

FOREWORD BY THE MANAGEMENT BOARD

Ladies and gentlemen,

The EU Commission's favourable decision in the state-aid proceedings characterised the year 2015 to a major extent for HSH Nordbank. Two years of negotiations were followed in October 2015 by the green light from Brussels. We therefore now have planning certainty and a clear outlook on the future. The agreement reached with the EU gives HSH Nordbank the opportunity to sell legacy assets of up to EUR 6.2 billion to an institution under public law that the states of Hamburg and Schleswig-Holstein established in December 2015. The plan is to make a transfer of initially EUR 5 billion in the summer of 2016. HSH Nordbank will thereafter be able to dispose of further critical assets worth up to EUR 3.2 billion on the market. The losses on these disposals will be charged to the existing guarantee. The Bank will thus be liberated from at least some of the massive legacy assets that stem from the time prior to 2009. It should not go unmentioned, however, that we would have wished for more substantial relief. The non-performing loans stemming from the past continue to weigh on HSH Nordbank to a major extent and conceal its actual ability to perform as they tie capital and are – to put it briefly – negatively reflected on the balance sheet. Ultimately, they will diminish the potential price to purchase HSH Nordbank. Everyone involved must be aware of that.

The change of ownership planned for 2018 will present HSH Nordbank with tremendous challenges – but it simultaneously means a great opportunity. These are the poles between which the Bank will be moving in the next two years. We must now establish the conditions for the change of ownership in order to make it a success. Potential investors will be interested in HSH Nordbank only if they are convinced by its structure, ability to perform as well as its long-term potential. Alongside a solid client base that has grown over time and a good market position, this also includes efficient processes in sales and back-office operations accompanied by a cost-income ratio that is appropriate overall.

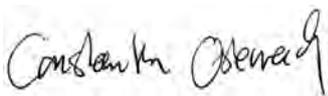
A glance at our results of the past year underscores HSH Nordbank's operating strength and shows its potential to generate steady income over the medium and long term. In 2015, HSH Nordbank generated a positive result with pre-tax income of EUR 450 million. However, this profit was heavily affected by technical factors that are directly connected with the complex guarantee structure. The Bank performed well in operating terms and increased its total income by nearly 70 per cent to EUR 995 million. That is particularly notable given a difficult market setting and the protracted uncertainty until the informal agreement was reached with EU Commission in October 2015. The amount of new business was, in accordance with projections issued during the year, down slightly on good margins and high disbursement ratios. However, following a very strong 2014, the figure of EUR 8.8 billion was well above the 2013 level. The crucial factor is that we are getting better and better at balancing our loan portfolio between the Shipping, Corporate Clients and Real Estate Clients divisions, with each accounting for about one third of the volume. Whereas we are intentionally reducing the portfolio in the Shipping division, which continues to be marked by the persistently weak shipping markets, our Real Estate Clients and Corporate Clients divisions are gaining in significance. In 2015, we were particularly successful in, amongst other areas, financing renewable energies – a future sector where we are amongst the market leaders in both Germany and Europe.

At the same time, we resolutely and extensively equipped ourselves to confront the risks in the portfolio: given the still deteriorating shipping markets and the effects already taken into account of the impending transfer of non-performing loans to the federal states' domain, the Bank has made very large risk provision of some EUR 3 billion before guarantee effects. By far the largest proportion of this concerns the legacy shipping portfolio. After guarantee effects, including the considerable reversal of premiums previously allocated, there was a positive balance for risk provisioning of EUR 304 million. We will continue to keep a very close eye on the remaining risks, which still stem from the legacy shipping portfolio. As was already the case in the preceding years, HSH Nordbank also showed a very solid, 12.3 per cent common equity ratio with its 2015 financial statements. That is testament to the Bank's stability. Total assets dipped – due above all to the planned wind-down in the Restructuring Unit – from EUR 110 to 97 billion.

All told, HSH Nordbank looks back on 2015 as a year that was as challenging as it was successful. The conclusion of the EU state-aid proceedings is a key milestone – and simultaneously the starting point for a new era. We are convinced that HSH Nordbank will be a bank of interest to investors. It has a strong market position, already well-functioning processes on which we continue to work, as well as skilled, motivated employees. Its position in the northern German market is excellent, but it is also present in the rest of Germany. The preconditions for a new owner are consequently favourable, especially given that such a new owner will, in the future, be able to fully develop the Bank's potential, i.e. without the EU Commission-stipulated restrictions that currently constrain our business opportunities.

HSH Nordbank is facing two crucial years that will be characterised by major effort and possibly unpopular decisions. We will do everything we can for a successful change of ownership and are convinced that this will be a step towards a thriving future.

Yours sincerely,



Constantin von Oesterreich
Chairman of the Management Board



Stefan Ermisch
Deputy Chairman of the Management Board



Torsten Temp
*Member of the Management Board,
Shipping Project & Real Estate Finance*



Ulrik Lackschewitz
Chief Risk Officer



Matthias Wittenburg
*Member of the Management Board,
Corporates & Markets*

CONSTANTIN VON OESTERREICH AND STEFAN ERMISCH IN CONVERSATION

START OF A NEW ERA

After more than two years of scrutiny under the state-aid proceedings against HSH Nordbank, the EU Commission gave the green light in October 2015. What does this decision mean for the Bank?

Constantin von Oesterreich: It established clarity and planning certainty, and it sets out unambiguous prospects with the change of ownership targeted for 2018. Everyone – our clients, investors and rating agencies, but also our colleagues – now knows where they stand.

