### Key Figures for KfW Bankengruppe

In EUR million

<table>
<thead>
<tr>
<th>Year</th>
<th>2003</th>
<th>2004</th>
<th>2005</th>
</tr>
</thead>
<tbody>
<tr>
<td>I KfW Mittelstandsbank</td>
<td>13,796.7</td>
<td>13,971.2</td>
<td>15,520.1</td>
</tr>
<tr>
<td>Loan financing</td>
<td>9,013.0</td>
<td>9,209.3</td>
<td>10,673.7</td>
</tr>
<tr>
<td>of which: Global loans to trade and industry</td>
<td>2,313.2</td>
<td>2,144.8</td>
<td>2,553.7</td>
</tr>
<tr>
<td>Mezzanine financing</td>
<td>986.1</td>
<td>619.8</td>
<td>583.1</td>
</tr>
<tr>
<td>Equity financing</td>
<td>341.1</td>
<td>341.1</td>
<td>300.1</td>
</tr>
<tr>
<td>Securitisation</td>
<td>3,484.4</td>
<td>3,728.4</td>
<td>3,063.3</td>
</tr>
<tr>
<td>II KfW Förderbank</td>
<td>44,851.5</td>
<td>34,438.9</td>
<td>38,687.5</td>
</tr>
<tr>
<td>Housing investment</td>
<td>15,442.2</td>
<td>11,929.5</td>
<td>10,503.6</td>
</tr>
<tr>
<td>of which: Global loans to the housing industry</td>
<td>2,607.0</td>
<td>2,008.0</td>
<td></td>
</tr>
<tr>
<td>Education</td>
<td>727.9</td>
<td>811.6</td>
<td>875.0</td>
</tr>
<tr>
<td>Municipal infrastructure</td>
<td>4,682.7</td>
<td>4,195.3</td>
<td>2,730.4</td>
</tr>
<tr>
<td>Environmental protection investment</td>
<td>4,020.8</td>
<td>2,165.5</td>
<td>4,241.6</td>
</tr>
<tr>
<td>Global credit lines for promotional institutions in the federal states</td>
<td>1,528.1</td>
<td>3,936.5</td>
<td>3,625.2</td>
</tr>
<tr>
<td>Securitisation</td>
<td>18,398.8</td>
<td>11,430.6</td>
<td>16,271.7</td>
</tr>
<tr>
<td>Investment finance in Germany and Europe</td>
<td>58,648.2</td>
<td>48,440.1</td>
<td>54,207.4</td>
</tr>
<tr>
<td>III KfW IPEX-Bank</td>
<td>11,526.7</td>
<td>11,914.7</td>
<td>12,148.1</td>
</tr>
<tr>
<td>IV KfW Entwicklungsbank</td>
<td>1,594.1</td>
<td>1,943.9</td>
<td>1,899.3</td>
</tr>
<tr>
<td>V DEG</td>
<td>505.9</td>
<td>562.8</td>
<td>671.8</td>
</tr>
<tr>
<td>Total financing volume</td>
<td>72,274.9</td>
<td>62,861.5</td>
<td>68,927.2</td>
</tr>
<tr>
<td>Business volume</td>
<td>402,341</td>
<td>426,484</td>
<td>454,201</td>
</tr>
<tr>
<td>Balance sheet total</td>
<td>313,894</td>
<td>328,596</td>
<td>341,143</td>
</tr>
<tr>
<td>Capital and reserves</td>
<td>9,339</td>
<td>11,055</td>
<td>13,559</td>
</tr>
<tr>
<td>Net income for the year</td>
<td>247</td>
<td>356</td>
<td>625</td>
</tr>
<tr>
<td>Staff numbers</td>
<td>3,670</td>
<td>3,077</td>
<td>3,800</td>
</tr>
</tbody>
</table>

Differences in this table are due to rounding.

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THE IMPACT OF OUR PRODUCTS – AIMING FOR SUSTAINABLE GROWTH. 42

Protecting the environment and the climate.
– Promoting environmental and climate protection – an overview. 43
– Climate protection in housing construction. 45
– Promoting renewable energies. 46
– Climate protection and resource efficiency in enterprises. 47
– KfW Carbon Fund – a new instrument. 50
– Protecting the climate and reducing vehicle emissions. 51
– Preserving biological diversity. 54

Economics and society.
– Stimulating structural change and employment. 56
– Education – an asset for better job prospects. 58
– Effectively promoting gender equality. 59
– Focus on health and quality of life. 60
– Foundations/compensation funds. 62
– Peace building, disaster relief and reconstruction. 62
– No development without human rights. 65

IN-HOUSE ENVIRONMENTAL PROTECTION – ALL RESOURCES IN VIEW. 66

Review, current status and future outlook.
– How we understand in-house environmental protection. 67
– Key figures for the years from 2003 to 2005 in retrospect. 68
– Objectives targeted and achieved. 70
– Highlights of in-house environmental protection. 71
– KfW objectives for 2006 - 2008. 73
– Measures already under way. 75
– Special topic: CO₂ neutrality at KfW Bankengruppe. 77

Auditor’s report PwC. 78
Glossary. 80
Imprint. 81

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The Federal Ministry for the Environment, Nature Conservation and Nuclear Safety was established twenty years ago, at the time of the Chernobyl disaster. Since that time many of Germany’s environmental problems have been solved. Nowadays, we take clean water and unpolluted air virtually for granted, while in other parts of the world careless handling of these natural resources is even beginning to hinder economic growth.

As climate change and the progressive loss of biodiversity show, worldwide we are still overusing fossil fuels and other raw materials – and our children will be the ones to suffer. We therefore still have a long way to go before we have achieved globally sustainable development of the earth.

We can only succeed in meeting this challenge if we can achieve a balance between environmental protection, economic growth and social development. A modern, intelligent sustainability policy which reflects that view is also a policy for the future.

To continue to achieve economic success in the future with resources that are becoming increasingly scarce, we need a sustainability policy that also drives innovation. Nowadays, Germany’s competitiveness is more than ever dependent on how willing we are to strike out along new paths. In the future, enterprises that adopt forward-looking approaches to dealing with social and ecological issues will enjoy clear competitive advantages in the global marketplace.

I consider KfW Bankengruppe to be one of those enterprises already. Its expertise and financial resources make it a key partner of the federal government in implementing the German sustainability strategy. As a member of the Board of Supervisory Directors, I am sure that KfW Bankengruppe, as a bank representing both the federal government and the federal states, will go on to further strengthen its commitment to sustainable development in Germany and throughout the world.
Living and promoting global responsibility – that is the leitmotiv running through KfW Bankengruppe’s first Sustainability Report. Together with our Annual Report, it provides a comprehensive overview of what KfW stands for and what it does. We used to publish an Environmental Report once every three years. We have now broadened its scope in order to produce a Sustainability Report. In addition to the topics of promoting environmental protection and active commitment to the environment by KfW Bankengruppe, for the first time this Report covers the Bank’s commitment to social policy in Germany and our partner countries, personnel policy and aspects of corporate governance. Through this report, we are addressing our stakeholders in all sections of society – our shareholders and strategic partners from the worlds of politics and business, those who take advantage of our offers, our employees and the general public.

Publishing an 80-page report on these issues emphasises the importance that we attribute to the concept of sustainability as well as to transparency and communication. Our aim is, first, to provide information about and to account for what we have done in this area in the past three years at both national and international levels and, second, to explain the principles and convictions that lie behind our activities.

We always have a dual function – as long-term promoters and as professional bankers. With a balance-sheet total of more than EUR 340 billion, KfW is one of Germany’s ten largest banks. We work professionally and in line with market conditions like a commercial bank, but we are very different from other banks. Our legal mandate is to use the opportunities open to us as a promotional bank to foster economic and social change. These are demanding and ambitious goals which underpin everything we do and, at the same time, act as our benchmark. The sustainability strategy of the German federal government is the guideline for how we exercise our social responsibility.
Entrepreneurial action must be combined with responsibility. That is particularly true for KfW. We understand responsibility fully in terms of sustainability. Using the resources and opportunities available to a promotional bank, our aim is to help people to improve their economic, social and ecological conditions of life. Behind that lies, for example, the conviction that economic activities can only be successful in the long term if supported by appropriate social conditions and if appropriate consideration is given to social and ecological aspects. We are aware that today, in the age of globalisation, responsibility can no longer be defined merely at the national level. For us, it is self-evident that responsibility must be placed in a global context and that it must then be lived out and promoted consistently at the global level. This starts with the fact that KfW is active in more than 90 countries and has representative offices in 50 countries and, at our locations in Germany, people from 28 different countries are working together successfully.

So as not to lose sight of the major objective of sustainable development, we follow the “KfW Compass” in our everyday working life. It summarises our guiding values and visions, which are given concrete expression in many individual projects. New environmental and social principles applying throughout the entire KfW Group enforce compliance with appropriate standards and the systematic evaluation of the ecological and social risks of our projects.

Responsibility goes hand in hand with credibility. That is why we have set high standards in in-house environmental protection, for instance. To show that we practise what we preach, we have made the entire KfW Group CO₂ neutral as from 2006. However, our standards do not only apply to climate protection. Our major objective is to see sustainability thinking firmly established in all core processes at KfW Bankengruppe. This year, therefore, we have undertaken to follow the Principles for Responsible Investment from now on when investing our own liquid funds.

This report sets out to provide comprehensive information. It is also an invitation to strengthen dialogue with us and to foster the discussion in society about important issues for the future. If this report is also taken as an encouragement to pay more attention to the subject of sustainability in general, it has undoubtedly fulfilled its purpose.

[Signature]
KfW Bankengruppe provides support for the economy wherever the free interplay of market forces is not enough on its own to foster growth, employment and hence prosperity. In addition to its headquarters in Frankfurt am Main, the Bank has branches in Berlin and Bonn. The main DEG office is located in Cologne.

KfW is owned by the German federal government (80%) and by the federal states (20%). Its tasks are enshrined in the Law concerning KfW. Governed by the basic principle of conducting its business in a goal-oriented and efficient manner and in line with market conditions, it promotes small and medium-sized enterprises as well as business start-ups, home ownership and modernisation, training, environmental and climate protection, project and export financing and provides support for developing and transition countries. Its work is always competition-neutral. KfW and eight affiliates together form the KfW Group; six of the companies in the Group are included in its consolidated accounts.

The Bank refinances most of its promotional loans in the capital market. Profits are channelled back into promotion and used to safeguard the promotional potential over the long term. With a balance sheet total of around EUR 340 billion (as at 31 December 2005), KfW Bankengruppe is one of the ten largest banks in Germany.

KfW Bankengruppe has packaged its range of tasks as five brands:

1. **KfW Förderbank** provides low-cost funding as a means of promoting the housing sector, environmental protection, municipal infrastructure and social tasks; the wide range of programmes is geared to enterprises, private individuals and municipalities. In addition, KfW Förderbank is active in the educational sector and grants loans for academic studies and advanced vocational training.

2. **KfW Mittelstandsbank** grants promotional loans to foster investment by small and medium-sized enterprises. In cooperation with banks and savings banks it provides support for business founders, self-employed professionals, innovators and SMEs by way of classic loans, equity solutions and mezzanine financing. In addition, KfW Mittelstandsbank operates an advisory service for small and medium-sized enterprises in matters related to financing.

This symbol indicates that further information on this subject can be viewed on our website: www.kfw.de/sustainability-report.de
3 **KfW IPEX-Bank** is a strong, innovative partner for German and European enterprises in project and export financing. Important areas of business are energy, the environment, and rail, air and sea transport. As of 2008 KfW IPEX-Bank will be operating competitively as an independent subsidiary of KfW Bankengruppe with all the rights and obligations of a bank.

4 Acting on behalf of the German Federal Ministry for Economic Cooperation and Development (BMZ), **KfW Entwicklungsbank** finances investment and accompanying advisory services in developing countries. It uses federal budget funds as well as its own funds to promote the development of the social and economic infrastructure, the establishment of reliable financial systems, protection of the environment and natural resources, and programmes to support economic and administrative reforms. As a rule it works together with state institutions. KfW Entwicklungsbank takes the United Nations Millennium Declaration and the Millennium Development Goals as its central guidelines.

5 **DEG**, a 100% subsidiary of KfW, is one of the largest development financiers in Europe for long-term project and corporate financing. It has been financing and structuring investment by private companies in developing and emergent countries for over 40 years. Its instruments are equity investment, mezzanine financing, long-term loans and guarantees at market-based conditions. The focus is on establishing and expanding private sector structures with the aim of creating sustainable economic growth and a lasting improvement in the quality of life for the local people.
SUSTAINABILITY - IT IS ALL ABOUT RESPONSIBILITY.
PRINCIPLES AND VALUES.

From the day on which it was founded nearly 60 years ago, KfW Bankengruppe has been conscious of its responsibility in society. Although the term “sustainability policy” had not been coined at the time, right from the start the Bank took upon itself the task not merely of working out solid principles and values but of consistently keeping to them and living them out. The thinking was that later generations should also be able to benefit from them.

As a bank owned by the German government and the federal states, KfW gears its decisions to the federal government’s sustainability strategy, which it uses as a kind of leitmotiv. This also comes through in KfW’s “Statement on environmental protection and sustainable development”, which it presented to the Bundestag. In that document, the Bank reaffirms its obligations arising from the UNEP Statement by Financial Institutions on the Environment and Sustainable Development.

Sustainability is also a key value built into the Group image ("KfW Compass"), which acts as a guide for KfW employees in their daily work. The values and attitudes that it presents make a vital contribution to global responsibility being lived out and promoted by every employee in the KfW Group.

KFW CONTRIBUTIONS TO THE GERMAN GOVERNMENT’S SUSTAINABILITY STRATEGY.

The aims of the German government’s sustainability strategy are generational equality, social cohesion and global responsibility. The government has developed a system of indicators that is intended to make it easier to implement its sustainability strategy and develop it further. The indicators are a means of measuring Germany’s contribution to sustainable development. The table “The federal government’s sustainability indicators” lists the indicators and points to the interfaces with KfW activities. It clearly shows that KfW is making a major contribution to achieving the sustainability goals.
The federal government’s sustainability indicators.

