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ISSUER COMMENT

HSH Nordbank's Significant De-risking Progress Is Credit Positive

From Credit Outlook

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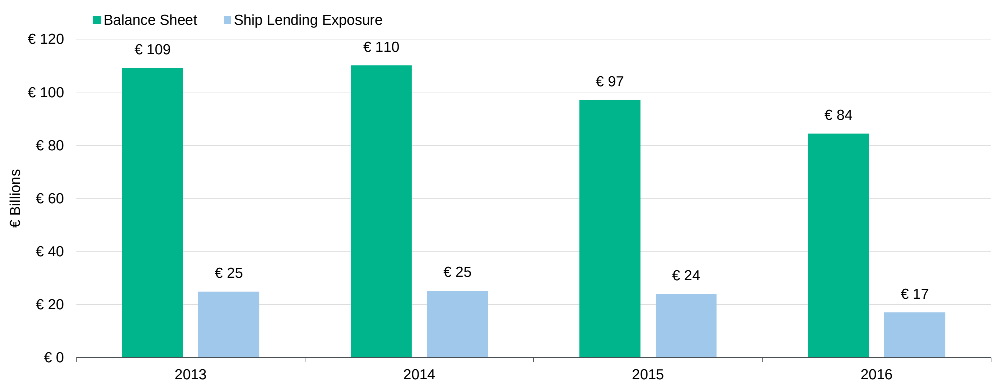
Last Thursday, German Landesbank and leading ship lender HSH Nordbank AG (Baa3/Baa3 developing, b3[1]) published year-end 2016 results that showed a reduction in non-core assets and a net increase in risk provisions on its large impaired ship finance portfolio. HSH's continued de-risking strategy is credit positive for the troubled ship lender, reducing threats from loan losses to its improved risk-weighted capitalization, as reflected in the bank's improved common equity Tier 1 ratio to 14.1% from 12.3% as of December 2015. Additionally, these efforts will make the bank more attractive to potential buyers in a privatization process as HSH tries to avoid an imposed wind-down and adverse effects on asset recoveries.[2]

As Exhibit 1 shows, HSH last year reduced its balance sheet by €12.6 billion to €84.4 billion, predominantly by reducing its shipping book to €17.0 billion from €23.9 billion at year-end 2015. The disposals of non-core assets and maturities of legacy assets largely drove this reduction. The shipping segment benefitted from the sale of €5.0 billion of nonperforming loans at a 52% haircut to hsh portfoliomanagement AoR (Aa1 stable). HSH plans to sell another €3.2 billion of nonperforming loans to the market in 2017, €1.6 billion of which it sold in January. We expect HSH to fully utilize its €10 billion credit guarantee in 2017. In 2016, the available headroom under the guarantee for additional risk charges fell by €1.8 billion to €100 million, with €900 million of the reduction of taking place in the fourth quarter.

EXHIBIT 1

HSH Nordbank Has Reduced Its Credit-Risky Shipping Exposure, € Billions



Note: Balance sheet size is measured in total assets; ship lending exposure is measured in exposure at default.
Sources: HSH Nordbank and Moody's Investors Service

What is Moody's Credit Outlook?

Published every Monday and Thursday morning, Moody's Credit Outlook informs our research clients of the credit implications of current events.

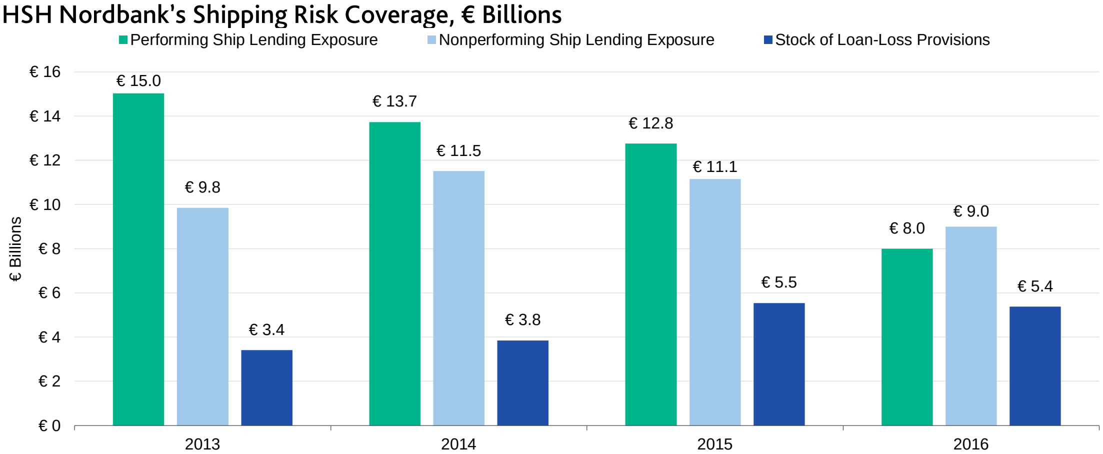
THIS REPORT WAS REPUBLISHED ON 6 APRIL 2017 TO CORRECT THE TIMING OF THE SALE MENTIONED IN THE SECOND PARAGRAPH.

1 The bank ratings shown in this report are HSH's deposit rating, senior unsecured debt rating and baseline credit assessment.
2 In January, HSH's public-sector owners formally announced the start of HSH's privatization process. In accordance with the European Commission's 2016 state-aid decision, the German states of Hamburg and Schleswig-Holstein intend to sell at least 75% of their shares in HSH in an open, transparent and competitive bidding process. The owners are allowed to retain up to 25% of their shares in HSH for up to four years after the sale's completion.

HSH's overall nonperforming exposure ratio decreased to 17.5% in 2016 from 18.8% in 2015, while within its shipping portfolio the ratio rose to 52.9% from 46.4%. At the same time, HSH's nonperforming exposure coverage ratio improved significantly, both for its entire portfolio and its shipping exposures (see Exhibit 2). The bank charged €1.6 billion of loan-loss provisions in 2016, materially lower than €3.0 billion in 2015 but sufficient to increase the coverage ratio to 60% in shipping, which is near the top of the 20%-64% range reported by German ship lenders thus far for 2016.

EXHIBIT 2

HSH Nordbank's Shipping Risk Coverage, € Billions



Sources: HSH Nordbank and Moody's Investors Service

We maintain that HSH's large underperforming legacy assets must be sold separately to ensure that the entity can change hands because the bank in its current shape will not be able to compete successfully as a private bank. In light of the ongoing challenges on shipping loans, the improved coverage ratios on the bank's nonperforming shipping assets increase HSH's chances of selling its legacy assets.

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