Stefan Ermisch: I regard this change of ownership as a great opportunity. We can now dispose of at least some of our legacy assets and offset this against the existing guarantee. At the same time, the guarantee premiums in the operating part of the Bank will drop from 4 to 2.2 per cent of the unutilised portion of the guarantee. That provides palpable relief for the future.



Are you also satisfied with the details of the EU decision?

Stefan Ermisch: The decision is a political compromise. Although the Bank will be relieved of some of the legacy assets from the years prior to 2009, it will still retain a considerable proportion of such legacy and unhealthy business. That doesn't make it any easier – I'm quite realistic about that, especially so given that the final decision of May 2016 deviates in some parts from the outcome indicated in October 2015 – and rather more so to our detriment.

Waiting for the EU decision entailed uncertainty. What impact did that have on business in 2015?

Constantin von Oesterreich: Clients and investors don't like a lack of clarity. We know that, and felt it. The months preceding the EU decision cost us business. There was a significant increase in the deals closed once we had the green light from Brussels. The fourth quarter was by far the strongest last year. Our Bank must now continue to prevail in the marketplace, and we are well on our way to doing just that. Our 2015 total income exceeded the budget target and we have a good grip on our costs.

Despite these difficult underlying conditions, HSH Nordbank reported a respectable profit for 2015 with pre-tax income amounting to EUR 450 million. How did that come about?

Stefan Ermisch: We see major benefits from the EU decision on our 2015 balance sheet. We previously made substantial provision for future premium payments. Much of that no longer applies, which on balance equated to non-recurring relief of more than EUR 650 million for 2015. Secondly, we generated a solid amount of new business in the Core Bank, with decent margins and better cross-selling. That would not have been possible without the big effort we put in together, and for which I would like to express my sincere thanks to all staff members. The solid capital ratios shown on our balance sheet also reflect how stable our Bank is meanwhile. That's good news. But we must not forget: the result was a positive one thanks only to exceptional factors.

What conclusions do you draw from that?

Stefan Ermisch: We must not rest on our laurels. Standing still would mean the end. It must be our objective to hand over an outstanding base, i.e. a high-performing organisation, to any new owner.

What is especially important about that?

Stefan Ermisch: We have to keep our focus on our capital base and continue to improve our efficiency. Given that competition is fierce right now, we must continue to reduce costs even if that entails cuts. That's painful, but unavoidable. Our Bank furthermore needs – like every other one, too – efficient and resilient processes in both sales and back office operations as well as fast execution. That, in turn, assumes clear, straightforward decision-making channels. We are working on becoming even stronger in operational terms. That is tremendously important because we are now establishing the basis for a new owner to fully release the Bank's potential under what will then be liberated conditions. We are working on the Bank's future success.



The agreement with the EU Commission provides that HSH Nordbank may initially transfer assets worth EUR 5 billion to the states of Hamburg and Schleswig Holstein. How far has this progressed?

Stefan Ermisch: The federal states have established the “hsh portfoliomanagement AöR” company in Kiel to which the assets can be transferred and have met all the other conditions for these transactions. The plan is to transfer the assets in the summer of 2016. This involves NPL portfolios from the Shipping division, which will be transferred at “market value” and charged to the guarantee. Given that there is no liquid market for these severely marred assets, the EU Commission has commissioned an appraiser to establish transfer prices that are neutral with respect to state aid legislation and described these as market prices.

HSH Nordbank may sell further assets worth EUR 3.2 billion at market prices. How far has the planning progressed?

Constantin von Oesterreich: The respective assets have been identified. They stem not only from the Shipping division, but also from others. We have more time to sell those. Our prime objective is to achieve adequate prices. There are investors who are prepared to take a certain amount of risk if they see opportunity for a good return.

How do you rate the prospects for HSH Nordbank’s planned privatisation?

Constantin von Oesterreich: I was always convinced that HSH Nordbank is viable for privatisation. Even though the EU decision did not turn out to be an ideal one for us – our Bank now has an opportunity that it will take.

What about the Shipping division, which has suffered so badly in recent time from ship overcapacity?

Stefan Ermisch: The Shipping division will be liberated from numerous legacy assets by 2018, although they will continue to weigh on the Bank’s result. We estimate an annual loss of about EUR 200 million, which is the price for the comparatively minor relief. This will make the change of ownership more difficult – or it will squeeze the price.

How do you rate the potential of the Bank’s healthy part?

Stefan Ermisch: The healthy part of the Core Bank should have potential for earning about EUR 300 million before taxes. In the long term, the Bank’s new owners will be able to expand the Bank’s strengths further, also because they – unlike HSH right now – will not be subject to any business restrictions. All told, HSH Nordbank is set up in a smart and balanced way. It has a strong market position, well-functioning processes and employees who are as skilled as they are motivated. This is a promising combination for investors. The Bank commands a very good position in northern Germany and is also represented in the rest of the country. Particularly the metropolitan region around Hamburg is very strong economically. The Bank has an excellent market position in its Real Estate Clients, Energy & Utilities as well as Corporate Clients divisions. With our Capital Markets, Wealth Management and Transaction Banking divisions, we support our client-related activity in a prudent manner.

Who would be a potential buyer for HSH Nordbank?

Stefan Ermisch: First, the important thing is that creative solutions are called for and that’s why I think much is conceivable: starting with the involvement of a strategic investor, then the possibility of an IPO and through to another Landesbank, which wants to extend or round off its business, buying a stake. Besides, it should be remembered that the states of Hamburg and Schleswig-Holstein might, even after 2018, continue to hold stakes of up to 25 per cent in the Bank for another four years.