<table>
<thead>
<tr>
<th>Indicator</th>
<th>Contribution by KfW</th>
</tr>
</thead>
<tbody>
<tr>
<td>Generational equality</td>
<td></td>
</tr>
<tr>
<td>1 Resource conservation</td>
<td>x</td>
</tr>
<tr>
<td>Energy productivity</td>
<td></td>
</tr>
<tr>
<td>Raw materials productivity</td>
<td>x</td>
</tr>
<tr>
<td>2 Climate protection</td>
<td>x</td>
</tr>
<tr>
<td>Reduction in greenhouse gas emissions</td>
<td></td>
</tr>
<tr>
<td>3 Renewable energies</td>
<td>x</td>
</tr>
<tr>
<td>Shares of renewable energies in energy consumption</td>
<td></td>
</tr>
<tr>
<td>4 Use of available space</td>
<td>x</td>
</tr>
<tr>
<td>Increase in settlement and transport areas</td>
<td></td>
</tr>
<tr>
<td>5 Biodiversity</td>
<td>x</td>
</tr>
<tr>
<td>Numbers of selected bird species as an indicator of biodiversity</td>
<td></td>
</tr>
<tr>
<td>6 Government debt</td>
<td>x</td>
</tr>
<tr>
<td>State deficit</td>
<td></td>
</tr>
<tr>
<td>7 Economic provision for the future</td>
<td>x</td>
</tr>
<tr>
<td>Ratio of gross fixed capital formation to gross domestic product</td>
<td></td>
</tr>
<tr>
<td>8 Innovation</td>
<td>x</td>
</tr>
<tr>
<td>Private and public research and development expenditure</td>
<td></td>
</tr>
<tr>
<td>9 Education</td>
<td>x</td>
</tr>
<tr>
<td>Educational status of 25-year-olds</td>
<td></td>
</tr>
<tr>
<td>New students rates</td>
<td>x</td>
</tr>
<tr>
<td>10 Economic prosperity</td>
<td>x</td>
</tr>
<tr>
<td>Gross domestic product per capita</td>
<td></td>
</tr>
<tr>
<td>11 Mobility</td>
<td>x</td>
</tr>
<tr>
<td>Transport intensity of passenger and goods transport</td>
<td></td>
</tr>
<tr>
<td>Shares of railways and inland shipping in goods transport services</td>
<td></td>
</tr>
<tr>
<td>12 Food</td>
<td>x</td>
</tr>
<tr>
<td>Surplus nitrogen in agriculture</td>
<td></td>
</tr>
<tr>
<td>Development of the area used for ecological agriculture</td>
<td></td>
</tr>
<tr>
<td>13 Air quality</td>
<td>x</td>
</tr>
<tr>
<td>Air pollution level</td>
<td></td>
</tr>
<tr>
<td>14 Health</td>
<td>x</td>
</tr>
<tr>
<td>Premature death (cases of death under the age of 65)</td>
<td></td>
</tr>
<tr>
<td>Satisfaction with health</td>
<td></td>
</tr>
<tr>
<td>15 Crime</td>
<td></td>
</tr>
<tr>
<td>Burglaries</td>
<td></td>
</tr>
<tr>
<td>Social cohesion</td>
<td></td>
</tr>
<tr>
<td>16 Employment</td>
<td>x</td>
</tr>
<tr>
<td>Percentage of the workforce</td>
<td></td>
</tr>
<tr>
<td>17 Family perspectives</td>
<td>x</td>
</tr>
<tr>
<td>Provision of day care nurseries for children in western Germany</td>
<td></td>
</tr>
<tr>
<td>18 Gender equality</td>
<td>x</td>
</tr>
<tr>
<td>Average wages for women as a % of the average wage for men</td>
<td></td>
</tr>
<tr>
<td>19 Integration</td>
<td></td>
</tr>
<tr>
<td>Foreign school-leavers without a secondary school leaving certificate</td>
<td></td>
</tr>
<tr>
<td>Global responsibility</td>
<td></td>
</tr>
<tr>
<td>20 Development cooperation</td>
<td>x</td>
</tr>
<tr>
<td>Public development cooperation</td>
<td></td>
</tr>
<tr>
<td>21 Opening up markets</td>
<td></td>
</tr>
<tr>
<td>Exports to the EU from developing countries</td>
<td></td>
</tr>
</tbody>
</table>

The indicators under the main headings “Generational equality” and “Social cohesion” (indicators 1–19) refer to Germany only. For this reason, there is no entry for some indicators such as biodiversity, although we are active in those areas in the context of development cooperation (indicator 20).
ENVIRONMENTAL AND SOCIAL PRINCIPLES.

Our new principles describe how sustainability policy is implemented at KfW Bankengruppe. They go further than the previous environmental principles, incorporating concerns connected with internal and external relations as well as corporate governance and compliance issues.

The emphasis is on our legally established promotional mission, which places KfW “hors concours” in the banking world. The issues that are covered relate to the objectives of KfW, the signature of international agreements, the consideration given to social aspects and environmental protection in the range of services provided, human resources policy and social benefits, corporate governance and corporate citizenship. The statements concern responsibility in business operations as well as internal operational measures and implementing and communicating the principles.

The new principles have laid the foundation for bank-wide social responsibility models that are applicable to all KfW fields of activity and subsidiaries but still leave suitable room for manoeuvre.

SUSTAINABILITY COMMUNICATION FOR MORE TRANSPARENCY.

The sustainability policy and strategy is fully documented and communicated. The important models referred to above also include this Sustainability Report, which KfW is publishing for the first time this year as a replacement for the previous triennial Environmental Report.

KfW also keeps the public informed about its environmental and social activities in its Annual Report and the joint Annual Report published by KfW Entwicklungsbank and DEG. In addition, reports are included in various publications, presentations are given on the further development of the Bank's work on environmental and social issues, and information stands are set up at conferences and similar events.
Stakeholder dialogue.

In accordance with its “Statement on environmental protection and sustainable development”, KfW presents an annual report to the Board of Supervisory Directors on its environmental management and what it has achieved in the area of environmental protection. Numerous events on current environmental and social developments provide a useful platform for an exchange with the worlds of politics and academia as well as with non-governmental organisations (NGOs) and customers. This exchange helps to further develop benchmarks and procedures for use in environmental and social concerns. However, it is also useful for the development of new promotional instruments and agreement on concerted promotional activities. For example, the agreement on a standard approach to environmental protection at the level of international development cooperation is coordinated in the Environment Working Group of the OECD Development Support Committee (DAC); KfW is a member of that group.

Bonn Platform for International Cooperation.

The aim of the discussion series is to stimulate the specialist and critical dialogue in development cooperation; the meetings are held in cooperation with the Deutsche Welle. The first meeting was held in late November 2004. This series of events provides an opportunity for experts from KfW Entwicklungsbank, the BMZ, business and academic circles, and NGOs to discuss current development policy issues.

Sponsorship.

Sponsorship is an integral part of KfW’s PR work. Public sponsorship projects that are closely linked to the Bank’s promotional mission are selected. The wide variety of sponsorship activities reflects the range of KfW’s tasks. The Bank is involved in sponsoring cultural activities specifically for the umbrella brand KfW Bankengruppe.

“Highly efficient coal-fired power plants, wind farms, double hull tankers and airbuses with a low fuel consumption are among the export hits today. That is perhaps one of the most lasting economic successes of European climate and environmental policy. It is good business for us, too, as commercial export and project financiers. However, we are very aware of the fact that the use of environmentally friendly technology can have negative side effects. In order to deal with these risks we are constantly updating the IPEX Environmental and Social Guidelines and seeking dialogue on them. At our Environment Day 2005, we also sought to exchange experience with non-governmental organisations (NGOs).”

Dr Peter Klaus, Member of the Board of Managing Directors of KfW Bankengruppe and Chairman of the Board of Managing Directors of KfW IPEX-Bank
In-house dialogue.

Various communication measures are helping to establish the objectives of the Group image ("KfW Compass") firmly at the Bank. Special events, for example, allow a regular in-depth exchange to take place between Board members, management staff and employees. Discussion forums on specific sets of topics from the Compass encourage implementation of the values. An internal suggestion procedure encourages employees to do what they can to uncover potential areas for improvement within the Bank and to enhance its promotional strength over the long term.

Employees also have the specific task of observing the environmental and social guidelines. Unless employees understand the goals and can identify with the guidelines, commitment to environmental and social topics is bound to fail. KfW is therefore investing in staff training on these issues.

The Central Environmental Unit regularly holds training courses in the environmental management system (UMS) for new employees and trainees. Training courses on how to deal with environmental and social issues in actual practice are held at KfW IPEX-Bank, KfW Entwicklungsbank and DEG. Environmental and social issues are also a regular feature of the staff magazine “Einblicke” and the Intranet news page “Einblicke Online.”

Sponsorship: Africa Alive Festival.

KfW has been sponsoring the Africa Alive Festival in Frankfurt for a good number of years; in 2004 the festival celebrated its tenth anniversary under the motto "History and stories of Africa". The festival is organised each year by a team comprising African associations, Frankfurt cultural establishments and private individuals from the Rhine-Main region. The cultural festival is one of the few in Europe which provide a platform for African creative artists of all kinds, giving them an opportunity to present their works, ideas and visions in person and to shed light on the history of Africa. Attracting an audience from a broad cross-section of people of various nationalities, the festival makes an important contribution to integration in multicultural Frankfurt. The programme includes films, concerts, readings, exhibitions, events for children and teenagers, and political platforms. UNESCO declared Africa Alive 1996 a project in the World Decade for Cultural Development. In 2001 the festival was the official German contribution to the UN Year of Dialogue between Cultures. In 2002 and again in 2003 its patron was the German section of UNESCO.
ORGANISING RESPONSIBILITY – MANAGING PROCESSES AND ENCOURAGING EMPLOYEES.
KfW’s environmental management system (UMS) manages, measures and controls two areas: the environmental and social impact of projects and in-house environmental protection, to which a chapter of this report is devoted. The effectiveness of UMS is continuously being reviewed and improved. The following chart illustrates how UMS fits into the organisational picture and the workflow.

The project appraisals are based on the environmental and social guidelines developed by the Environmental Coordination Group for the individual fields of activity.
An environmental and social review is an integral part of every project appraisal in developing and emergent countries. Project risks for people and the natural environment have to be weighed against project benefits and specific measures need to be taken to avoid, mitigate or offset them. In its business operations, the Bank will not provide financing for projects which are likely to have unacceptable ecological or social repercussions.

More than 40 technical experts from a variety of disciplines can, if necessary, be called in from any of the Bank’s business areas to accompany projects through all the stages of their development. External skills are used, where necessary, to complement the Bank’s own expertise.

The environmental impact assessment is the main instrument used to ensure that projects are designed and executed in an environmentally sound manner. In line with standard international practice, social aspects such as forced resettlement, cultural heritage or indigenous population groups are taken into consideration. Further internal KfW guidelines on how to take account of social aspects such as gender equality can be built in to the assessment. An expanded environmental and social impact assessment means that co-financed projects can be systematically reviewed for possible negative impacts. It can also define protection and offsetting measures, which are subsequently monitored.

"As a 100% subsidiary of KfW Bankengruppe, DEG makes an active contribution to establishing international environmental and social standards in developing and emergent countries. We do this by cooperating closely with the project partners as the project unfolds. This includes monitoring as well as giving advice. In the context of a systematic compliance review we examined all our current projects to see whether they comply with contractually agreed environmental and social requirements and standards. Not one of the projects indicated a need to take direct steps to deal with environmental or social risk. One very positive sign is that the projects newly approved in 2005 demonstrated 93% compliance with the internationally recognised environmental protection standards established by the World Bank and international social standards or will achieve compliance in the course of the project. In two-thirds of the cases special environmental effects such as more efficient use of resources were achieved."

Dr Winfried Polte, Chairman of the Board of Management of DEG
In all its fields of activity, KfW gears its project appraisals to the legal requirements of the countries in which the projects are to be conducted. If the legislation in the project countries in question does not go far enough, the standards set by the EU, the OECD and the United Nations as well as the regulations of the World Bank Group and the core labour standards of the International Labour Organization (ILO) are taken as the benchmark.

Appraisal and monitoring procedures are transparent. In the case of projects that are particularly environmentally and socially sensitive, this includes, first and foremost, informing the local people and ensuring their participation. KfW consistently gives serious consideration to critical objections to individual projects. We also understand stakeholder dialogue to mean transparent ex post reporting, as carried out by the independent evaluation unit at KfW Entwicklungsbank, for example.

The scope of the reviews and opportunities for action vary from one field of activity to another. As a general rule, KfW Entwicklungsbank accompanies projects from the early stages and insists on the project design being environmentally and socially acceptable, providing additional promotional funding where appropriate. KfW IPEX-Bank and DEG, too, finance only those projects that are environmentally acceptable and meet social standards. Their guidelines ensure that projects are environmentally and socially acceptable. The following project report illustrates clearly the extent of measures that can accompany commercial projects.
Island in the sun.
KfW IPEX-Bank finances the construction of a coal-fired power plant on Mindanao.

In the north of Mindanao, the second largest island in the Philippines, a new coal-fired power plant is currently being built on 56 hectares of industrial land in the town of Villanueva. The total cost of building the plant is USD 305 million, USD 42 million of which is covered by a KfW IPEX-Bank loan granted in 2003. Subsidies have not been required. Construction began in December 2003 and commercial operation is set to begin in December 2006.

The power plant feeds into the public electricity supply and when working at full capacity it will provide 15% of the island’s electricity. It will thus largely replace highly inefficient electricity production by outdated diesel generators.

The power plant is being built and operated by STEAG State Power Inc (SPI), a project company which is 89% owned by STEAG AG, a German power plant construction and operating company, and 11% owned by a Philippine investment company, State Investment Trust Inc (SITI).

Coal-fired power plants are criticised for emitting greenhouse gases and polluting the air. Non-governmental organisations therefore often suggest that industrialised and developing countries use only renewable energies when carrying out the necessary upgrading and development of their energy production structure. However, to be realistic, without subsidies renewable energies are not yet fully economical – which is true, for example, for many locations where wind energy is being produced. Another problem is that in many places, the resources cannot be expanded further; a simple example is the major resistance encountered by new hydropower plants.
The World Bank has acknowledged this and, when formulating strategies to promote “cleaner”
energies in developing countries, it is now emphasising the key significance of options that are
as effective as possible and, at the same time, low in cost. In so doing, it is clearly fostering the
use of modern, efficient coal-fired power plant technology. The power plant in Villanueva
makes use of modern energy production technology and has two steam boilers with a gross
electricity output of 116 MW. It burns low-sulphur coal in low-NOₓ burners with an efficiency
of 36.1%.

Conceivable negative environmental effects caused by the construction and operation of the
power plant were reviewed thoroughly by a well-known independent technical consultant – PB
Power from New Zealand. In every case, conformity with local Philippine and World Bank
standards was affirmed, particularly with regard to the important aspects of pollutant emission,
coal dust pollution and water heating. The consortium supplying the plant has signed
an agreement to comply with the standards. To ensure that this is more than just a piece of
paper, the emission levels of NOₓ, SO₂, particles and noise are measured continuously by an
independent enterprise at eight measuring stations. The chemical composition of the coal and
ash is also analysed regularly. In addition, groundwater, surface water and sea water samples
are taken and analysed. Non-compliance with the threshold values can lead to compulsory
shutdowns.

Technically speaking, the high environmental and climate protection requirements in this
project are guaranteed by, inter alia, the high energy efficiency of the power plant in converting
coal into electricity, a flue gas desulphurisation plant, a tube filter system for the dust in the
flue gas and special storage of the fly ash produced during the burning process at a dump near
the power plant so that the groundwater is protected. Furthermore, the cooling system is so
designed as to ensure that the warm sea water is fed back in accordance with World Bank
standards, thus avoiding any harmful warming. A team – comprising representatives of the
operating company, the environment and nature conservation ministry, the regional environ-
mental and nature conservation authority, non-governmental organisations, citizens associ-
ations and the municipalities concerned – is in charge of monitoring compliance with all
regulations.

