 2020 alone, more than half of the limited volume had been distributed. We’ll soon be launching another product that will once again take sustainability to a new level. The focus will be on long-term relationships with our customers so they can continue to live in their own homes in old age without having to worry.

## **As Head of the Credit Expertise Centre, you are an expert in the financing business. What for you personally is the most important aspect about the new direction AKB is taking?**

We cannot expect to suddenly “activate” or even impart a sustainable attitude to life. We are on a path and change will come one step at a time.