A fund financed by the project company caters for an information, educational and communi-
cation programme that is geared, for example, to the local people, municipalities and NGOs. It
helps to ensure that people are informed about the impact of the power plant on the environ-
ment and the measures that are taken to offset and guard against any damage.
These measures include:

– Planting some 5,000 mangrove seedlings in close proximity to the power plant;
– Mapawa forest conservation programme to develop 1,200 hectares of timber and protected forest in the hills close to the provincial capital of Cagayan d’Oro;
– Forestry project in Villanueva for the reforestation of 500 hectares of urban land;
– Forestry project along a 500 hectare stretch of the Tagaloan River to prevent riverbank erosion.

The measures are being financed from another fund, the Environmental Guarantee Fund, which is co-financed by the project company.

So that the major project has no negative social repercussions for the local people, they were integrated into a prior consultation procedure. This consultation procedure complied with World Bank standards and Philippine guidelines – a matter which was expressly checked by the technical consultant. In all, 131 families had to be resettled but all of them agreed to be rehoused and were given compensation in accordance with World Bank standards, i.e. suitable alternative housing, farmland and monetary compensation.

However, the operators did more than strictly observe the World Bank standards or compensate those who were directly affected; they implemented in parallel an extensive social programme for which the project company provided USD 416,000 in funding (until the end of 2006).

– SPI supports the Villanueva Water Works Project. This support is not a legal requirement; it has been given voluntarily. SPI granted a loan of USD 130,000 to support the project.

– Training 400 people from Villanueva in manual skills so that they can find work on the building site; setting up a day nursery for some two dozen children in San Roque.

– Cookery and management courses for local women; 14 women are now successfully running their own canteen service (“Villa Kusina”).

– Four medical/dentistry missions in Villanueva and Tagoloan; some 1,250 families take advantage of these facilities every year.

Of no minor significance, substantial employment effects are connected with the project. In the construction stage more than 3,200 jobs were created. For STEAG it is important to create as many opportunities as possible for the local people to earn an income and it is giving Philippine engineers jobs in long-term plant operation.
Risk management at KfW Bankengruppe includes managing counterparty risk, market price risks (interest and currency risks), liquidity risks and operational and legal risks. In addition, the management of operational risks is becoming increasingly important.

Supervisory law defines operational risk as “the risk of direct or indirect loss resulting from inadequate or failed internal processes, people and systems or from external events”. The Capital Requirements Directive “Basel II” calls for capital cover to counter operational risk and for it to be appropriately integrated into the bank’s risk management system. In the course of a project, KfW has therefore collected data on the risks that may occur in individual areas. In addition, events were organised at all locations to inform staff fully of the issues involved.

The Bank has contingency plans to maintain its business operations – including the assessment of projects for environmental and social acceptability. There is a comprehensive contingency plan, for example, for dealing with an influenza epidemic. Among other things, the plan allows for a stock of medicines to be set up for its employees.

The quality management system (QMS) comprises three important pillars: quality standards, complaints management and ideas management. Entrepreneurial success is inconceivable unless we offer high quality products and services. Even if quality is an unwritten law at KfW, KfW Bankengruppe set up a central bank-wide QMS in 2006. The aim is to increase customer satisfaction further still and to maintain an ongoing improvement process.

Complaints management plays a key role in the QMS. It defines how we actively deal with breakdowns in the relationship between KfW and its customers. We respond to complaints quickly and appropriately; they are therefore handled in a decentralised manner by the departments concerned. As these complaints may also pinpoint operational weaknesses or market opportunities, they are analysed centrally in the QMS.
At KfW, ideas management goes by the name of “Compass Competition”. In the competition suggestions are taken for measures which, for example, can help to save materials, energy and work or are intended to improve customer relations. Of course, ideas can also be submitted by individual staff members or a team about the areas in which they work. If the suggestions lead to a quantifiable benefit they are acknowledged with a percentage-based financial reward. If, however, the financial benefit cannot be quantified, a fixed-rate financial award is made for the suggestions. In addition, each year a jury selects five prizewinning suggestions from all those submitted during the year.

COMPLIANCE ALSO MEANS SECURITY.

Compliance is the term generally used to refer to the voluntary, regulatory and legally prescribed requirements and measures needed to avoid conflicts of interest between a bank, its employees and its customers. Compliance procedures ensure that a bank adheres to all applicable laws, rulings and customary practices. The Federal Ministry of Finance supervises KfW in consultation with the Federal Ministry for Economics and Technology (BMWi) and is responsible for ensuring that KfW’s operations are in line with the laws, statute and other legal provisions. The Internal Auditing Division at KfW, which functions as an instrument of the Board, appraises the effectiveness and appropriateness of the risk management and the internal controlling system. In addition, an independent audit is carried out by a firm of external auditors. The Federal Audit Office can then conduct an extensive review of how KfW manages its resources.

Compliance is structured to include, in particular, systems to prevent money laundering, the financing of terrorism, corruption and fraud as well as violations of data protection laws, insider trading regulations and embargo provisions. We update those systems regularly to keep them in line with the underlying legislation and market requirements. Compliance training courses are arranged for all new members of staff.

At KfW there is a Compliance Division which deals with these matters and is the contact point for all staff members. Other interested parties can e-mail the division at Compliance@kfw.de.
FOCUSING ON STAFF.

KfW’s staff are our greatest source of potential, which is why, contrary to the general trend in the banking sector, there have been further moderate staff increases at KfW over the past three years. The Bank thus maintains a balance between three essential objectives: safeguarding existing jobs, expanding the staff in a way that is commensurate with the volume of business and ensuring that the development of personnel costs is well under control. At the end of 2005 KfW Bankengruppe had a staff of 3,800. Above-average growth was related to the establishment of KfW IPEX-Bank. The merger with DtA took place in the period under review, 2003-2005. Adjusted to take account of the merger, the increase in staff was just over 3% per annum. This increase is also related to KfW’s positive image as an employer. Furthermore, our corporate and management culture has also helped to put us in a leading position in employer rankings over the past three years.

“The merger with DtA led to numerous synergies. Nevertheless, contrary to the general trend in the banking world, there has so far been no mention of operational redundancies at KfW and the intention is for things to stay like that – which is particularly welcome news for the staff representative bodies. Our employees therefore have long-term job security.”

Percentage of disabled staff members still above legal requirements.

The percentage of KfW staff who are disabled is unchanged at just under 6%. At KfW disabled people are taken on as trainees or employed in various positions throughout the Bank, dealing with anything from administrative matters to market operations. This has advantages for both the employers and employees. The Bank sees them as making a productive contribution to the business results while the disabled persons acknowledge the attractive professional opportunities that are open to them. In the future, too, the Bank will increase the number of disabled employees as staff numbers grow, so that the percentage of disabled employees will remain above the legally required level.
Personnel structure in the light of the intensive promotion of women.

At 49%, the percentage of women on the staff is still high. The Bank has set itself ambitious goals in its gender equality plans to make a distinct increase in the percentage of women among staff not covered by collective wage agreements and in management. Overall, in the period under review the percentage of staff not covered by collective wage agreements has remained relatively high, particularly because of the changes to the employment contracts of staff of the former DtA which were rendered necessary by the merger. The current figure is 64% (2003: 68%). The percentage of women in this high share of staff not covered by collective wage agreements has gone up from 37% to 38% in the past three years. The promotion of female staff is far more clearly seen with regard to a second criterion. The potential assessment procedure and the specific promotion of qualified female staff has led to a steady growth in female executive staff – from around 17% in early 2003 to more than 22%. The percentage of women at the lowest management level has gone up from 20% to 27% in the past three years. This development is a necessary prerequisite for increasing the percentage of women in upper management. The objectives of the gender equality plan cannot be implemented in the short term. They depend on staff increases and fluctuation at management levels. This is not automatic in times of task-related and cost-conscious staff planning. In this respect the Bank is in an economically favourable position, which means that it can continue to pursue the ambitious objectives of the equality plan in the years ahead.

DEG has been included in the genderdax run by the IPA Institute for Human Resource and International Management at the Helmut Schmidt University in Hamburg. The genderdax pays tribute to enterprises which are particularly active in promoting gender and diversity measures and provides an information platform for well-qualified women.

Job-sharing in management positions – a pilot project to promote combining motherhood with a career.

Young mothers in management positions expressed the wish to work part-time for a period and therefore looked for a suitable partner with whom they could work in tandem. The Human Resources Department and their own management gave them their support. In particular, the Board gave its backing to this development and actively encouraged its furtherance. By 2005 five “tandems” were in operation. These arrangements are boosting the motivation and flexibility of the job-sharing partners, enabling them to look after their children and to pursue a career at the same time.
Combining a job and a family.
KfW in Frankfurt has had a company kindergarten and flexitime for more than 30 years, and since 1994 it has also had a staff agreement making it easier to combine a job and a family. The agreement offers generous opportunities for parents to take time out to bring up their children, to look after relatives or to further their own education. The bank has been involved in the audit on combining a job and a family since 2001. The re-audit in 2004 led to staff policy being made even more family-conscious.

As one aspect of the KfW project aimed at making it easier to combine a job and a family, around 65 members of staff are taking advantage of teleworking opportunities. The advantages of teleworking are that it is easier to combine private and professional life, time can be saved that would otherwise be lost in getting to and from work, and the home atmosphere is possibly quieter and perhaps also more creative. The advantages for the Bank are that its staff are more motivated, that it does not need to provide expensive office space and that it saves on travel expenses.

Frankfurt Alliance to Promote the Family.
KfW Bankengruppe has been actively involved in the Frankfurt Alliance to Promote the Family since 2005. The aim of the Alliance is to set up projects that make it possible to achieve a better balance between work and family life. The Bank’s involvement enables it to benefit from the experience of others and to pass on its own findings to other enterprises and the city of Frankfurt.

A parents’ association made up of Bank staff was actively involved in setting up a multilingual crèche for 45 children, the Jardin Palmito. KfW contracted Le Jardin, a company specialising in implementing the educational concept of an international, multilingual nursery. The parents’ association is responsible for ensuring adequate enrolment and the basic financing. The local alliance of the Bundesbank, the City of Frankfurt and KfW fill the remaining financing gap, thus ensuring the continuous integration of the project into the public life of Frankfurt.
More vocational training than needed.

Training is an area to which KfW traditionally pays a lot of attention. The Bank is particularly conscious of its social responsibility towards the younger generation. The number of places for trainees increased steadily in the period under review. At the start of the training year in autumn 2005, there were 139 trainees in the initial vocational training programme, compared with 92 in autumn 2003. In the period under review the number of trainees went up from 46 to 57. With a trainee rate of 5.7% (2003: 4.2%), KfW is providing far more training than is actually needed.

The bank is particularly concerned to ensure that those who complete their course have a good chance of finding a job. There is a clear trend towards opting for a dual training system combining practical training periods with academic studies at a higher education institution. KfW trainees can study at various higher education establishments. In the future far more high-school graduates will be admitted to these dual courses of study and therefore fewer to the traditional bank apprenticeships. Hence, KfW will not only respond to the greater internal demand for quality but also to the labour market opportunities and needs of young people.

STRATEGIC PERSONNEL MANAGEMENT PLANNING.

Growth and change at KfW Bankengruppe has led in recent years to an increase in staff numbers and locations. With several subsidiaries and more than 20 divisions to deal with, the need to ensure that personnel management retained its customer closeness and efficiency meant that we had to rethink our human resources policy. In December 2003 KfW set up a new management committee to deal with strategic human resources work, the Human Resource Board (HRB). The aim of the HRB is to devise a uniform, strategically oriented human resources policy for KfW Bankengruppe. The Board of Managing Directors and representatives of the in-house departments, DEG and the Berlin and Bonn offices come together in the HRB, which is chaired by the Human Resources Department. The HRB's mandate is to coordinate and discuss strategic human resources planning. In general, the HRB makes recommendations.
JOB SECURITY AND HEALTH PROTECTION MEAN
A BETTER QUALITY OF LIFE.

The tasks of the in-house medical service include providing occupational medical care, medical examinations to ensure that staff are fit to travel in tropical countries, and regular eye tests for staff members.

From time to time, the company doctor and the corporate safety officer tour the premises to check ergonomics and safety aspects at the workstations. There is also a wide range of health courses and sports groups on offer.

Influenza immunisation is available to staff every year; in 2005 the offer was taken up by more than 900 members of staff.

Conflict at the workplace can also be the cause of health problems. There are therefore social advisers at each location; they work with the company medical service to advise the staff members concerned.
OUR PRODUCTS –
BROAD OFFER AND OPTIMAL ADVICE.
CAPITAL AND PROMOTION.

The financing offers of KfW Bankengruppe are designed in such a way as to ensure that we offer the right product for every capital need. However, our promotion covers more than finance; mediation and advisory services – mostly provided free of charge – are becoming an increasingly important part of our work. KfW offers its partners a consistent and transparent service from a single source.

FINANCING FOR ALL TYPES OF CAPITAL NEED.

In the period under review, large parts of KfW's financing offer were revised and overlaps eliminated. The wide range of products now includes loan, mezzanine and equity financing, asset securitisation, grants and information services. KfW's promotional instruments usually focus on the customer's investment activity. The objective is not only to support environmentally and socially acceptable projects but also to promote competitive and economically sound investments that advance structural change and thus strengthen the social market economy.

In Germany, in particular, the aim is to tackle the persistently high level of unemployment, which is one of the most pressing problems. To achieve this aim, the first priority must be to increase the demand for labour. Investment activities by small and medium-sized enterprises, which have traditionally been the job engine of the German economy, play a decisive role. However, especially when financing job-creating investments, small and medium-sized enterprises (SME) often have huge obstacles to overcome. Only promotional programmes that take account of changing framework conditions will be able to support SME financing in the long run.

If highly complex financial products such as securitisation are used in this area, their impact – in terms of job creation, for example – needs to be explained. The following description of KfW's financing instruments therefore sets out to show the possibilities as well as the limitations for KfW in carrying out its mission.
**Long-term promotional loans.**

Long-term loans at favourable long-term interest rates are the Bank’s main promotional instrument. The interest rates available to customers are at the lower end of the market range. Low-interest loans help to correct financing disadvantages due, for example, to company size or higher investment costs for particularly environmentally sound technologies. The repayment obligation ensures that funds are only provided for economically viable projects. Depending on the promotional objective, interest rates on “conventional” long-term loans can be reduced further or the loans otherwise modified. For example, a greater reduction in interest rates can be made in the CO₂ Building Rehabilitation Programme and a repayment bonus can be granted for particularly energy efficient projects.

**Risk-adjusted interest rate system.**

As the financial markets have continued to change, internal rating systems have become firmly established throughout the banking industry. Today, banks are in a position to calculate risk-adjusted interest rates for all companies. Especially for SMEs with a lower credit standing, the uniform credit margin that used to be customary was no longer sufficient to cover the administrative and risk costs of the on-lending bank. In such cases banks and savings banks refused to grant loans in order to avoid losses. To counteract this development KfW introduced risk-adjusted interest rates in most of its financing programmes. Risk-adjusted pricing enables banks to grant loans at cost-covering rates. In this way companies are given better access to promotional loans, their investment capacity is strengthened and, finally, jobs will be safeguarded and new ones created.

**Private equity and mezzanine financing.**

If innovation is to be encouraged, it is of prime importance to provide venture capital for technology-oriented companies at the early stage of business development. In the past few years KfW has increasingly focused its promotional activities in the equity capital market in Germany on the early stage segment. Since 2005 KfW has been providing increasing support for innovative business start-ups through the ERP Start-up Fund and the High-Tech Start-up Fund, the latter having been set up jointly with the German government and partners in industry. KfW’s programmes also help to attract private market participants to the early stage as a special segment of the venture capital market.
KfW has also expanded its mezzanine financing offers. The possibility of financing innovation projects through mezzanine capital in the form of subordinated quasi-equity loans means that a broad range of mezzanine products is now available to SMEs. Through its subsidiary DEG, KfW also offers venture capital instruments to enterprises in developing countries.

**Innovative instruments strengthen our promotional performance.**

To enable KfW to maintain or even further increase its promotional performance in the future, new innovative instruments need to be created. These instruments include global loans, credit lines, programme-based joint financing, securitisation, project financing and public private partnerships.

**Global loans for Europe.**

Global loans for the low-interest refinancing of SME or housing loans supplement KfW’s classic promotional programmes and simplify the financing process. KfW Bankengruppe extends a large global loan to a partner bank to enable it to finance eligible projects instead of granting individual refinancing loans for each customer. The partner bank uses the global loans to on-lend tailor-made individual loans to small and medium-sized corporate customers or private customers.

To support the integration of the European single market, since 1992 KfW has advised 18 transition countries in Eastern Europe on the establishment of 15 promotional banks. It offers global loans to promotional and commercial banks in other European countries for the promotion of SMEs and other promotional purposes. To achieve an effective blend of European and national promotional instruments, in Central and Eastern Europe funds provided by the European Union are increasingly being combined with KfW global loans.
Credit lines for developing countries.
To support small and medium-sized enterprises in developing countries, KfW Entwicklungsbank extends credit lines via state and private banks in the partner country. These credit lines are sometimes combined with grants to cover advisory services, for example. KfW Entwicklungsbank’s environmental credit lines are used to provide long-term refinancing for environmental protection investment in the partner countries. However, the refinancing lines also serve to strengthen banks in the partner countries. Better access to financial services is provided and an effective instrument for reducing poverty is thus created. Support for the financial sector in developing and transition countries is a priority area in the work of KfW Entwicklungsbank and DEG; in 2005 it accounted for more than 30% of the commitments.

Cooperation with partners in the financial sector: DEG workshop in Bangkok.
Long-term lending through partner banks and acquiring stakes in them also helps to establish the principles of in-house environmental protection and a socially just development in the economy of the partner countries. To achieve this goal, DEG requires the partner banks to implement appropriate management systems.

At the end of 2005 DEG organised a workshop to provide support for its customers in the financial sector in Asia on how to deal with environmental and social aspects and risks. The objective was to highlight the strategic importance of risks in the environmental and social areas and to inform the participants of possible ways to introduce effective environmental and social management systems in their organisations. The DEG workshop was attended by representatives of 14 financial institutions, including commercial banks, investment funds and leasing companies from countries such as China, India, Bangladesh, Indonesia and Vietnam.

The workshop was the first in a series of events in a two-year programme initiated by DEG to support its customers in the introduction and further development of environmental and social management systems. DEG and experienced international consultants give the participants intensive assistance and individual support.
Programme-based joint financing in developing countries.

An innovative instrument at KfW Entwicklungsbank, which helps donors to achieve greater harmonisation of their policies, is programme-based joint financing, through which several donors jointly finance a spending programme of a developing country in the health, education or transport sector. The precondition is that the donors have confidence in the efficiency of the authorities of the country concerned and consider the political objectives worthy of support.

The challenge is that the customary procedures and appraisals have to be conducted jointly with the other donors and other proprietary procedures may not be used. In addition, the programmes financed need intensive joint support from all donors to limit fiduciary risks. Controlling tasks, as well as the continuous monitoring of reforms at state and sector policy levels, are new challenges which KfW has to address more intensively than in the past.

Securitisation.

KfW has successfully set up securitisation platforms and thus given a major boost to the German securitisation market. Securitisation is a financial market innovation which has been used in Germany since the mid-1990s. In a securitisation transaction a pool of comparable assets such as mortgage loans or corporate loans are transformed into tradeable securities. In this way a bank can transfer the risks related to its loan portfolio to the capital market, making equity available for new loans to SMEs or for housing investment. This is a way of creating or safeguarding jobs. An expert opinion prepared for the EU Commission on the impact of securitisation on SME financing confirms that KfW has successfully contributed to the establishment of a securitisation market for SME credit risks.

Looking to the future, the objective of KfW is to open up this market to a broader range of companies.
**Project financing.**

Large investment projects are becoming more important in the field of project financing. Loans are granted for projects conducted by project companies that are set up especially for this purpose. Financing is provided for a self-sustaining economic entity, the project. The debt service is served solely or at least primarily from the project cash flow.

**Public private partnerships.**

In the case of public private partnerships (PPPs) or private finance initiatives (PFIs), private investors or operators work closely together with the public sector in the financing operation. Public private partnerships are used as a financing instrument in development cooperation, too.

**Cotton made in Africa.**

Acting on behalf of the BMZ, DEG has been implementing the public private partnership programme since 1999. It is entering increasingly into strategical alliances with several partners with the aim of achieving a correspondingly broader developmental impact. At the end of 2005, for example, the “Cotton made in Africa” alliance was established on the basis of an initiative of the Otto Group in Hamburg. DEG can contribute its long experience of project financing in the cotton sector. Other project partners are GTZ, the German textile company Tom Tailor, Deutsche Welthungerhilfe, the WWF and cotton producers in Africa. The aim is to help to strengthen the demand for cotton from Africa and to create a transparent value-added chain as well as to introduce a certifiable, marketable production standard that complies with ecological, economic and social criteria. At the same time, the intention is to safeguard the income of a large number of smallholders.
SUSTAINABLE INVESTMENT WITH THE GREATEST POSSIBLE SECURITY.

KfW is one of the major bond issuers in the world. It offers investors a broad range of investment opportunities with regard to maturity, interest rate structure and currency. KfW bonds are noted for being extremely safe; they are covered by a guarantee of the Federal Republic of Germany and have an AAA rating.

Socially responsible investors have recently been increasing their prominence in the capital market. Independent rating agencies have been commissioned by these investors to assess enterprises according to socially responsible investment (SRI) standards. KfW Bankengruppe is regularly evaluated by several national and international rating agencies with regard to its socially responsible approach.

In analysing sustainable business management, the rating agencies first apply positive criteria (qualitative screening) and, second, exclusion criteria are reviewed. In the latter procedure, which is also referred to as "negative screening", an analysis is also carried out to establish whether the issuer is actively involved in "negative" sectors such as the armaments industry, the production of alcohol or tobacco, or gambling. If an enterprise is found to be involved in one of these areas, investors are unable or unwilling to invest in securities issued by that enterprise.

Qualitative screening for banks such as KfW is usually carried out on the basis of the criteria of "ecological responsibility in lending and in internal operation", "social responsibility towards staff, customers, service providers and society" and "corporate governance". In addition, financing projects that are a subject of public controversy are presented.

In the analysis, the rating agencies evaluate publications by the issuers, media reports and information provided by other organisations. KfW is invariably one of the front-runners among the bond issuers appraised. KfW can therefore offer extremely safe as well as sustainable investment opportunities. This is even more so because, in evaluating the exclusion criteria, the rating agencies also regularly confirm that KfW is not involved – or at the most, only marginally – in critical sectors.

At present, the market for sustainable investments in Germany is still relatively small but will become considerably more important in the future. This is particularly evident from the situation in Scandinavian countries, the Netherlands and the United Kingdom, where far more attention is being paid to socially responsible investment (SRI). Owing to KfW's specific
statutory mission, its business model and its outstanding ratings, KfW bonds are predestined for purchase by this group of investors. Against that background, KfW will also be taking greater account of this investor group when deciding how to gear its operations in the years ahead.

Evidence of the increasing importance of socially responsible investment is also given by the initiative of the United Nations General Secretary Kofi Annan on Principles for Responsible Investment (PRI), which he launched early in 2005 and which, following signature and publication in April 2006, meant that a key milestone had been reached. Institutional investors agreed on six principles which deal with how to take account of environmental and social concerns and matters of corporate management and control in their investment activities.

As KfW is also an investor and purchases securities for the purpose of liquidity and equity management, it welcomes this initiative. In 2006 it decided to join the initiative and to apply socially responsible trading principles to its future investments.

"The mission and self-image of KfW require it to operate in a sustainable and socially responsible manner. The bonds that we as KfW place in the international capital market for our refinancing purposes are therefore an appropriate basic investment for socially responsible investors. Wherever we buy securities ourselves, our aim is also to follow the criteria of sustainable investment and we will therefore be implementing the Principles for Responsible Investment from now on."

Dr Günther Bräunig,
Member of the Board of
Managing Directors
of KfW Bankengruppe
MEDIATION AND ADVICE AT EVERY STAGE.

KfW promotion is not only about financial resources. Advisory services – which are usually provided free of charge – are becoming increasingly important. The advisory services available in the field of SME promotion, for instance, cover all business development stages – advice at KfW Consultation Days and at the KfW Advisory Centres on selecting and applying for financing; KfW start-up coaching and the mediation opportunities known as the “Consultant Exchange” (Beraterbörse) and “Franchise Exchange” (Franchisebörse) as a means of preparing for a successful business launch; the nexxt-change business exchange, which acts as a marketplace for business successors; and, finally, the “Round Table” and “Turn Around” advisory services intended to ensure that businesses can keep going in crisis situations.

Successor Exchange.

For years the demographic development has been creating a problem for German SMEs; a broad generational change is immanent and many enterprises have made no provision for it. If the business is not handed on promptly and efficiently, jobs will be at stake. To make it easier for enterprises to find successors and to support potential successors in finding a suitable enterprise, entrepreneurs who wish to pass on or take over a business can be put in touch via the Germany-wide internet exchange nexxt-change. KfW is working on this exchange with the BMWi (the initiator) and other institutions¹ that focus on promoting the SME sector. There are around 700 regional partners mediating between sellers and buyers.

¹ Association of German Chambers of Industry and Commerce (DHIK); German Confederation of Skilled Crafts (ZDH); Bundesverband der Deutschen Volks- and Raiffeisenbanken (BVR); German Savings Bank Association (DSGV); www.nexxt-change.org.
Crisis advice.

Enterprises that are receiving promotional assistance do not always develop in a positive manner. If an enterprise finds itself in payment difficulties, the impact on jobs at the enterprise is usually negative. For that reason every enterprise in difficulties is first examined to determine whether it can be saved. It must present a restructuring strategy that has been appraised by a consultant and indicates that restructuring has a chance of success.

In such cases, the advisory instrument employed by KfW Mittelstandsbank is the “Round Table”, an initiative implemented in conjunction with the chambers of industry and commerce and the chambers of trade. All parties which may be able to contribute to avoiding the crisis are brought together around a table. Before all those concerned come together at the “Round Table”, a business consultant analyses the company’s situation and presents the results in a matter of days. The cost of this check is borne by KfW Mittelstandsbank. Only those consultants which have provided KfW with evidence of their suitability are eligible for this task. The analysis is taken as the basis for working out a solution. All those concerned must ultimately agree on the planned measures. The “Round Table” has so far helped around 26,000 SMEs and self-employed professionals to avoid insolvency – which also means that some 260,000 jobs have been saved.
“SUSTAINABILITY FOR THE BENEFIT OF PRESENT AND FUTURE GENERATIONS”
INTERVIEW WITH JÜRGEN H LOTTMANN

Mr Lottmann, in the course of your professional career you have often addressed the guiding principle of sustainable development. Is the fact that this term is imprecise or used in too many different ways a hindrance to its implementation?

Yes and no. In many respects the concept of sustainable development is very precise. However, this precision is not particularly welcome. You only have to think of calls for public budgets to be managed so that no burdens are placed on future generations. The arbitrary use of the term dates back to the Rio de Janiero conference in 1992, which stressed both resource conservation and economic growth. Since then efforts have been made to define these objectives more precisely, to weigh them up against each other and perhaps to harmonise them. In addition, many other generally agreed concerns have been placed under the umbrella of sustainability, although – strictly speaking – they are not directly related to that issue, e.g. calls for participatory democracy. In my view, right at the heart of concept is the need for present-day economics and politics to take account of the material needs of younger generations today and in the future. That also means that we have to make sacrifices today. That is not easy, as we all know.

What sustainability concept do you consider particularly appropriate to meet these challenges?

In my view, the most usable concept is the federal government’s sustainability strategy. Everyone wishing to tackle the principle of sustainably and its realisation in Germany in a practical manner has to start with this concept although its actual implementation is not compulsory. That also applies to enterprises. If they do not actively join in, it is difficult to see how we can move towards greater sustainability.

Does KfW Bankengruppe have a particular role to play?

It is quite deliberately taking its direction from the federal government’s sustainability strategy. However, as a public sector bank KfW Bankengruppe can only do so much to ensure its implementation. The Bank is part of the economic system, meaning that, ultimately, what it achieves is only as sustainable as that system. As part of that system, however, KfW can promote the changeover to sustainable structures if it has the instruments and resources to do so at its disposal.
Let us take a look at actual assessment practices. As a KfW staff member, you were repeatedly involved in projects that were based on using finite supplies of raw materials. Was that always sustainable?

As a government-owned bank, KfW basically has to comply with Germany’s energy and raw materials policy and assess projects designed by business enterprises. These projects and the energy and raw materials policy are not only geared to the principle of sustainability. Just think of the many gas-fired power plants built in the past decade that burn the finest fossil fuel, which, as far as we can tell, is in limited supply. From the perspective of environmental protection, gas is naturally a good option today, because coal, oil and nuclear power each come with their own environmental problems. KfW also finances ore and metal extraction, although we all know that these resources are finite.

What can KfW do to resolve this dilemma?

KfW cannot address the issue of finite resources on its own but it can help to promote resource-conserving technology at home and abroad. The most successful example, in my opinion, is the support provided for energy savings in Germany’s real estate and the worldwide promotion of renewable energies. Another quiet success, but one with long-term effects, is the setting-up of credit lines for banks in developing countries with the aim of converting highly pollutant industrial plants to better procedures. This is often one way of actually introducing the task of industrial environmental protection.

How can KfW improve its assessment of the environmental and social impact of projects abroad?

In foreign commercial business, we could first of all expand the monitoring of projects that are particularly environmentally and socially sensitive. Monitoring means periodically reviewing the actual environmental approach, from which lessons can be derived for the future. At present KfW Entwicklungsbank rarely finances industrial or infrastructure projects with a considerable environmental and social impact. The focus is on financing projects with the aim of achieving the Millennium Development Goals, particularly poverty reduction. In recent years it has also become apparent that in the future those funds which invest in “sustainable” enterprises will play a greater role in determining how we assess and report on the environmental and social
acceptability of our projects. That is a sensible long-term trend that KfW should support because it also makes a contribution to implementing the principle of sustainable development.

Do you think that "sustainability people" will prevail over people who are concerned purely with economic success?

No, at least not in my lifetime. First, because it is not a question of individuals but of the economic system. Second, because, from the experience that I have gathered over the past 30 years or so, those with the political responsibility find it very difficult to dismantle and rebuild the economy's system of objectives. The current predominant system of objectives involving shareholder value and quarterly reporting cannot anticipate shortages that will only become critically apparent in a few decades' time. That means shortages for our children and grandchildren – the intended beneficiaries of the principle of sustainable development.

Following his employment at the German Federal Ministry of the Interior from 1976 to 1985, Jürgen H Lottmann was general manager of the German Advisory Council on the Environment (SRU). He was then head of the department for emission control and general environmental matters at the Environment Ministry in the federal state of Hesse. In 1988 he transferred to KfW. As the head of the Central Environmental Unit, his tasks included monitoring projects abroad for environmental acceptability. For many years he also chaired the Scientific-technical Committee at the Forschungszentrum Karlsruhe and, on a voluntary basis, was a member of the jury for the Blue Angel environmental label. Mr Lottmann has now entered retirement and since July 2005 he has been working as a freelance expert both in Germany and abroad.
THE IMPACT OF OUR PRODUCTS – AIMING FOR SUSTAINABLE GROWTH.
PROTECTING THE ENVIRONMENT AND THE CLIMATE.

The effects of financing programmes are always complex. The intended direct impacts are always accompanied by indirect effects. Promoting environmental protection, for example, is not only of benefit to the environment. A study recently published under the aegis of the Institute for Futures Studies and Technology Assessment and others clearly shows that product-integrated and production-integrated environmental protection also pays off commercially for investors. Enterprises that put resources to use efficiently are more productive than others.

On closer examination, it becomes clear that promoting investment in environmental protection does more – it achieves positive impacts in the area of business development and encouraging innovation, in promoting structural change and economic development, and in the creation of employment which, in turn, secures income and reduces poverty.

Environmental protection ensures, for example, the sustainable use of natural resources and preserves the natural basis of life of people who rely on those resources. Environmental protection projects reduce air, water and soil pollution and thus contribute to a healthy, inhabitable environment. These examples show that protecting the environment not only has an economic dimension but a social one, too. Hence environmental protection must always be understood as a holistic contribution to sustainability.

PROMOTING ENVIRONMENTAL AND CLIMATE PROTECTION – AN OVERVIEW.

In the past three years the promotion of environmental and climate protection has regularly achieved a share of roughly 20%\(^2\) of KfW Bankengruppe's total volume of commitments. This underscores its exceptional importance as a cross-cutting task for the Bank. Overall, from 2003 to 2005 KfW Bankengruppe made EUR 29 billion in loans available for these purposes (see Table “KfW financing for environmental and climate protection”).

Financing for renewable energy technologies and energy conservation measures was around EUR 17.7 billion, which represented 85% of the domestic lending volume for climate and environmental protection. KfW is thus making an important contribution to achieving the climate protection objectives in Germany.

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\(^2\) Excluding securitisation transactions.
Climate protection is a primary objective that extends across all KfW's fields of activity. We apply various instruments to ensure that greenhouse gas emissions remain within acceptable limits – from the financing of housing through development cooperation to the KfW Carbon Fund. The severe climate changes show that new thinking is necessary – not only because oil, natural gas and coal reserves are limited but because of the atmospheric impact of burning these fossil fuels. The solution can only consist in using traditional sources of energy more sparingly and efficiently and making greater use of renewable energies.
The German federal government has therefore approved a national climate protection programme. It specifies what action needs to be taken in the sectors not directly affected by emissions trading, such as private households, transport, trade, commerce and services. The National Climate Protection Programme aims to reduce greenhouse gas emissions by 21% between 2008 and 2012, with 1990 as the reference year. KfW’s programmes are a major component of this German climate protection programme.

“Highly innovative technologies and services are being developed to protect the climate. Unlike KfW’s “conventional” innovation financing for suppliers, KfW is also encouraging innovation in climate protection through financing on the demand side. This applies to highly efficient heating technology, renewable energy, geothermal heat pumps, innovative ventilation systems or passive house technology. To put it in a nutshell, promoting the use of renewable energy and energy efficiency also means promoting innovation.”

CLIMATE PROTECTION IN HOUSING CONSTRUCTION.

In Germany the lion’s share of primary energy is consumed in the home. This is where the greatest savings can be achieved. Of the 30 million homes that were built in Germany prior to the Second Ordinance on Thermal Insulation of 1984, only five million have been completely renovated. For this reason climate protection is also a prime objective of the Bank’s housing finance programmes. Here KfW has set standards of its own. The energy-saving houses KfW 40 and KfW 60 are now well-established energy-saving architectural concepts. Nearly EUR 8 billion was committed for the renovation of home energy systems and new ecologically designed homes between 2003 and 2005.

Under the federal government’s national climate protection programme, the aim is to reduce CO₂ emissions in private households by some five million tonnes by 2010; the emissions are mainly generated by residential property heating. By adding to the promotional funds as part of the “Housing, Environment, Growth” initiative, a reduction of at least 2.5 million tonnes in
annual CO₂ emissions may well be achieved, i.e. half the national reduction target. The under-
lying programmes are thus, in Germany, by far the most effective and most significant climate
protection measures for residential properties.

PROMOTING RENEWABLE ENERGIES.

The international Renewables Conference held in Bonn in 2004 tackled the question of how
to substantially increase the share of renewable energies in industrialised and developing
countries. At the end of the conference a comprehensive international action programme was
adopted. One of Germany’s most important contributions to this action programme is KfW’s
Special Facility for Renewable Energies and Energy Efficiency.

Under the Special Facility KfW Entwicklungsbank will grant low-interest loans up to a total of
EUR 500 million for projects in developing and transition countries. These funds will be provided
for investment dedicated to promoting the use of renewable energies and improving energy
efficiency. KfW will grant the loans and bear the loan risk. The German federal government allo-
cates funds to the BMZ budget to make these loans more affordable for developing countries.

According to a World Watch Institute report, KfW Entwicklungsbank is one of the three largest
financiers of renewable energies in developing countries. DEG, too, is financing the con-
struction of private wind farms, run-of-river power plants and geothermal power plants in
developing countries. Between 2003 and 2005 the Power, Renewables, Water Division of KfW
IPEX-Bank provided more than EUR 580 million in financing for renewable energy projects
worldwide.

KfW’s domestic financing operations are also outstanding by international standards. From
2003 to 2005 KfW Förderbank provided a total of around EUR 8.4 billion to finance the use of
renewable energies; EUR 3.6 billion of this amount was allocated in 2005 alone. KfW’s financ-
ing activities will become even more important in the future. In the face of rising energy costs,
stepping up the diversification of electricity and heating supply in Germany by speeding up the
development of renewable energies is a high priority on the energy policy agenda.
Industrial pollution control is being increasingly based on process-integrated procedures. Downstream end-of-pipe technologies are being replaced wherever possible. Innovative processes, for instance, are making it possible to confine potentially hazardous substances to the operational cycle. Other technologies are based on a more sparing use of raw materials and energy or on the use of raw materials that are compatible with the environment.

Promotion of renewable energies by KfW Entwicklungsbank – biogas plants in Nepal.

Inhabitants of rural areas in Nepal still mainly use wood for cooking and heating. Three-quarters of Nepal’s total energy consumption is attributed to this traditional source of energy. Smoke and soot cause eye and respiratory diseases, particularly among women and children. Depletion of the forests is eroding the soil and increasingly destroying the people’s basis of life.

The Nepalese government has been promoting the construction of biogas plants since 1975. Since 1997 it has been supported by KfW Entwicklungsbank with EUR 15 million from the BMZ budget. The plants supply gas for stoves and lamps. A farmer can operate one of these plants if he has at least two cows. The household latrines are also connected to the system. The fermented slurry produced in this way is composted, turning it into valuable fertiliser. To date 100,000 biogas plants have been installed under the project, and an additional 200,000 systems are to follow by 2009.

The funds are lent on to the local system builders by the Agricultural Development Bank of Nepal. A portion of the funds is granted in the form of construction subsidies. The farmers are the contractors; they participate in building the plants and later operate the systems. They thus bear a significant share of the total programme costs.
Under the prevailing market conditions, forward-looking investments of this kind are not always being rewarded. They often require higher investment amounts when they incorporate environmental aspects. KfW’s aim is to make it easier for investors to decide in favour of environmental protection. Between 2003 and 2005 KfW committed nearly EUR 1.2 billion for investment in production-integrated or product-integrated environmental protection.

The potential of manufacturing enterprises to conserve resources is often underestimated. According to a study conducted by the Centre for European Economic Research (ZEW), German enterprises are lagging behind their international counterparts in energy and resource efficiency. The decisive approach to changing this must come from the entrepreneurs themselves. One instrument which KfW is using to raise awareness of energy efficiency needs in the manufacturing process is the KfW Energy Efficiency Award.

The KfW Energy Efficiency Award has been presented by KfW Förderbank every year since 2004. With prize money totalling EUR 15,000, the award pays tribute to exemplary enterprises that have successfully implemented in-house measures to reduce energy consumption and have thus been able to significantly lower their carbon dioxide emissions and achieve considerable cost savings. The prizewinning achievements are required to demonstrate forward-looking solutions for the implementation of energy-saving measures and to serve as models for other enterprises.
Energy advice at the federal and regional level.

In this area KfW collaborates closely with federal and Länder agencies. Two examples from the area of energy advice are intended to illustrate this collaboration.

The federal level
A particular form of cooperation with the German federal government in the area of climate protection is the ongoing support of the German Energy Agency (dena), which has evolved into an important institution – particularly through its activities related to promoting energy efficiency and renewable energies. KfW holds a 50% interest in this agency. Dena’s mission is to support the state and enterprises in promoting rational and clean energy generation and utilisation, including renewable energies. Its programmes and projects encourage the use of state-of-the-art technologies and services and accompany their development.

The city-state of Berlin
KfW holds a 25% interest in another institution with energy expertise, Berliner Energieagentur. Established on the initiative of the Berlin Senate, Berliner Energieagentur has the mission of developing the potential of industrial and commercial clients, the housing sector, the tertiary sector and the public sector for conserving energy and improving energy efficiency. The agency contributes to innovation, climate protection and cost reduction by offering advice and employing state-of-the-art technology.
KFW CARBON FUND – A NEW INSTRUMENT.

The EU introduced the European Emissions Trading System (ETS) as part of the Kyoto process in response to global climate change. Through the ETS, the Member States set up national allocation plans (NAP) which define the exact emission amounts that can be traded. Coupling ecological objectives with business activity means that a price has now been put on climate protection. Competition thus becomes a way to ensure the use of the most efficient greenhouse gas reduction technologies. The system also supports the transfer of modern technologies and provides impulses for environmentally and socially compatible investment in developing and emergent countries.

Enterprises have to decide whether to reduce their emissions themselves or to purchase emission rights and credits from projects. They usually opt for the most cost-effective solution. KfW provides support not only for enterprises that invest in emission reduction but also for those that wish to purchase emission credits from projects. KfW supports the latter through its new instrument, the KfW Carbon Fund.

In its Environmental Report 2003 KfW announced its intention to set up a climate protection fund of this kind. The KfW Carbon Fund was launched in April 2004. It is a programme designed to enable the purchase of emission credits from projects that make use of flexible mechanisms provided for under the Kyoto Protocol. Enterprises participating in the KfW Carbon Fund can meet their ETS obligations in a cost-effective manner. For this purpose KfW acquires emission credits from projects in developing, emergent and transition countries on a trust basis.

In the first tranche, the KfW Carbon Fund contains EUR 84 million. This far exceeds the originally targeted volume of EUR 50 million. Around 20 German and European enterprises, the German Ministry for Economics and Technology and KfW have contributed to this sum.

DEG advises enterprises on the acquisition of certified emission reductions under the initiative Kyoto Coaching Cologne, which it is sponsoring together with TÜV Rheinland (Technical Inspection Association Rhineland). DEG is also cooperating closely with the KfW Carbon Fund.
KfW participates in World Bank Carbon Fund.

KfW has contributed USD 2.5 million to the World Bank’s Community Development Carbon Fund (CDCF), which targets small-scale projects. The fund acquires emission credits from projects that are aimed at reducing greenhouse gas emissions in developing countries and also improve the living conditions of poor sections of the population.

Project example: More efficient brickmaking kilns.
The traditional fabrication of Indian clay bricks uses simple kilns that burn coal inefficiently, releasing harmful emissions such as soot particles and nitrous oxides. This exposes the workers to severe health risks. In addition, inefficient fuel combustion is the cause of avoidable CO₂ emissions. The Indian Vertical Shalf Brick Kiln Cluster Project promotes the use of more efficient kilns. These kilns burn only half the fuel of traditional kilns. Training courses for managers and workers enhance efficiency even further. The reduced emissions and modified working behaviour also improve the workers’ quality of life. The additional revenue from emissions trading gives investors the necessary basis for financing investment in the new kilns.

PROTECTING THE CLIMATE AND REDUCING VEHICLE EMISSIONS.

In the transport sector, climate protection and emission reductions are urgently needed but hard to implement. KfW has given a variety of impulses here, particularly through its financing activities under the BMU Innovation Programme. Prominent projects include the pilot project “1000 Clean Taxis for Berlin” and buses that comply with the Enhanced Environmentally Friendly Vehicle (EEV) standard.


**Promoting gas-powered vehicles.**

In 2000 the Federal Ministry of the Environment, the Berlin Senate and the German natural gas industry launched the environmental pilot project "1000 Clean Taxis for Berlin". The acquisition and operation of gas-powered taxis and driving school vehicles as well as the expansion of the petrol station network were supported with grants made available under the Environmental Innovation Programme. The aim of the project was to make a significant contribution to climate protection and to the necessary reduction in pollutant emissions from Berlin's urban traffic. This was achieved by using natural gas, which is low in carbon and thus releases little CO₂ when burned, and has low emission figures for nitrous oxide and soot particles. This environmental project will serve as an example to show other large cities and conurbations in Germany that clean mobility with natural gas is both possible and economical.

**Promoting low-emission buses.**

Buses aggravate air pollution particularly by emitting hazardous diesel exhaust particulates. Public transport accounts for a considerable share of this pollution. To preserve its ecological bonus, the acquisition of buses that met the EEV standard was supported under the project "High Environmental Standards in Competing Public Transport". This standard even goes beyond the EURO 5 emission standard, which will apply from 2008. At the same time, the reduction of soot emissions guarantees a considerable reduction in the emission of further harmful substances such as nitrous oxides.

**Commercial financing of low-emission vehicles.**

KfW IPEX-Bank is one of the world's leading ship financiers. Shipping is considered one of the most environmentally friendly modes of transport as it is efficient and has a lower environmental impact than land-based transport. Nevertheless, we rigorously assess environmental impacts in our ship financing operations, too. In the case of tankers, for instance, we only finance state-of-the-art double hull vessels. In highly innovative shipbuilding Germany has again become a preferred location.
KfW IPEX-Bank is also a strong financing partner in aviation. KfW financed Europe’s Airbus Industrie right from the start, thus contributing to its strong market position. Modern, energy-efficient and quieter aircraft are now being sold all around the world.

KfW IPEX-Bank supports German exporters in establishing entire rail systems. It finances rolling stock as well as signalling technology, control systems and electrification. One example of this comprehensive project approach is the Express Rail Link that connects Kuala Lumpur (Malaysia) to the international airport.

Promotion of transport infrastructure by KfW Entwicklungsbank.

The promotion of mobility, access to markets, social infrastructure and participation in globalisation is an important area of activities for KfW Entwicklungsbank. The road construction projects completed in 2005 alone gave over two million people improved access to markets, schools, health stations and employment – by providing roads that can be used all year round.

“In the dynamic, populous developing countries of Asia private transport is increasing rapidly, making it also the fastest growing energy consumer. This growth has global impacts on CO₂, the climate, oil markets and oil prices. For these reasons KfW Entwicklungsbank is supporting very energy-efficient alternatives such as railways and public transport systems in China and Indonesia, for instance.”

Dr Norbert Kloppenburg, Member of the Board of Managing Directors of KfW Bankengruppe from 1 January 2007
Two-thirds of the world’s poor live in rural areas. Their living and housing conditions make these people particularly dependent on the preservation and functioning of the ecosystems that surround them. Their environment provides them with the supplies they need but contamination poses severe risks to their health. As they have to survive on low incomes, few options are open to them. Poverty and environmental degradation are interrelated and the interactions are complex.

Natural resources and biological diversity are increasingly at risk all over the world, and the consequences for humankind and the environment are unforeseeable. Protecting them is therefore a global concern comparable to protecting the climate. From a global ecological perspective it is necessary to knit the worldwide “network” of conservation areas more tightly and to place representative portions of all natural ecosystems under protection. Existing conservation areas are often underfinanced, particularly in developing countries. Preserving biodiversity around the world is therefore a priority of German development cooperation. It focuses on measures directed at creating new and consolidating existing conservation areas. The Biodiversity Offsets Working Group at KfW has the task of developing a model for financing offsetting measures in nature conservation.

A gift to the world – the Madagascar Foundation for Protected Areas and Biodiversity.

For many years KfW Entwicklungsbank has been supporting Madagascar in setting up, maintaining and operating, together with other donors and the World Wide Fund for Nature (WWF), a sustainable network of national parks that is to be representative of Madagascar’s biological diversity and natural landscapes. The network of 47 Malagasy conservation areas currently includes 8 integrated nature reserves, 16 national parks and 23 nature reserves.

In order to ensure the long-term financial security of these areas, three years of work have gone into establishing a foundation with the support of KfW Entwicklungsbank: the non-profit environmental foundation “Fondation pour les Aires Protégées et la Biodiversité de Madagascar”. The foundation has an initial endowment of USD 5 million. Its capital is to be increased to USD 50 million by 2008.
In order to place what have so far been isolated initiatives of the common project activities on a broader basis, KfW Entwicklungsbank and WWF entered into a cooperation agreement in May 2004 (see Box “A gift to the world”). The main goal is to identify and make use of opportunities for cooperation.

KfW Entwicklungsbank has been a member of the Conservation Finance Alliance (CFA) since the end of 2003. The CFA is a network of nature conservation organisations and donor institutions (among them Conservation International, Danida, GTZ, UNDP, USAID and WWF) set up to promote the exchange of information and experience relating to the issue of financing nature protection and conservation areas. One of its main activities is to disseminate working materials and information about model projects.

Another forum for nature protection on which KfW is represented is the World Commission on Protected Areas (WCPA). The WCPA is the most widely acknowledged body of experts in the field of “conservation areas” in the world. One of the main concerns of the WCPA, besides preserving natural landscapes and keeping them as representative as possible, is the complex of “effective and sustainable management” of such areas. The WCPA pioneered the reorientation of the “conservation area philosophy” away from the isolated, purely conservationist perception towards a comprehensive approach that also takes account of the socio-economic environment.

KfW’s accession to the Kompetenzverbund Biodiversität (Competence Association Biodiversity) in 2006 represents a new partnership in the area of nature protection and conservation of natural resources. The network includes renowned institutions from the Frankfurt area that are committed to the investigation, protection and sustainable use of biological diversity.

**Sponsoring nature conservation.**

On behalf of the German Ministry for Economic Cooperation and Development (BMZ), KfW Entwicklungsbank has been cooperating with the Southern African Wildlife College at the Orpen Gate of the internationally known Kruger National Park in South Africa since 1995. In addition, KfW Entwicklungsbank is sponsoring the college from 2005 to 2007. Each year three female students from various African countries are given the opportunity to receive basic and advanced training to enable them to become national park managers. In this sponsorship project a major concern for KfW Entwicklungsbank is to ensure that this educational programme opens up career opportunities for women as well.
ECONOMICS AND SOCIETY –
STIMULATING STRUCTURAL CHANGE AND EMPLOYMENT.

Founded in 1948, KfW has supported the reconstruction of the German economy and contributed substantially to Germany’s “economic miracle”. It also financed comparable reconstruction efforts in the course of German unification. As Germany’s leading economic development institution we have continuously perfected our toolbox. In order to promote structural change and development in an even more targeted way we aim to:

– provide additional growth and employment impetus for small and medium-sized enterprises,
– further improve their access to financing schemes, and
– strengthen the innovation system.

Innovation is of paramount importance for any economy – it is the main driver of structural change and economic growth. Precisely because it is an export-oriented country, Germany has to rely on its very high technological prowess and innovative enterprises to survive amid fierce international competition. This is the only way to safeguard sustainable jobs and create new ones in the environment of global competition.

Small and medium-sized enterprises are of special importance for an economy’s innovative ability and innovative dynamism. In particular, R&D-intensive, knowledge-based, small, young enterprises as well as start-ups are working on completely new technologies. What makes small and medium-sized enterprises so vital for the economy, however, is the high share of the workforce that they employ. SMEs employ more than 70% of Germany’s workforce. The main goal pursued by KfW in supporting SMEs is therefore to contribute to making full use of the sector’s innovation and employment potential wherever possible.

“The results of our surveys show that our promotional activities also contribute to strengthening the job market. Long-term loans to enterprises, the housing sector and municipal infrastructure make more than a million jobs more competitive and crisis-resistant each year. This occurs directly through the investments financed or indirectly through demand-side effects. Tens of thousands of new jobs are created each year as a result of our promotional input.”

Dr Peter Fleischer,
Member of the Board of
Managing Directors
of KfW Bankengruppe
The long-term capital needed for investment in employment and production expansion is in short supply in developing and emergent countries too. This is the basis for reducing poverty. The projects financed by KfW Bankengruppe often earn important foreign exchange for the partner country, creating additional employment and a stable income for the often poor rural population in the region.

An important approach to mitigating poverty is to create better access to financial services. For example, enterprises can be created with the aid of microloans. However, this presupposes a minimum of legal security and banking supervision that permits the establishment of microbanks and gives them scope for their business activities.

A great day for microfinancing.

In October 2006 KfW Entwicklungsbank congratulated Muhammad Yunus and Grameen Bank in Bangladesh on being awarded the Nobel Peace Prize.

The microfinancing idea developed by Professor Yunus is one of the most important approaches to promoting poverty reduction and developing prosperity. KfW Entwicklungsbank has been gathering experience in successfully establishing and financing specialised microbanks in developing and emergent countries since the 1980s.

KfW’s first major commitment to a microbank was to the Grameen Bank, which was awarded the 2006 Nobel Peace Prize. In the 1980s and 1990s KfW made a total of EUR 24 million available to the bank to enable it to grant microloans. Today Grameen Bank is in a position to fund its microcredit operations from its clients’ savings. Helping people to help themselves really works.

KfW Entwicklungsbank is one of the leading microfinancing players in the world. At the end of 2005 it had a microfinance portfolio of EUR 580 million. However, using federal funds and also funds of its own, KfW is currently supporting, on behalf of the BMZ, 92 microfinancing projects in 39 countries, thus affecting the lives of more than 12 million people. In the meantime KfW has also encouraged other commercial banks to participate in microbanks.
EDUCATION – AN ASSET FOR BETTER JOB PROSPECTS.

Education is a basic need of everyone in a society. It opens up individual opportunities for life and development and promotes social cohesion. Obviously, there is also an economic side to education needs – people with a good education are more likely to find employment and be able to earn an income. Education and professional qualifications increase the value of human capital and are a vital prerequisite for economic growth. Education is a lifelong process that enables individuals and societies to meet new economic, social or political challenges. This is why education is a key to economic development, innovation, structural change and sustainability.

Particularly in developing countries, many young people have had no prospect of finding employment. There is a lot of catching up to do in this sector.

Vocational schools in Ethiopia.

KfW Entwicklungsbank is helping young people to train for a profession by financing the establishment and operation of vocational schools in Ethiopia.

As Ethiopia does not have an approved vocational training system, German Financial Cooperation is promoting education there under a sustainable PPP project. It is financing the construction and operation of centres of competence in which young vocational trainees can learn tailoring or technical skills, for example. The professional support significantly improves young people’s prospects on the local job market.
KfW Student Loan – for focused studying.

Various studies have revealed that Germany, although a highly-developed country, has deficits in education and vocational training. It is generally agreed that the number of students needs to increase, particularly the proportion of students from less wealthy sections of the population.

“We need to ensure fair access to education. By ‘fair’ I mean that education – especially primary education – must be equally accessible to all sections of the population. We have not been able to fully achieve this yet. Educational poverty is hereditary! This is not only a symptom of social imbalance. Most of all, it points to the great potential that needs to be developed. The purpose of enhancing efficiency in the education sector must therefore be to encourage more pupils to pursue an academic education, particularly those from a low-income background.”

One way of achieving this is the new Student Loan from KfW Förderbank. This loan secures students’ livelihood so that they do not have to take jobs while they are studying. They can focus more on their studies and may be able to shorten the length of time they need to complete their higher education. KfW has generally been committed to promoting education for many years, with domestic financing programmes conducted by both KfW Förderbank and on a global basis through KfW Entwicklungsbank.

EFFECTIVELY PROMOTING GENDER EQUALITY.

Gender equality is both a human right and an economic necessity. Yet all over the world women and girls suffer far more from poverty and poor living conditions than men and boys. However, balanced participation in the development process is also a prerequisite for sustainable poverty reduction. Gender-related disadvantages are among the serious structural causes of poverty. Gender equality, the advancement of women and improving their opportunities are thus key objectives in development cooperation and, hence, for KfW Entwicklungsbank.
In July 2005 KfW Entwicklungsbank adopted its new gender strategy and supplemented it with a binding plan of action, the aim being to give gender equality an established place in its activities and to ensure that it is implemented more effectively in projects. This is intended to further professionalise the work of KfW Entwicklungsbank with regard to gender aspects. This should help to change the structural causes of inequality and poverty and thus to pursue the Millennium Development Goals more effectively. More specifically, the number of new projects with positive gender impacts is to be increased by over 40% within three years.

“Microloans enable women to work their way out of poverty and to advance towards a state of gender equality in society. Microbanks also stand to gain because repayment rates are very high among female borrowers. An ideal ‘win-win’ situation.”

FOCUS ON HEALTH AND QUALITY OF LIFE.

One of the greatest challenges in development cooperation is the health of the people in the partner countries. Establishing and expanding health care is therefore a main focus of the work of KfW Entwicklungsbank in 16 partner countries. Activities include hospital projects, health stations and awareness campaigns about family planning and HIV prevention.

In the industrialised countries, technological progress is expanding the range of diagnostics and therapy, raising life expectancy ever further. The challenge: exploding public health care costs. It is not without reason that medical technology has been selected as Business Angels' favourite target industry for the fifth time in a row. Businesses in this sector are founded on the basis of highly innovative concepts which, however, are fraught with a high degree of uncertainty. The challenge is how to identify promising business models. KfW supports experienced venture capital companies which provide biotechnology enterprises with venture capital, for instance, through co-investments and refinancing schemes and as anchor investors in special early-phase funds.
Many urban agglomerations in developing countries are experiencing a demographic problem of an entirely different sort. People from the countryside, who are often particularly poor, move into large cities where they expect living conditions to be better. What they find there instead are hygienic, living and nutrition conditions that are humanly degrading. In Africa one in every two town dwellers lives in a slum.

In its poverty reduction efforts KfW Entwicklungsbank is working to overcome the worsening impoverishment of slum dwellers. Urban development projects are designed to improve the infrastructure, prevent violence and promote slum rehabilitation with the participation of the residents.

KfW Award 2006.

Almost one in five Germans has now reached retirement age, a fact which has a direct impact on the living environment. Innovative ideas that accommodate this development are therefore needed – from the design of the individual housing environment to the organisation of the social setting. KfW has chosen this topic for this year’s KfW Award. Under the motto “Europäisch Leben – Europäisch Wohnen” ("Living European Style") the KfW Award acknowledges model residential buildings in Germany that are committed to the European way of building and that were inspired by creative and forward-looking ideas or models. The Award is granted for a specific topic each year; in 2006 it was "Living as a Senior Citizen".
FOUNDATIONS/COMPENSATION FUNDS.

In its business area “Advice and Services” KfW, acting as a service provider, manages two foundations – the Humanitarian Aid Foundation for Persons infected with HIV through Blood Products (HIV Foundation) and the Contergan Foundation for Handicapped Persons, better known as the Contergan Foundation. KfW conducts the business on behalf of the foundations’ executive boards. It includes all administrative and operative functions as well as the full handling of pension payments.

Until the end of 2005 KfW also managed the Compensation Fund for Severely Handicapped Persons. This fund, which is located at the Federal Ministry for Labour and Social Affairs, is endowed with the levies paid by enterprises that employ too few or no disabled persons. In coordination with the federal government, KfW has invested the funds and co-financed measures to construct and equip workshops and living quarters for disabled persons. The measures have so far created 120,000 workshop places and 38,000 residential places.

PEACE BUILDING, DISASTER RELIEF AND RECONSTRUCTION.

Environmental problems may spread across borders and trigger conflicts between states. The need for joint efforts to solve these problems can also be an opportunity for conflict prevention and cross-border cooperation. Such cooperation can go a step further and build a new basis of trust. Positive environmental impacts can thus also help to promote peace. With this in mind the German federal government launched the Caucasus Initiative in 2001. This initiative has enhanced cooperation between the three southern Caucasian countries of Georgia, Armenia and Azerbaijan through cross-border projects, thus contributing to mitigating conflicts and preventing crises in the region. Within the framework of the Caucasus Initiative KfW Entwicklungsbank supports the establishment of cross-border national parks as well as the rehabilitation and construction of power lines across national borders. The following example from the Middle East also illustrates how cross-border environmental projects promote peace.
Disaster relief is another area in which KfW Entwicklungsbank operates on behalf of the German government. In 2004, for example, it took part in the reconstruction work immediately following the tsunami disaster. KfW Entwicklungsbank had been supporting development cooperation projects in the affected areas of Sri Lanka prior to the flood. The province of Aceh in north-western Indonesia, on the other hand, had been excluded from international support owing to the civil war conditions there. Both regions received long-term aid. The health sector was given top priority. Funds were provided for the reconstruction of the biggest hospital, the

Cross-border environmental projects – helping to promote peace.

The limited water resources in the region of Tulkarem in the Palestinian Territories and the district of Emek Hefer on the Israeli side of the border are a critical bottleneck and a possible cause of additional conflict. Owing to the insufficient opportunities for sewage treatment on the Palestinian side, Wadi Zeimar, which crosses the "green line" and flows into the ecologically valuable Alexander River on the Israeli side, was heavily polluted, as was the groundwater on both sides – meaning a further reduction in the available water resources. A further consequence of the pollution is that use of the Alexander River is restricted to irrigation. The problem affects both areas and was the common ecological theme and starting point for an initiative launched by the head of the Emek Hefer Regional Council some ten years ago to provide well-functioning sewage treatment plants in Tulkarem for the benefit of both districts. On the long route to project realisation, the external support provided by KfW Entwicklungsbank (financing and intermediation) was an important element in helping the project to achieve success.

In 2005, despite the difficulties caused by the intifada, the largest obstacle to realisation, the plant in Tulkarem was completed at the end of a one-year building period and was inaugurated jointly by the Mayor of Tulkarem and the Israeli head of the Emek Hefer Regional Council. As part of the project, the existing clarifying ponds were rehabilitated and enlarged. Around EUR 1.5 million in financing was provided. Both parties noted with pride that, despite adverse political circumstances, it had proved possible to cooperate in a way that might perhaps form the basis for future cooperation and encourage other communities through the positive example given; there is still a large need for plants of this kind.
General Hospital Zainael Abidin in Banda Aceh. Another priority area of KfW’s involvement is education. Around 750 schools were destroyed by the flood in 2004. Many of them have since been rebuilt. The reconstruction of the vocational training centre in the provincial capital Banda Aceh was financed by funds that included a donation from KfW’s Board of Managing Directors.

The example of Afghanistan shows that the reconstruction of the social and economic infrastructure can also have a peace-building impact. With its infrastructure reconstruction projects KfW Entwicklungsbank helps to improve the population’s living conditions sustainably and tangibly so as to enable Afghanistan to return to a lasting peace.

Reconstruction in Afghanistan.

KfW Entwicklungsbank has been operating in Afghanistan since December 2001. Over EUR 100 million in financing is being channelled to ongoing projects from funds of the BMZ and other donor organisations. Visible signs of this commitment can be found in the areas of road rehabilitation, water supply, energy and the reconstruction of schools and hospitals that had been destroyed.

Forty-two schools have been rebuilt. KfW Entwicklungsbank has supported the reconstruction of 14 health stations and clinics and supplied urgently needed medicine and medical equipment. Around 6,000 patients can now be cared for each day. The water supply system of Kabul has been repaired, and 140 kilometres of streets have been upgraded in this and other cities.

KfW’s commitment, however, is by no means limited to disaster relief abroad. From time to time, for example, floods also affect parts of Germany. Even if the consequences are much less severe and lives are rarely lost, the people affected usually face great challenges. The additional financial burden caused by production losses and flood damage can threaten the very existence of enterprises. In these cases KfW, in cooperation with the German federal government, offers individual flood relief programmes which support the affected enterprises with loans at particularly favourable conditions.
NO DEVELOPMENT WITHOUT HUMAN RIGHTS.

The major international conferences of the 1990s clearly showed that global development objectives cannot be achieved without effectively implementing economic, social, civil and political human rights. Development also means improved access to these human rights. KfW contributes to safeguarding or fulfilling human rights in different ways – depending on the instruments or support schemes at its disposal in the fields of activity concerned. The human rights conventions which Germany and the partner countries have signed are binding in the strict legal sense.

Apart from the imperative of not violating human rights through its financing activities, however, KfW also has active ways of contributing to the observance of human rights. Projects such as the construction of schools can have a direct impact on the right to education, while support for health stations in remote regions and wide-scale HIV prevention programmes may directly affect the right to health. In some projects, these rights are not merely a cross-cutting task but the promotional priority, e.g. in the case of programme-based joint financing in the area of good governance.

Indirect impacts with regard to the rights to education and health are generated, for example, through improvements in the transport infrastructure when such improvements enable many people to reach schools and hospitals. Individual civil and political rights are also promoted as a cross-cutting task in projects supported by KfW Entwicklungsbank. Examples include the participation of the population in decision-making processes or the advancement of gender equality.

However, all efforts lead, at best, to isolated solutions if the partner country fails to acknowledge its human rights obligations. This is where the political dialogue between the competent government ministries and the countries concerned sets in, and human rights is one of the key topics. Human rights are an integral part of development policy criteria used by the BMZ when taking decisions on the eligibility of countries for promotion. A decision on whether or not to provide support always involves deciding the extent to which development cooperation can contribute to improving the human rights situation in the long term despite current problems with the observance of human rights.
IN-HOUSE ENVIRONMENTAL PROTECTION – ALL RESOURCES IN VIEW.
REVIEW, CURRENT STATUS AND FUTURE OUTLOOK.

Resource conservation is the main driving force behind KfW's active commitment to in-house environmental protection – a major ongoing challenge. Ambitious goals have been set for in-house environmental protection work. However, for all projects and objectives to take effect, they must first be integrated into the in-house environmental management system. This system covers KfW headquarters in Frankfurt, the branches in Berlin and Bonn and KfW subsidiary DEG (Deutsche Investitions- und Entwicklungsgesellschaft mbH) in Cologne – a total of 19 separate buildings and around 4,200 members of staff. The advantage of having a standard system at all locations is that it allows internal comparisons. However, it is also the cause of particular problems as building materials and technologies and business processes vary considerably from one location to another – as shown in the key figures, some of which indicate a marked divergence.

HOW WE UNDERSTAND IN-HOUSE ENVIRONMENTAL PROTECTION.

The new environmental and social guidelines reinforce in-house environmental protection. The focus is on the individual member of staff, who, through information and motivation campaigns, is involved more closely than ever in implementing the objectives.

At the same time, the guidelines cover reliable compliance with all official and legal requirements, limiting energy, water and material consumption and the incidence of waste as well as efforts to implement far-reaching innovative building technology solutions in construction work – the aim being to achieve values below the existing emission thresholds and to exceed current standards.
This chapter will give details of the most important aspects of actual consumption for the years from 2003 to 2005. The table “Key figures from the years from 2003 to 2005” provides an overview of consumption figures at the individual locations. Environmental accounting follows the widely recognised guidelines of the German Association for Environmental Management at Banks, Savings Banks and Insurance Companies (VfU). With regard to staff figures, the guidelines generally restrict the data to staff members on the company’s own premises as it is seldom possible to apply clear consumption standards at rented property, which means that no direct influence can be exerted on consumption figures. The accounts for paper and business travel are an exception; the specific figures are based on the total number of staff. Various rehabilitation and construction measures meant that in 2003 staff in Frankfurt had to move from KfW’s own premises to rented offices. However, in 2009 at the latest all staff will be working in highly efficient buildings owned by KfW.

Influential factors such as the development of the business volume or staff numbers, mergers, internal restructuring, intensive construction measures, the need to recalculate individual figures or the climate in a given year make it difficult to analyse the data. Nonetheless, in this chapter we will now take a closer look at least at clear tendencies in the development of the key figures and the achievement of objectives.
CO₂ emissions.

Premises that are highly efficient in their use of energy, intensive consumption monitoring and the use of video conference facilities to avoid car journeys are leading to a slight reduction in CO₂ emissions per staff member (2003: 7,840 kg/staff member, 2004: 7,700 kg/staff member, 2005: 7,680 kg/staff member). In accordance with the VfU guidelines, the calculations were based on staff members on KfW-owned premises.

Energy.

The decline in energy consumption in Frankfurt from 2003 to 2004 can be explained by the modernisation and complete refurbishment of the main building which began in 2003. Around 600 staff members had to move to rented offices while the refurbishment was carried out. The slight increase in the 2005 figures was caused by the relocation of the Bonn accounting centre to Frankfurt, which also explains the drop in consumption in Bonn.
Transport.
The upward trend in annual kilometrage is mainly due to the increase in business volume and the merger of KfW and DtA, which took place in 2003. Nonetheless, the annual number of kilometres per staff member was kept stable (2003: 11,407 km/staff member, 2004: 11,618 km/staff member, 2005: 11,726 km/staff member). In accordance with the VfU guidelines, the calculations were based on staff members on KfW-owned premises.

Paper.
New tasks in Bonn and an increase in the volume of work in Berlin mean a substantial increase in paper consumption at these locations. Reductions can be expected to be achieved through the electronic archiving project launched in 2005 and through a change in filing procedures.

Water.
The decrease in water consumption in Frankfurt from 2003 to 2004 is due to the fact that staff members were relocated while the main building was being refurbished. Lower water consumption in Bonn is due to a number of measures executed during the period in question; the biggest impact was made by dismantling all fixed hot-water boilers and repairing the leak-prone pipe leading to the fountain.

Waste.
The volume of waste was reduced at all four locations despite the fact that staff numbers increased in some units. This is because suppliers are increasingly being obliged to remove and dispose of packaging themselves.

**OBJECTIVES TARGETED AND ACHIEVED.**

The above-mentioned merger made it necessary to merge and harmonise the environmental objectives presented in the last environmental reports of KfW, including DEG and DtA. As a result, a new table of targets was drawn up on the basis of the former KfW programme and targets for all locations added. The table “Some quantitative objectives and the extent to which they have been achieved” presents a brief extract. The selection deliberately includes both unachieved and achieved targets.
With regard to electricity and water consumption in Frankfurt, the actual figures for 2005 were well above the target values although the key figures for energy and water were lower overall. As some target values were too ambitious, trends have generally been formulated for the years from 2006 to 2008.

One major task in in-house environmental protection over the next three years will be to analyse the high incidence of waste at all locations and to develop solutions to reduce it.

The objective of ensuring that at least 45% of all paper used for photocopying and computer printing at all locations is recycled paper was not achieved. In 2005 the figure for Frankfurt was 20%, for Berlin 15% and for Bonn 37%.

### HIGHLIGHTS OF IN-HOUSE ENVIRONMENTAL PROTECTION.

A few special results for in-house environmental protection in the period under review are presented below.

#### Guidelines for in-house environmental protection.

Following their approval in 2003, the guidelines entered into effect in 2004, as planned. They are applicable at the four locations in Germany and for all staff members. They cover organisation and tasks in in-house environmental protection as well as details on operational procedures and the principles of environmental accounting. The new guidelines also cover how to deal with staff suggestions for improvements. If the ecological advantages involve considerable

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### Some quantitative objectives and the extent to which they have been achieved.

<table>
<thead>
<tr>
<th>Site</th>
<th>Quantitative environmental objectives/measures</th>
<th>Target value</th>
<th>Actual value in 2005</th>
</tr>
</thead>
<tbody>
<tr>
<td>Frankfurt</td>
<td>Maintain electricity consumption</td>
<td>Max 7,200 MWh per annum</td>
<td>8,770 MWh per annum</td>
</tr>
<tr>
<td>Frankfurt</td>
<td>Reduce municipal water consumption</td>
<td>Max 75 l/staff member/day</td>
<td>123 l/staff member/day</td>
</tr>
<tr>
<td>Berlin</td>
<td>Limit total volume of waste</td>
<td>Max 215 t per annum</td>
<td>146 t per annum</td>
</tr>
<tr>
<td>Berlin</td>
<td>Maintain electricity consumption</td>
<td>Max 3,800 MWh per annum</td>
<td>2,531 MWh per annum</td>
</tr>
<tr>
<td>Bonn</td>
<td>Limit total volume of waste</td>
<td>Max 250 t per annum</td>
<td>376 t per annum</td>
</tr>
<tr>
<td>Bonn</td>
<td>Reduce municipal water consumption</td>
<td>Max 9,000 m³</td>
<td>7,989 m³</td>
</tr>
<tr>
<td>Cologne</td>
<td>Limit total volume of waste</td>
<td>Max 135 t per annum</td>
<td>156 t per annum</td>
</tr>
<tr>
<td>Cologne</td>
<td>Reduce municipal water consumption</td>
<td>Max 9,000 m³</td>
<td>8,107 m³</td>
</tr>
</tbody>
</table>

All figures have been rounded.
additional costs or other disadvantages, this suggestion for improvement is to be submitted to
the Board of Managing Directors of KfW Bankengruppe or DEG management, as appropriate,
before a decision can be taken.

**An energy certificate for new KfW offices.**

For one office building, the East Arcade in Frankfurt, an energy certificate which complies with the calculation procedures of the prestandard DIN V 18599 was issued in December 2005 – before this was rendered compulsory by the EU Directive on the energy performance of buildings.

The result is convincing: at around 90 kWh/(m²a) in 2005, the total primary energy needs are estimated as being 40% below the average for conventional new office buildings (150 kWh/(m²a)) – which makes a substantial contribution to reducing CO₂ emissions. The two-year monitoring period in the German SolarBau Monitor project also contributed to these excellent consumption figures. Because of the complex building management technology involved, a certain "settling in" period is required for buildings with highly efficient energy consumption before the target values are achieved. This is the only way that the original target values can be aligned with the actual values, to which staff use of the facilities makes a major contribution.

**Incentive system to encourage the acquisition of more environmentally friendly company vehicles.**

Data on the CO₂ emissions produced by around 160 company vehicles are collected each year and represent around 4% of the total emissions. One possible way of reducing these emissions is to change over gradually to purchasing vehicles that produce little CO₂. In 2005 the decision was taken to introduce an incentive scheme (bonus-malus system) as a means of contributing to including as many vehicles with low CO₂ emissions as possible in the company fleet. Initial experience shows that when a new vehicle is chosen, greater attention is paid to CO₂ emissions than was previously the case and natural gas vehicles are being considered as an alternative.

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4 The comparative value is the value that would be achieved by a building of the same geometry
and use if precisely defined "standard technologies" were used.

The new environmental objectives that apply throughout KfW and KfW Bankengruppe's most important accompanying measures are outlined below. A brief explanation of the objectives is given. Measures that were already under way at the time of publishing this report are also presented.

From the end of 2007 100% "green electricity" at all locations.
From the end of 2007 the four locations in Germany are to be run entirely on "green electricity". To ensure that the invitation to tender complies with EU regulations, the guiding principle of the BMU on EU-compliant tender procedures for green electricity will be followed. The changeover to "green electricity" and the concomitant avoidance of CO₂ emissions is a considerable contribution to CO₂ neutrality. The pilot project on acquiring "green heat" has also been approved. However, the feasibility depends on there being a corresponding offer and on the costs. In addition, as part of a pilot project, there is a plan to purchase "green gas" to run the gas-fired heating system.

Pushing for the use of recycled paper.
As an environment bank, KfW is conscious of its trend-setting role in resource-saving procurement, too. Alongside efforts to generally reduce the consumption of paper, in terms of paper purchasing this also means working towards using a high percentage of recycled paper. Measures taken to date have not achieved the objective. In 2006, therefore, KfW decided that, essentially, recycled paper would be the only type of paper used in the future. Exceptions can only be made for good reasons. Recycled paper was introduced for internal use at DEG on 1 January 2006. The move was thoroughly prepared, with the result that a very satisfactory level of 84% was achieved at DEG in the first half of 2006.

Energy certificates for all KfW buildings.
The EU Directive on the energy performance of buildings deals with the compulsory certification process – for non-residential buildings, too. In its environmental and social guidelines, KfW has set itself the target of exceeding current legal obligations wherever possible. Every effort is therefore being made to provide certificates for all KfW buildings by the end of 2008.
Staff information processes intensified to promote environmentally conscious behaviour.

We see our staff members as the executive and multiplier arm of our work. In order to exert a positive influence on our staff, even more information on in-house environmental protection issues is to be provided in the future. In this connection, an exhibition on “Environmental and climate protection at KfW” is planned as a means of providing additional information; it will be set up at all four locations. Environmental protection will also continue to be an important feature of the periodical KfW staff magazine.

Implementation of framework guidelines for environmentally friendly procurement.

Setting an example in in-house environmental protection means ensuring that procurement is efficient, environmentally sound and hence sustainable. KfW is therefore endeavouring to prepare a framework guideline which defines the generally applicable purchasing principles governing environmentally friendly procurement.

Ongoing monitoring of the system limits of our environmental accounting procedure.

In the future the intention is to record data on CO₂ emissions on journeys to and from home and the office. Data on CO₂ emissions produced by company cars that are used to commute are already being collected and are included in the total of all traffic-related emissions. In addition, the emissions caused by producing and transporting paper in connection with consumption volumes are also to be shown in the future, as are CO₂ emissions produced by waste disposal.

Limiting the consumption of energy, water and material and the incidence of waste.

Despite the substantial efforts made in recent years to limit consumption and volumes of waste and the positive results, it will still be necessary to pursue these issues in depth in the future. The most important key figures must therefore be collected and evaluated at regular intervals as part of the annual environmental accounting procedure. However, staff information must also still be given a high profile if the above-mentioned multiplier effect is to be achieved.
### Top priority measures.

<table>
<thead>
<tr>
<th>Applicable</th>
<th>Area of impact</th>
<th>Description</th>
<th>Date</th>
</tr>
</thead>
<tbody>
<tr>
<td>Bank-wide</td>
<td>Transport</td>
<td>Procurement of environmentally friendly company cars.</td>
<td>From 2006</td>
</tr>
<tr>
<td>Bank-wide</td>
<td>All environmental accounts</td>
<td>All new staff and trainees must be given training on environmental protection.</td>
<td>From 2006</td>
</tr>
<tr>
<td>Bank-wide</td>
<td>All environmental accounts</td>
<td>An exhibition on “Environmental and climate protection at KfW” at all four locations.</td>
<td>2006</td>
</tr>
<tr>
<td>Frankfurt</td>
<td>Emission/energy</td>
<td>Further reductions through consumption rules for new and converted buildings.</td>
<td>Ongoing</td>
</tr>
<tr>
<td>Frankfurt</td>
<td>Emission/energy</td>
<td>The monitoring procedure that proved successful in the East Arcade will also be implemented in the main building.</td>
<td>From 2006</td>
</tr>
<tr>
<td>Frankfurt</td>
<td>Transport/emissions</td>
<td>Participation in &quot;bike + business&quot; to encourage more staff members to cycle to work.</td>
<td>2006</td>
</tr>
<tr>
<td>Frankfurt</td>
<td>Water</td>
<td>Key figures derived in connection with the introduction of vacuum toilets (main building).</td>
<td>From 2006</td>
</tr>
<tr>
<td>Berlin</td>
<td>Emission/energy</td>
<td>Further reductions through intensive controlling in conjunction with the operational management company.</td>
<td>Ongoing</td>
</tr>
<tr>
<td>Bonn</td>
<td>Energy</td>
<td>Replacement of blinds and lighting controls in the staff canteen.</td>
<td>2006</td>
</tr>
<tr>
<td>Bonn</td>
<td>Water</td>
<td>Trainee project with simultaneous use of the results for staff information.</td>
<td>2006</td>
</tr>
<tr>
<td>Cologne</td>
<td>General</td>
<td>Optimisation of environmental protection in planning new “Kämmergasse” building.</td>
<td>From 2008</td>
</tr>
</tbody>
</table>

### MEASURES ALREADY UNDER WAY.

**Bank-wide training of all new staff and trainees.**

From 2006 all new staff members and trainees will be trained on “Environmental protection at KfW”. The staff are an important target group in terms of in-house environmental protection as they have a direct influence on various consumption variables such as lighting or water consumption. Detailed information will motivate staff members to support efforts to achieve the environmental objectives.
Setting up the corporate environmental protection network in the Rhine/Main region.

To enable a regular exchange of experience on all issues related to in-house environmental protection to take place, in 2005 a decision was taken at KfW in Frankfurt to establish a "Rhine-Main Network for Office and Building Ecology" with other well-known enterprises. The idea of setting up the network was inspired by the positive experience of our Bonn office of participating in the "NRW Environmental Platform" network, an association of regional financial service providers.

Participation in "bike + business".

Bicycles are part of the in-house mobility concept – also because their use can help to reduce "home-made" CO₂ emissions. To persuade more staff to use their bicycles, KfW is taking part in the "bike + business" project in the federal state of Hesse, the aim being to help to encourage commuters to leave their cars at home and to cycle to work, thus increasing the share of bicycles in business commuter traffic. The other locations will also benefit from the experience gathered in Frankfurt, enabling them to provide an infrastructure that is attractive for cyclists.
In going climate neutral, we have assumed an international pioneering role. The objective is to
offset operational CO\textsubscript{2} emissions.

CO\textsubscript{2} emissions produced by KfW business activities as a result of air traffic\textsuperscript{5}, other business trips
and electricity consumption and heating in KfW-owned buildings are first calculated precisely.
The second step is to use the neutralisation approach to offset these emissions: to cover the
quantities of CO\textsubscript{2} produced, emission credits, e.g. from CDM projects, are purchased and set
aside. As the impact of carbon dioxide is global, it is irrelevant, in terms of effectiveness, where
the offsetting actually takes place. For example, CO\textsubscript{2} emissions generated by KfW in Germany
can be offset through a biomass project in India. The certificates required are acquired by the
KfW Carbon Fund.

Our initial expectations are that up to 30,000 tonnes of CO\textsubscript{2} per annum will need to be offset.
This figure exceeds the data in the table ”Key figures for the years from 2003 to 2005” by
roughly 8,000 tonnes. This gives us a buffer for the move back into the main building in Frank-
furt in 2006 and the progressive occupation of the new buildings in the following years. Our
aim is to ensure that all staff members are in highly efficient office buildings by 2009.

The aim of the third stage of the KfW strategy, however, is to achieve a further, steady reduction
in the volumes of CO\textsubscript{2} that need to be offset. This includes, first, reducing energy consumption
by achieving greater energy efficiency in our office buildings and company vehicles. Second,
our aim is to use CO\textsubscript{2}-free energy such as
“green electricity” or “green gas”\textsuperscript{6} as far as
possible to cover the remaining energy
requirements, thus minimising the number
of certificates needed.

\textsuperscript{5} The calculation takes account of the Radiative Forcing Index (RFI).
\textsuperscript{6} Biogas of the same quality as natural gas fed into the natural gas network.

We have audited the quantitative assertions included in the Sustainability Report 2006 of KfW Bankengruppe. The Sustainability Report covers the period from 1 January 2003 to 31 December 2005 and has been prepared in accordance with the principles for topic selection and reporting set forth in the Global Reporting Initiative (GRI) guidelines.

The preparation of the Sustainability Report is the responsibility of the Board of Managing Directors of KfW Bankengruppe. Our mandate is to express an opinion on the topic selection and the completeness and accuracy of the quantitative assertions under consideration of the reporting principles of auditability, completeness, relevance, accuracy and comparability as set forth in the GRI guidelines.

Within the scope of our work we have audited the quantitative assertions included in the Sustainability Report 2006. The contents of other reporting media such as websites were outside the scope of our audit.

We conducted our audit in accordance with the generally accepted German standard for the audit of sustainability reports promulgated by the Institut der Wirtschaftsprüfer (IDW PS 821). This standard requires that we plan and perform the audit in such a way as to allow a conclusion to be expressed with reasonable assurance on whether the topics have been selected in accordance with the principles of the GRI and whether the quantitative assertions have been presented completely and accurately in accordance with the GRI reporting principles of auditability, completeness, relevance, accuracy and comparability. The audit includes assessing the effectiveness of the underlying environmental information systems and evidence corroborating the assertions in the report, primarily on the basis of random samples. We believe that our audit provides a reasonable basis for our opinion.
In our opinion based on the findings of our audit, the topics addressed in the Sustainability Report have been selected in accordance with the GRI criteria and the quantitative assertions have been presented completely and accurately in accordance with the GRI reporting principles of auditability, completeness, relevance, accuracy and comparability.

Frankfurt, 20 October 2006

PricewaterhouseCoopers
Aktiengesellschaft
Wirtschaftsprüfungsgesellschaft

Dr Manfred Waltz
ppa Dieter Horst
| **Biodiversity offsets** | Nature conservation measures used to offset negative effects on the natural environment. They ensure that there is no net loss of biological diversity. |
| **Corporate citizenship** | Systematic civic/social commitment by enterprises forming an integral part of the corporate culture. |
| **Corporate governance** | The establishment and observance of rules for staff and corporate behaviour within an enterprise. |
| **End-of-pipe** | Term applied to supplementary environmental protection measures introduced at the end of the cycle. |
| **Energy productivity** | Measurement of the efficiency of the use of the input factor energy, e.g. from an economic perspective, the ratio of gross domestic product to primary energy consumption. |
| **Renewable energies** | Sources of energy which are constantly being renewed by natural processes. These include solar, water and wind energy as well as biomass and tidal energy. |
| **Facility** | Option granted by a bank to its customers to draw, within fixed limits, on a loan at short notice or to build up credit. |
| **Global Reporting Initiative (GRI)** | The Global Reporting Initiative (GRI) is an institution whose objective it is to develop globally applicable guidelines for sustainability reporting. For more information: [www.globalreporting.org](http://www.globalreporting.org) |
| **Kyoto mechanisms** | 1 Clean Development Mechanism (CDM) for projects in countries without emissions objectives. 2 Joint Implementation (JI) between countries with emissions objectives. 3 International Emissions Trading (IET). 4 Formation of target communities (“bubbles”). |
| **Mezzanine** | Generic term for hybrid types of financing which are legally and economically designed to combine debt and equity financing. |
| **Millennium Declaration** | The declaration signed by 189 Member States of the United Nations on 8 September 2000 listing fundamental binding objectives for a secure global future, the Millennium Development Goals (MDG). |
| **Product-integrated environmental protection** | An approach aimed at mitigating the harmful environmental effects of manufacturing, using and disposing of products. |
| **Production-integrated environmental protection** | Industrial or commercial production with the aim of minimising the harmful and residual substances generated in the production process, ensuring that they are extensively recycled and that the consumption of fuel and inputs is minimised. |
| **Raw materials productivity** | Measurement of the efficiency of the use of the raw materials, e.g. from an economic perspective, the ratio of gross domestic product to raw materials consumption. |
### Key Figures

**I KfW Mittelstandsbank**  
In EUR million  

<table>
<thead>
<tr>
<th>Year</th>
<th>2003</th>
<th>2004</th>
<th>2005</th>
</tr>
</thead>
<tbody>
<tr>
<td>Net income for the year</td>
<td>247</td>
<td>341</td>
<td>431</td>
</tr>
<tr>
<td>Staff numbers</td>
<td>3,670</td>
<td>3,077</td>
<td>3,809</td>
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</table>

**II KfW Förderbank**  
In EUR million  

<table>
<thead>
<tr>
<th>Year</th>
<th>2003</th>
<th>2004</th>
<th>2005</th>
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</thead>
<tbody>
<tr>
<td>Investment finance in Germany and Europe</td>
<td>58,648.2</td>
<td>48,440.1</td>
<td>54,207.6</td>
</tr>
<tr>
<td>Securitisation</td>
<td>3,484.4</td>
<td>3,738.4</td>
<td>3,963.2</td>
</tr>
<tr>
<td>Equity financing</td>
<td>311.1</td>
<td>344.1</td>
<td>300.1</td>
</tr>
<tr>
<td>Mezzanine financing</td>
<td>988.1</td>
<td>618.8</td>
<td>583.1</td>
</tr>
<tr>
<td>of which: Global loans to trade and industry</td>
<td>2,067.0</td>
<td>2,008.0</td>
<td>1,987.0</td>
</tr>
<tr>
<td>Education</td>
<td>727.9</td>
<td>811.6</td>
<td>675.0</td>
</tr>
<tr>
<td>Municipal infrastructure</td>
<td>4,020.8</td>
<td>2,165.5</td>
<td>4,241.6</td>
</tr>
<tr>
<td>Environmental protection investment</td>
<td>1,529.1</td>
<td>3,936.5</td>
<td>3,625.2</td>
</tr>
<tr>
<td>Global credit lines for promotional institutions in the federal states</td>
<td>18,389.9</td>
<td>11,430.6</td>
<td>16,271.7</td>
</tr>
</tbody>
</table>

**III KfW IPEX-Bank**  
In EUR million  

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<td>18,398.8</td>
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**IV KfW Entwicklungsbank**  
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**V DEG**  
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<th>Year</th>
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<tr>
<td>Total financing volume</td>
<td>72,274.9</td>
<td>62,861.5</td>
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**Business volume**  
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**Balance sheet total**  
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**Capital and reserves**  
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**Net income for the year**  
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Differences in this table are due to rounding.